

Policy Brief # 1

Electronic and Mobile Banking in India: Gearing-up for Growth

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Financial inclusion has witnessed extraordinary investments and efforts from a variety of stakeholders in India over the past two years. The central bank ([RBI](#)), the Ministries of Finance and of Rural Development ([MoF](#) and [MoRD](#)) have undertaken numerous reforms and measures¹ to make the policy and regulatory climate more conducive for the banks, agent network managers, agents and for the customers. Though setting stringent targets for financial inclusion, and constantly pushing banks to achieve those, has been the prime emphasis of Government, recent moves to increase the digitisation of subsidies may prove to be more effective. Nonetheless, the high levels of account² (and increasingly agent³) dormancy as a consequence of this regulation-driven approach has drawn significant criticism.⁴ There is however, a need to step back and objectively assess several vital measures that have been undertaken in recent times, together with the announcements in the 2012 budget speech, and the impact thereof.

The Finance Minister in his [budget speech](#) on March 16, 2012, has made some vital announcements, and articulated certain elements of Governmental intent for the next few years, that would have a radical impact on accelerating the growth of branchless-banking and moving towards a cash-lite economy.

1. **Direct Transfer of Subsidies:** The Government intends to ensure targeted and leakage proof distribution of subsidies. Making distribution of subsidies efficient would achieve the twin objectives of increasing the quantum delivered to the (real) recipients, while bringing down the overall central Government's expenditure on subsidies to 2.0% of GDP in 2012-13 and further to 1.75% of the GDP in the next three years. In value terms this would translate to US\$40 billion worth of subsidies in 2012 and going up to US\$42 billion by 2014. The recommendations of the Nandan Nilekani (Chairman UIDAI) task force on IT strategy for direct transfer of subsidies have been accepted. Basis this, a mobile-based fertiliser management system for efficient tracking of movement of fertilisers would be implemented during 2012 and extended to direct distribution of fertiliser subsidies to farmers in subsequent years, benefiting 120 million farmers. A pilot project for transfer of subsidy on kerosene (a major component of petroleum subsidy) directly into the bank accounts of beneficiaries is running successfully at Alwar (state of Rajasthan). A similar one based on UIDAI *Aadhaar* to authenticate recipients of food subsidy is running successfully in the state of Jharkhand. Another pilot for transfer of subsidies on cooking fuel (LPG, another large component of subsidies on fuel) into beneficiary bank accounts is being considered in Mysore (state of Karnataka). Banks through the BC channel are likely to take on most of the responsibility for management of subsidy funds.
2. **Acceptance and Strengthening of UIDAI:** After the Prime Minister's intervention in resolution of a conflict between UIDAI and National Population Register (under ministry of home affairs) in February 2012, where UIDAI's mandate was extended to enrol 600 million Indians, the budget has further strengthened UIDAI, announcing a number of measures. Firstly, adequate funds have been allocated in the budget to enable UIDAI achieve registration of the remaining 400 million population. Secondly, *Aadhaar* is being viewed as trusted platform to enable achieve economies and efficiency in distribution of subsidies. Thirdly, *Aadhaar* has now been accepted as ready to deliver direct Government payments under various schemes, including MGNREGA (employment guarantee), various pension programs (SSP) and scholarships. As a result the *Aadhaar* enables payment system ([AEPS from NPCI](#)) for various G2P schemes would be extended to at least 50 selected districts (out of a total of 640) within the next 6 months. Despite fiscal and budgetary pressures on the

¹ See *MicroSave* India Focus Note 83, [Financial Inclusion through E/M Banking – The Regulatory Landscape in India](#)

² See *MicroSave* Research Study on [Dormancy in No Frills Accounts, 2011](#)

³ See *MicroSave* forthcoming paper on the Rapid Agent Assessments and Agent Journals studies

⁴ The Economic Times Article: [Opened 80 million, working 15 million, February 2012](#)

government, the 2012/13 budget allocation for *Aadhaar* was increased from the previous year's US\$290 million to US\$352 million – a remarkable change from 6 months ago when there was credible talk of slashing the UIDAI's budget by 50%.

3. **Mainstreaming Rural Banking:** The push towards moving Regional Rural Banks, who are primarily serving the low-income group, onto online core banking system (CBS), has yielded results and 81 out of a total of 82 RRBs have migrated to online CBS and integrated to the National Electronic Fund Transfer ([NEFT](#)) system. Along with the regulation on interoperability of BC agents, this would be a significant enabler for extending RRB banking products through BCs to the rural residents. Domestic migrant remittances would also get a further boost and an opportunity to move from informal channels to banks. With RRBs connected to the NEFT network, the direct distribution of subsidies would also become operationally more feasible, as the outreach of RRBs along with their BC network would be considerably more than what scheduled commercial banks alone could offer.
4. **Increasing G2P Payments:** The outlays for various G2P programmes have been increased considerably. About 25% to 45% of these are delivered through banking channel and this is expected to increase further.
 - a. **Social Security Pensions:** An overall 37% increase to US\$1.7 billion. 50% increase in pension amounts per beneficiary under widow and disability pension programs.
 - b. **National Rural Livelihood Mission (NRLM):** An overall increase of 34% to US\$0.8 billion.
 - c. **National Rural Health Mission (NRHM):** An increase of 20% to US\$4.2 billion. The health workers (ASHA workers) are paid through this program and BCs like Eko are successfully running electronic salary distribution for them in parts of state of Bihar.

MicroSave has long argued that India's path to significantly enhanced financial inclusion, though rocky and at times tortured and tortuous, is well set.⁵ Over the last 6 months, there have many other announcements on policies and guidelines that accelerate the pace of reforms around financial inclusion. Some of the major ones along with their likely impact are discussed below.⁶

#	Policy / Directive / Other Measures	When Announced	Key Features	Impact
1	RBI circular on Interoperability of banking services at agents/retail outlets	March 2012	<ol style="list-style-type: none"> 1. Allows transaction acquisition for any bank by a BC agent / customer service point, provided authentication and transactions are online and supported by banks' technology. 2. Advises Indian Bank's Association (IBA) to develop standard operating procedures that might include amongst others, revenue sharing, as it exists for interoperable ATMs. 	<ol style="list-style-type: none"> 1. Meets a major expectation from agent network managers (ANMs), helping agents get scale, would enhance level of competition and would prevent arbitrage caused due to tariff differential across banks.⁷ 2. Provides legitimacy to surreptitious interoperable practices followed by agents, as there was considerable consumer demand. 3. Urban migrants would benefit by getting greater choice and enhanced access to agent outlets.⁸ 4. Recipients of Government payments in rural areas are likely to get better access to agents, provided BCs are willing and capable of offering interoperability. Initially likely to be adopted mobile and internet based

⁵ See *MicroSave's* paper [Why E/M-Banking Will Soon Reach Scale in India](#)

⁶ See *MicroSave* India Focus Note 83 [Financial Inclusion through E/M-Banking - The Regulatory Landscape in India](#) for an overview and discussion of previous regulatory provisions.

⁷ See *MicroSave* India Focus Note 90 [Taking Financial Inclusion to the Next Level](#) and 80, [Driving Viability for Banks and Business Correspondents](#)

⁸ See *MicroSave* Research Studies on [Understanding Domestic Remittance, 2011](#)

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				BCs. 5. Sets stage for enabling Aadhaar (UIDAI) based central authentication for 'off us' transactions.
2	MoRD – Recommendations of Mihir Shah Committee Report on MGNREGA	March 2012	<ol style="list-style-type: none"> 1. Recommends setting-up an electronic fund management system (eFMS) at state level to optimise and speed-up fund distribution across. 2. Recommends mandatory wage payout when work cannot be allotted within 15 days of demand. 3. Recommends measures to reduce delays in payments. 	<ol style="list-style-type: none"> 1. Seeks greater transparency in creation, allocation and payment for work. Initiatives like common state fund, managed electronically pushes for greater reliance on banks for managing MGNREGA corpus and distribution. 2. Thrust on MIS and emphasis on accountability for timely wage distribution through electronic means and cash.
3	MoF – Report of the task force on UIDAI Aadhaar enabled Unified Payment Infrastructure	February 2012	<ol style="list-style-type: none"> 1. Interoperable network of BCs, Banks and India Post. 2. Recommends Government to bear a last mile processing fee of 3.14% (with a cap of Rs. 20 per transaction) and distribution between acquiring bank (64%), issuing bank (31%) and switch (5%). 3. Proposes direct transfer of subsidy (DTS) and EBT to recipients through <i>Aadhaar</i> enabled accounts. 4. Recommends ways for linking existing bank and post office accounts to <i>Aadhaar</i> number. 5. Recommends quicker adoption of mobile banking. 	<ol style="list-style-type: none"> 1. The task force had Secretary -level representation from Ministries of finance, agriculture, rural development, fertilisers, public distribution, petroleum and expenditure, and from UIDAI, IBA, RBI, NPCI etc. It comprehensively represented all stakeholders and decision implementers. 2. Recommendation, if accepted would enable a quantum jump in moving towards a cash-lite system, recognising the challenges and recommending steps to address them. 3. Recognises the need for greater coherence across Government departments, banks and India post to leverage a common interoperable infrastructure based NPCI and enabled through <i>Aadhaar</i>. 4. Recognises duplication of accounts for various purposes and recommends convergence into a single account. 5. Recognises the need for savings and recommends for payments to be held in accounts rather than State mandate for immediate disbursement, subject to adequate coverage and service levels by BCs.⁹ 6. Recommends transaction based¹⁰ payout from Government rather than enrolment or fixed-fee based, to incentivise usage of electronic channels by banks, BCs and India

⁹ See *MicroSave* India Focus Note 90, [Taking Financial Inclusion to The Next Level](#)

¹⁰ See *MicroSave* Research Paper, [Cost and Willingness to Pay, 2011](#)

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				post. 7. Recommendations on unification and simplification of processes for G2P, if adopted, can be very effective in adoption and scaling-up.
4	RBI draft guidelines on white label ATMs	February 2012	Thrust on expansion of ATM network beyond metros and tier-I/II towns, by allowing non-banks to set-up and operate them.	<ol style="list-style-type: none"> 1. A non-banking entity with a minimum net-worth can set-up and operate ATMs as white label ATM (WLA) operator and become acquirer of transactions for all banks. They can earn revenue from 'interchange fee', payable to an acquirer bank and from advertisements. 2. The operator would need to ensure a minimum ratio of ATMs in tier-I/II vs tier-III/IV towns as per RBI's directions.
5	RBI letter for accelerating opening of UIDAI Aadhaar enables bank accounts (AEBA)	November 2011	Advises banks to accelerate opening of <i>Aadhaar</i> enables bank accounts, including for villages with less than 2000 population, for EBT payments and direct distribution of subsidies.	<ol style="list-style-type: none"> 1. Emphasizes the greater thrust on opening new bank accounts that are <i>Aadhaar</i> enabled. 2. Precursor to the gradual migration of welfare payments and subsidies to direct payout into bank accounts with <i>Aadhaar</i> based authentication.
6	RBI circular on relaxations on domestic-money transfer	October 2011	<ol style="list-style-type: none"> 1. Liberalises transaction limits and monthly caps for receipt or withdrawal from a bank account and a non account holder (sender or recipient). 2. Enables fund transfers between domestic debit/credit/pre-paid cards, subject to a cap. 	<ol style="list-style-type: none"> 1. Opens debit and credit cards, and pre-paid instruments for transfer of funds, going beyond payment for goods and services and cash withdrawal at ATMs. 2. Enables considerable ease in transfer of small value funds between bank accounts, debit and credit cards, and open/semi-closed pre-paid instruments. 3. Gives a boost to migrants trying to use banking channel to remit money within India.¹¹
7	RBI - KYC norms – Letter from UIDAI with Aadhaar details	September 2011	UIDAI letter with <i>Aadhaar</i> details accepted as KYC proof, without limitation for 'small accounts'.	<ol style="list-style-type: none"> 1. UIDAI letter with name, address and <i>Aadhaar</i> number can now be treated as a valid document for KYC purposes, with further verification of customer's current address left to the discretion of banks. 2. The same has also been extended to KYC norms for NBFCs/RNBCs from December 2011.

¹¹ ibid

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8	RBI guidelines on implementation of EBT and convergence with FIP	August 2011	<ol style="list-style-type: none"> 1. Attempts to realign the distribution of villages to banks for financial inclusion plan (FIP, under service area approach) and for EBT (under ‘one district – one bank’ approach) that caused multiple agencies approaching same rural clients for different services, without the mandate or flexibility to provide full basket of banking services to anyone. 2. Introduces ‘one district – many banks – one lead bank’ model for EBT, allowing flexibility to banks to offer more than just EBT services. 	<ol style="list-style-type: none"> 1. Enables market forces to determine bank’s expansion plans rather than artificial allocation of territories that might be sub-optimal.¹² 2. Would enable banks to optimise their investments by allowing them to offer a wider range of banking services according to their reach and market potential. 3. Tries to address the sub-optimal use of EBT accounts by State Governments, recommending their wider usage for banking services. 4. Introduces greater choice for customers instead of tying them down to one assigned bank.

¹² ibid