

INDIA IS NOW AHEAD OF CHINA IN FINANCIAL INCLUSION METRICS: HOWEVER IT IS IMPORTANT TO FINE-TUNE NON BRANCH BC MODELS

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Sound financial inclusion policies have a multiplier effect on economic growth, reducing poverty and income inequality, while also being conducive for financial stability. India has stolen a march in financial inclusion with the initiation of PMJDY accounts since 2014, enabled by a robust digital infrastructure and also careful recalibration of bank branches and thereby using the BC model judiciously for furthering financial inclusion. Such financial inclusion has also been enabled by use of digital payments as between 2015 and 2020, mobile and internet banking transactions per 1,000 adults have increased to 13,615 in 2019 from 183 in 2015. The number of bank branches per 100,000 adults rose to 14.7 in 2020 from 13.6 in 2015, which is higher than Germany, China and South Africa. Our research also shows that states with higher PMJDY accounts balances have seen a perceptible decline in crime. We also observed that there is both statistically significant and economically meaningful drop in consumption of intoxicants such as alcohol and tobacco products in states where more PMJDY accounts are opened.

The Banking Correspondent (BC) model in India is enabled to provide a defined range of banking services at low cost and hence is instrumental in promoting financial inclusion. Interestingly, the new branch authorisation policy of 2017 – which recognises BCs that provide banking services for a minimum of 4-hours per day and for at least 5-days a week as banking outlets has progressively obviated the need to set up brick and mortar branches. For example, the number of ‘Banking Outlets in Villages - BCs’ has risen from 34,174 in Mar’10 to 12.4 lakh in Dec’20. Such progress shows an impressive outreach of banking services through branchless banking.

However, the success of financial inclusion depends upon BCs who are micro-level entrepreneurs. As per RBI guidelines, under the BC Model, while a BC can work for more than one bank, at the point of customer interface, a retail outlet or a sub-agent of a BC shall represent and provide banking services of only one bank. Interoperability of transactions is permitted by RBI at the retail outlets or sub-agents of BCs (i.e. at the point of customer interface), subject to certain conditions. Herein lies the problem.

It is sometimes observed that there is no uniformity among the BCs across banks regarding adherence to the above guidelines. PSBs mostly follow ‘Branch Led BC Model’, while other banks follow ‘Branch Less/Corporate BC model’. The BCs of PSBs extend basic banking services, including opening of accounts, from a fixed location under the oversight of specific bank branch. The BCs of other banks operate through ‘Micro ATM/Kiosk Application on Mobile’ and primarily provide fee-based financial services, viz. withdrawals and remittance services, using hand-held devices. This also adds to the bottom-line by way of interchange fee from the PSBs or remittance fee from PSB customers. As a typical example, BCs convert AePS ON-US transactions of one set of bank customers, to AePS OFF-US issuer transactions and also carry out multiple AePS ON-US and AePS OFF-US transactions on the primary bank application/software. Data indicates that the share of OFF-US transactions in AePS increased from 4% in Sep-16 to 51% in Sep-21. Considering these facts, PSBs (who opened around 77% of the PMJDY accounts) are now net payers of interchange fee. We estimate that the PSBs could be paying around Rs 600-700 crore per annum as interchange fee.

We make the following recommendations to make the BC model more rigorous and uniform across all banking entities.

Firstly, we recommend that as AePS works like a Point of Sales (PoS), logically the ‘acquiring bank’ should pay the interchange fee to the ‘issuing bank’. Alternatively, there could be rationalisation in interchange fee as there is no level playing field in infrastructure provided by all banks. With requisite savings, banks can further strengthen/upgrade their BC model and promote financial inclusion in a more holistic manner.

Secondly, we recommend RBI to disincentivise BCs who are converting the ON US transactions of PSB customers to AePS OFF US transaction in order to earn interchange fee and more commission. For this, we propose that a comprehensive database of BC agents be prepared through IBA’s BC registry, JanDhan Dharshak App and RBI’s CISBI portal. Additionally, we also propose that the log-in to the AEPS applications of the non branch BC model must be through Aadhaar authentication. This will prevent anyone from logging and performing unverified transactions. This will also results in BCs their friends and relatives not being able to game the system by opening accounts with multiple banks and performing round tripping/ withdrawals.

Indian economy is at the cusp of becoming a more efficient and formal one. We strongly believe some minor tweaks in the existing branch less BC model could act as a multiplier for promoting financial inclusion objectives. This is all the more important as we are currently formalising 34.7 crores of informal labour force through the E-Shram portal.

FINANCIAL INCLUSION: PROGRESS SO FAR

- ◆ Sound financial inclusion policies have a multiplier effect on economic growth, reducing poverty and income inequality, while also being conducive for financial stability. The Financial Access Survey data of the IMF show that various initiatives taken by RBI and the Government in the direction of financial inclusion are bearing fruit. The number of bank branches per 100,000 adults rose to 14.7 in 2020 from 13.6 in 2015, which is higher than Germany, China and South Africa.
- ◆ With strong Government push to increase bank account among unbanked adults through Pradhan Mantri Jan Dhan Yojana (PMJDY), the number of persons with deposit accounts at banks has significantly increased, becoming comparable with emerging economy peers and even some of the advanced economies. In terms of use of digital payments too, India has made noteworthy progress. Between 2015 and 2020, the number of mobile and internet banking transactions per 1,000 adults has increased to 13,615 in 2019 from 183 in 2015.

FINANCIAL INCLUSION MODELS IN INDIA

- ◆ Traditionally, Indian banks have favoured expanding their brick-and-mortar branches to reach the unbanked population in remote and unbanked villages. However, it was difficult for the banks to open such branches in each and every village. So, RBI had designated Business Correspondent (BC) models from January, 2006 to provide an alternative banking channel to millions by making financial services accessible for the un-/underbanked population through a branchless banking facility but also supporting the national agenda for employment generation.
- ◆ The corporate BCs (also known as the BC network managers) act as a conduit and distribute the banking products with the help of multiple Customer Service Points (CSPs) commonly referred as agents or Bank Mitras. Accordingly, individuals such as Retired Teachers, Bank and Government employees, Ex-Service men, Individual Shop Owners, Petrol Pump Owners and other individuals qualified up to secondary level (10th Standard) can act as conduits in BC model. **The BCs are enabled to provide a defined range of banking services at low cost and hence are instrumental in promoting financial inclusion.** Every BC is required to be attached to and overseen by a designated bank operating in its general vicinity.

Benefits of Financial Inclusion		
Indicator	2015	2020
Number of commercial bank branches per 100,000 adults	13.5	14.7
Number of deposit accounts with commercial banks per 1,000 adults	1536	2031
Number of loan accounts with commercial banks per 1,000 adults	154	267
No. of mobile and internet banking transaction per 1,000 adults	183	13615

Source: Financial Access Survey

- ◆ Interestingly, **the new branch authorisation policy of 2017** – which recognises BCs that provide banking services for a minimum of 4-hours per day and for at least 5-days a week as banking outlets – coupled with emphasis on digitisation and modernisation of technological **infrastructure has progressively obviated the need to set up brick and mortar branches.** As has been observed for the last few years, during 2019-20 also, branch expansion in rural areas remained subdued as BC model made further inroads in villages with population more than 2,000.
- ◆ The BC model has now gained popularity even in urban areas. Based on experience gained during the COVID-19 pandemic, the BC model is likely to strengthen further as physical access to banks is constrained by social distancing. The BC model has also been instrumental in giving a push to PMJDY scheme.
- ◆ In the last seven years of launch of PMJDY scheme, the total number of accounts opened under PMJDY has reached 43.7 crore, with ₹1.46 lakh crore of deposits as on October 20, 2021. Of these accounts, nearly two-third are operational in rural and semi-urban areas. More than 78% of PMJDY accounts were with PSBs and 18.2% are of RRBs, while non-PSBs’ share is 3%.
- ◆ As per the latest available data on the number of bank branches in rural areas shows an increase from 33,378 in Mar’10 to 55,073 in Dec’20; **while the number of ‘Banking Outlets in Villages - BCs’ has risen from 34,174 in Mar’10 to 12.4 lakh in Dec’20.** Such progress shows an impressive outreach of banking services through branchless banking.

Financial Inclusion Plan					
Particulars	Mar-10	Mar-19	Mar-20	Y-o-Y Grth FY20	Dec-20
Banking Outlets in Villages- Branches	33,378	52,489	54,561	3.9	55,073
Banking Outlets in Villages>2000-BCs	8,390	1,30,687	1,49,106	14.1	8,51,272
Banking Outlets in Villages<2000-BCs	25,784	4,10,442	3,92,069	-4.5	3,85,537
Total Banking Outlets in Villages – BCs	34,174	5,41,129	5,41,175	0.0	12,36,809 [^]
Banking Outlets in Villages – Total	67,694	5,97,155	5,99,217	0.3	12,95,322
Urban Locations Covered Through BCs	447	4,47,170	6,35,046	42.0	3,24,345

Source: RBI; SBI Research; [^]: Significant increase in numbers is due to reclassification done by a bank

THE CHALLENGES WITH THE EXISTING MODEL

- ◆ The success of financial inclusion depends upon the success of the BCs who are micro-level entrepreneurs. As per RBI guidelines, under the BC Model, while a BC can be a BC for more than one bank, at the point of customer interface, a retail outlet or a sub-agent of a BC shall represent and provide banking services of only one bank. Interoperability of transactions was permitted by RBI at the retail outlets or sub-agents of BCs (i.e. at the point of customer interface), subject to certain conditions.
- ◆ However, it is sometimes observed that there is no uniformity among the BCs across banks regarding adherence to the above guidelines. PSBs mostly follow ‘Branch Led BC Model’, while other banks follow ‘Branch Less/Corporate BC model’. The BCs of PSBs are extending all the basic banking services, including opening of accounts, from a fixed location under the oversight of specific bank branch. **As per estimates, Rs 1.0-1.5 lakh capital expenditure is required to set-up a Kiosk under Bank led BC model.**
- ◆ The BCs of other banks operate through ‘Micro ATM/Kiosk Application on Mobile’ and primarily provide fee-based financial services, viz. withdrawals and remittance services, using hand-held devices. This also adds to the bottom-line by way of interchange fee from the PSBs or remittance fee from PSB customers. **The capex of other banks BC model in ‘Micro ATM/Kiosk Application on Mobile’ is around Rs 30,000 or less.**
- ◆ The interchange fee received from the PSBs for AePS (Off-US Acquirer) transactions are significant as almost 51% transactions are OFF-US. The PSBs at the same time pay fixed minimum remuneration to rural CSPs in addition to activity/transaction based incentives.
- ◆ PSBs, who are active in Financial Inclusion activities, have opened large number of PMJDY accounts (out of 44 crore accounts, PSBs opened 34 crore accounts and non-PSBs: 1.3 crore, rest RRBs) with minimal balance and thus incur recurring expenditure by way of servicing such customers including issuance of Free RuPay Debit Card, besides monthly remuneration for BC operations.
- ◆ Further, the BCs who are already engaged with say one set of banks as CSP either in their name or in the name of their relatives, that is not as per the requisite guidelines of RBI. Additionally, such BCS convert AePS ON-US transactions of one set of bank customers, to AePS OFF-US issuer transactions and also carry out multiple AePS ON-US and AePS OFF-US transactions on the primary bank application/software.
- ◆ The ‘Micro ATM/Kiosk Application on Mobile’ model might also lead to several fraud, as the mobile BCs introduce themselves as Government persons and need biometric authentication to provide different type of subsidy.

AePS Statistics (in Million)				
Month	Total Transactions	of which, Off-us	On-us	Off-us to Total
Sep-21	344	176	166	51%
Sep-20	298	144	153	48%
Sep-19	191	67	123	35%
Sep-18	138	42	95	31%
Sep-17	82	16	66	19%
Sep-16	24	1	23	4%

Source: NPCI; SBI Research

PMJDY Accounts & BCs of PSBs and non-PSBs			
Bank	PMJDY A/Cs (in Lakh)	Total BCs (Actual) in lakh	A/Cs per BC
Major 5 PSBs	2612	1.3	1994
Major 5 non-PSBs	49	11.0	4

Source: PMJDY; SBI Research; as of 13.10.2021

POSSIBLE SOLUTIONS FOR A LEVEL PLAYING FIELD

In order to ensure a level playing field in the BC model, we recommend the following:

- ◆ **Rationalisation of Interchange Fee:** The account opening bank pays an interchange fee to the operator of the BC/CSP when a customer makes a transaction at micro-ATM that does not belong to the account opening bank (i.e. OFF-US transaction). At present the interchange fee is 0.5% of transaction amount (min Re 1 and max Rs 15) for an OFF-US financial transaction and Rs 5-7 for non-financial transaction.
- ◆ Three facts in this regard are quite evident: (i) more than 77% PMJDY accounts have been opened by PSBs, (ii) the number of BCs/CSPs of other banks largely outnumbered the PSBs, (iii) Over the years the OFF-US transactions are increasing. Data indicate that the share of OFF-US transactions in AePS increased from 4% in Sep-16 to 51% in Sep-21. Considering these facts, PSBs (who opened around 77% of the PMJDY accounts) are now net payers of interchange fee. **We therefore recommend a rationalisation in interchange fee as there is no level playing field in infrastructure provided by all banks.**
- ◆ **Interchange Fee to be paid to the Issuing Bank:** As AePS works like a Point of Sales (PoS), logically the ‘acquiring bank’ should pay the interchange fee to the ‘issuing bank’.
- ◆ **Disincentivise BCs for Unfair Business Activities to Generate Commission:** We request RBI to disincentivise BCs/CSPs who are converting the ON US transactions of PSB customers to AePS OFF US transaction in order to earn interchange fee and more commission.

SIGNIFICANT BENEFITS OF FINANCIAL INCLUSION

- ◆ In India, over the years crimes has been increasing. In 2020, a total of 66 lakh cognizable crimes comprising 42.5 lakh IPC crimes and 23.4 Special & Local Laws (SLL) crimes were registered, with an increase of 30% in registration of cases over 2018. Crime rate registered per lakh population has increased marginally from 383.5 in 2018 (385.5 in 2019) to 487.8 in 2020. Crimes against women and children has increased by 7.3% in 2018 and 4.5% in 2019, however, there is a decline of 8.3% in 2020.
- ◆ To see the impact of Jan Dhan accounts on crimes, we looked at the state wise data accounts level data of PMJDY both ‘No of accounts’ and ‘Balance’ and mapped with the state ‘number of total crimes’ from 2016 to 2020.

- ◆ As crime data is available till 2020, so we had taken into account 37-states & UTs (including India) and 5-years data (2016-2020) to build a panel data model as : $CRIME = C + \alpha PMJDY\ Accounts + \beta PMJDY\ A/C\ Balance + \mu$. The estimated results indicate that with the rise in number of PMJDY accounts and balance in these accounts leads to a significant fall in crime.
- ◆ We also observed that there is both statistically significant and economically meaningful drop in consumption of intoxicants such as alcohol and tobacco products in states where more PMJDY accounts opened. This could be because of Jan Dhan-Aadhaar-Mobile (JAM) Trinity which has helped in better channelizing of Government subsidies and helped in curbing the unproductive expenditure such as alcohol and tobacco expenses in rural areas.

Some examples of inefficiency of current non branch BC model	
Multi-Level Marketing (MLM)	<ul style="list-style-type: none"> • The Corporate BCs (CBCs) adopt MLM techniques for deploying retail agents
Agents not monitored	<ul style="list-style-type: none"> • The retail agents are not linked to any of the Bank branch for monitoring which is in violation of RBI guidelines
No Data of Agents	<ul style="list-style-type: none"> • IBA's BC registry, JanDhan Dharshak App and RBI's CISBI portal does not have the data. In case of failure of transaction(s), customer(s) fall back on the issuer Bank (Mostly PSBs). This also results in agents, their friends and relatives open accounts with multiple banks and perform round tripping/ withdrawals.
Collection of extra charge from customers	<ul style="list-style-type: none"> • BCs are resorting to collection of additional charges from customers by debiting Rs.10 or more along with the transaction amount such as Rs 1010, Rs 1020 etc. which can not be tracked / monitored.
Agents indulging in frauds	<ul style="list-style-type: none"> • The log-in to the AEPS applications of the non branch BC model are not through Aadhaar authentication. Hence anybody can log in and perform transaction.
Rationalising Agent Incentive Schemes	<ul style="list-style-type: none"> • Many Corporate BCs have incentive schemes to lure agents to increase the number of transactions and that too in the range of Rs 3000 to Rs 3500.
Transactions	<ul style="list-style-type: none"> • Interchange fee is 0.50% on the transaction amount (min Rs 1 and max Rs 15). But the agents are paid in fixed values and the commission amount is tapered for txns above a specified threshold. This typically boost the number of transactions and maximises interchange fee.
Splitting through application	<ul style="list-style-type: none"> • Transactions get split through applications within a minimal time.

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