Inclusive Finance India Report 2018

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List of Abbreviations

ABAL	Asset Backed Agri Loan
ABBA	Aadhaar-Based Biometric Authentication
ABC	Agent Business Correspondent
ADB	Asian Development Bank
ADBI	Asian Development Bank Institute
ADEPT	Automated Data Extraction
AEPS	Aadhaar-Enabled Payments System
AFI	Alliance for Financial Inclusion
AI	Artificial Intelligence
AIBEA	All India Bank Employees Association
AMFI	Association of Mutual Funds in India
AML	Anti Money Laundering
ANBC	Adjusted Net Bank Credit
AP crisis	Andhra Pradesh Crisis
APBS	Aadhaar Payment Bridge System
APGVB	Andhra Pradesh Grameen Vikas Bank
API	Application Programming Interface
APL	Above Poverty Line
APMAS	Andhra Pradesh Mahila Abhivruddhi Samiti
APY	Atal Pension Yojana
ASPIRE Fund	A Scheme for Promotion of Innovation, Rural Industry and Entrepreneurship
ATM	Automated Teller Machines
AUA	Authentication User Agencies
AUM	Assets Under Management
B&DC	Business And Development Correspondent
B&DF	Business and Development Facilitator
B2B	Business to Business
B2C	Business to Consumer
BBPS	Bharat Bill Payment Services
BSBDA	Basic Savings Bank Deposit Account
BC-MFI	Business Correspondent-Microfinance Institution
BC	Business Correspondents
BCA	BC Agent
BCA	Business Correspondent Agent
BCFI	Business Correspondent Federation of India
BCNM	Business Correspondent Network Manager
BF	Business Facilitator
BFIL	Bharat Financial Inclusion Ltd
BFSI	Banking, Financial Services and Insurance
BHIM	Bharat Interface for Money
BIRD	Bankers Institute of Rural Development
BOP	Bottom of the Pyramid?
BPL	Below Poverty Line
BRLPS	Bihar Livelihoods Promotion Society
BSDA	Basic Savings Deposit Accounts
BTDP	Bihar Targeted Development Programme
C-PEC	Centre for Professional Excellence in Cooperatives
CA Grameen	CreditAccess Grameen

CAGR	Compound Annual Growth Rate
CASA	Current Account Savings Accounts
CBC	Corporate Business Correspondent
CBCNM	Corporate Business Correspondent Network Manager
CBS	Core Banking Solution
CCC	Certified Credit Counsellors
CCC4CCC	Certified Credit Counsellors for Credible Credit Connect
CCI	Competition Commission of India
CD	Certificate of Deposit
CDF	Cooperative Development Fund
CDG	Chandigarh
CDOT	Center for Development Orientation and Training
CEOBE	Credit Equivalent Amount of Off-Balance-Sheet Exposure
CERSAL/CERSAI	Central Registry of Securitisation Asset Reconstruction and Security Interest of India
CFI	Centre for Financial Inclusion
CFL	Centre for Financial Literacy
CFT	Cluster Facilitation Team
CGAP	Consultative Group to Assist the Poor
CGFMU	Credit Guarantee Fund for Micro Units
CGS	Credit Guarantee Scheme
CGTMSE	Credit Guarantee Trust Fund for Micro and Small Enterprises
CHC	Custom Hiring Centre
CIC	Credit Information Company
CIF	Community Investment Funds
CKYCR	The Central KYC Records Registry
CLF	Cluster-Level Federation
CMRC	Community Managed Resource Centre
COF	Cost Of Funds
CoR	Certificate of Registration
CPR	Community Resource Person
CRAR	Capital to Risk-Weighted Assets Ratio
CRISIL	Credit Rating Information Services of India Limited
CRM	Cash Recycler Machine
CRP	Community Resource Person
CRR	Cash Reserve Ratio
CSC	Common Service Centre
CSP	Customer Service Point
CTI	Cooperative Training Institute
DAY-NRLM	Deendayal Antyodaya Yojana-National Rural Livelihoods Mission
DBT-F	Direct Benefit Transfer in Fertiliser
DCCB	District Central Cooperative Bank
DDO	Disbursing and Drawing Officer
DEA	Depositors Education and Awareness
DFLAP	Digital Financial Literacy Awareness Programme
DFS	Department of Financial Services
DHRP	Draft Red Herring Prospectus
DL	Direct lending
DNH	Dadra and Nagar Haveli
DSCB	Domestic Scheduled Commercial Bank

DSS	Decision Support System
E-NACH	Electronic-National Automated Clearing House
E2E	End-to-End
EAP	Eastern Asia & Pacific
ECS	Electronic Clearing System
EDO	Entrepreneurship Development Officer
EPFO	Employees' Provident Fund Organisation
ERP	Enterprise Resource Planning
FBC	Field Business Correspondent
FIAC	Financial Inclusion Advisory Committee
FIF	Financial Inclusion Fund
FIG	Financial Intermediary Group
FINO	Financial Inclusion Network and Operation
FIP	Financial Inclusion Plan
FIRC	Financial Inclusion Resource Centre
FITF	Financial Inclusion Technology Fund
FLC	Financial Literacy Centre
FLDG	First Loss Default Guarantee
FRDI	Financial Resolution and Deposit Insurance
FSDC–SC	The Financial Stability and Development Council-Sub Committee
FY	Financial Year
G2C	Government To Citizen
G2P	Government To People
GAIN	Global Alliance for Improved Nutrition
GAP	Good Agricultural Practice
GBA	Gramin Bank of Aryavart
GF	Grameen Foundation
GIS	Geographic Information system
Global AUA	Global Authentication User Agency
GLP	Gross Loan Portfolio
GMSS	Grameen Mahila Swayamsiddha Sangh
GNPA	Gross Non-Performing Advances
GoI	Government of India
GPFI	Global Partnership on Financial Inclusion
GST	Goods and Services Tax
GSTN	GST Network
HDBS	Horizontally Differentiated Banking System
HDI	Human Development index
HR	Human Resources
IBA	Indian Banks' Association
IBC	Insolvency and Bankruptcy Code
ICDS	Integrated Child Development Services
ICE	Industry Cluster Enterprise
ICT	Information and Communications Technology
IFC	International Finance Corporation
IFMR	Institute for Financial Management and Research
IFMR-LEAD	Institute for Financial Management and Research-Leveraging Evidence for Access and Development
IGL	Income Generating Loan

IIBF	Indian Institute of Banking and Finance
IMPS	Immediate Payment Service
INFE	International Network on Financial Education
IPO	Initial Public Offer
IRDA	Insurance Regulatory and Development Authority
IRDP	Integrated Rural Development Program
IRR	Internal Rate of Return
IRV	Individual Rural Volunteer
ISB	Business School
IT	Information Technology
ITU	International Telecommunications Union
JAM	Jan-Aadhaar-Mobile
PMJDY	Pradhan Mantri Jan Dhan Yojana
JLG	Joint Liability Group
JLGPI	JLG Promoting Institution
KCC	Kisan Credit Card
KVGB	Karnataka Vikas Gramin Bank
KVIC	Khadi and Village Industry Commission
KYC	Know Your Customer
LAB	Local Area Bank
LAC	Latin American Countries
LAMPS	Large-sized Multi-purpose Societies
LEDP	Livelihood and Enterprise Development Programme
LIC	Life Insurance Corporation
LLG	Limited Liability Group
LMI	Lower-Middle Income
LMS	Loan Origination System
LWE	Left-Wing Extremism
M-LAP	Micro Loan Against Property
MACC	Mutually Accepted Code of Conduct
MACS	Mutually Aided Cooperative Society
MAVIM	Mahila Arthik Vikas Mahamandal
MBGB	Madhya Bihar Grameen Bank
MCLR	Marginal Cost of fund-based Lending Rate
MDR	Merchant Discount Rate
MEDP	Microenterprise Development Programme
MEITY	Ministry of Electronics and Information Technology
MENA	Middle Eastern North Atlantic Countries:
MF	Microfinance
MFI	Micro Finance Institution
MFIN	Microfinance Institutions Network
MGNREGS-NRLM	Mahatma Gandhi National Rural Employment Guarantee Scheme-National Rural Livelihoods Mission
MGNREGS	Mahatma Gandhi National Rural Employment Guarantee Scheme
MIS	Management Information System
ML	Machine Learning
MNO	Mobile Network Operators
MOPAD	Multi Option Payment Acceptance Device
MoU	Memorandum of Understanding

MP	Madhya Pradesh
MSE	Micro and Small Enterprises
MSMED Act, 2006	Micro, Small and Medium Enterprises Development Act, 2006
MSMEs	Micro, Small and Medium Enterprises
MSRLM	Maharashtra State Rural Livelihoods Mission
MUDRA	Micro Units Development and Regulatory Agency
NABARD	National Bank for Agriculture and Rural Development
NABFINS	NABARD Financial Services Ltd
NACH	National Automated Clearing House
NAFIS	NABARD All India Financial Inclusion Survey
NAFSCOB	National Federation of State Cooperative Banks Ltd.
NAMCABS	National Mission for Capacity Building of Bankers for Financing the MSME Sector
NBFC-MFI	Non-Banking Finance Company-Microfinance Institution
NBFC	Non-Banking Finance Company
NCD	Non-Convertible Debentures
NCGTC	National Credit Guarantee Trustee Company Ltd.
NDA	Nirantar Deposit Agent
NE	North-East
NEFT	National Electronic Funds Transfer
NeGD	National e-Governance Division
NICT	Network for Information and Computer Technology
NJGB	Narmada Jhabua Gramin Bank
NOFN	National Optical Fibre Network
NPA	Non-Performing Asset
NPCI	National Payments Corporation of India
NRI	Non-Resident Indian
NRLM	National Rural Livelihoods Mission
NRLP	National Rural Livelihoods Project
OECD	The Organisation for Economic Co-operation
OER	Operating Expense Ratio
OSCB	Odisha State Cooperative Bank
P2P	Peer-to-Peer
PACS	Primary Agricultural Credit Societies
PACS	Primary Agricultural Societies
PAO	Pay and Accounts Office
PAR	Portfolio at Risk
PB	Payments Bank
PCA	Prompt Corrective Action
PCI	Payment Council of India
pcNSDP	per capita Net State Domestic Product
PDC	PACS Development Cells
PDS	Public Distribution System
PDY	Puducherry Locate
PFRDA	Pension Fund Regulatory and Development Authority
PIB	Press Information Bureau
PIN	Personal Identification Number
PLF	Panchayat-Level Federation
PMEGP	Prime Minister Employment Guarantee Programme
PMFBY	Pradhan Mantri Fasal Bima Yojana

PMGDISHA	Pradhan Mantri Gramin Digital Saksharta Abhiyan
PMJDY	Pradhan Mantri Jan Dhan Yojana
PMJJBY	Pradhan Mantri Jeevan Jyoti Bima Yojana
PMJJY	Pradhan Mantri Jeevan Jyoti Yojana
PMJSY	Ptradhan Mantri Jeevna Suraksh Yojana
PMMY	Pradhan Mantri MUDRA Yojana
PMSBY	Pradhan Mantri Suraksha Bima Yojana
PNB	Punjab National Bank
POS	Point Of Sale
PPI	Prepaid Instrument
PSB	Public Sector Bank
PSGIC	Public Sector General Insurance Companies
PSL	Priority Sector Lending
PSLC	Priority Sector Lending Certificate
PSU	Public Sector Undertaking
PTC	Pass Through Certificates
QR	Quick Response
RBI	Reserve Bank of India
RCB	Rural Cooperative Bank
RF	Revolving Fund
RIDF	Rural Infrastructure Development Fund
RKCC	RuPay ATM cum Debit Kisan Credit Card
RMU	Risk Management Unit
RRB	Regional Rural Bank
RSCB	Rajasthan State Cooperative Bank
RTGS	Real Time Gross Settlement
RTI	Right to Information
SAP	Structural Adjustment Programme
SBA	Small Borrowal Account
SBLP	SHG-Bank Linkage Programme
SBM	Swachch Bharat Mission
SBN	Scheduled Bank Note
SC	Scheduled Caste
SCB	Scheduled Commercial Bank
SCNL	Satin Creditcare Network Limited
SDG	Sustainable Development Goal
SEBI	Securities and Exchange Board of India
SERP	Society for the Elimination of Rural Poverty
SFB	Small Finance Bank
SGSY	Swarnajyoti Gram Swarozgar Yojana
SHG-BLP	Self-Help Group-Bank Linkage Programme
SHG	Self-Help Group
SHPA	Self-Help Promoting Agency
SHPI	Self-Help Promoting Institution
SIDBI	Small Industries Development Bank of India
SIFMI	Systematically Important Financial Market Infrastructure
SKDRDP	Sri Kshetra Dharmasthala Rural Development Project
SLA	Service-Level Agreement
SLBC	State Level Bankers Committee

SLBC	State-Level Bankers' Committee
SLI	Second-Level Institution
SLR	Statutory Liquidity Ratio
SME	Small and Medium Enterprises
SRLM	State Rural Livelihood Mission
SSA	Sub-Service Area
SSI	Small Scale Industry
ST	Scheduled Tribe
StCB	State Cooperative Banks
STCCS	Short-Term Cooperative Credit Structure
STRBI	Statistical Tables Relating to Banks in India
Sub-K	Name of Organization
SVCL	SV Credit Line
TAT	Turn Around Time
TBA	To Be Announced
ToT	Trainers of Trainees
TRAI	Telecom Regulatory Authority of India
TSP	Technical Service Provider
UBGB	Uttar Bihar Grameen Bank
UCB	Urban Cooperative Bank
UCV	Used Commercial Vehicle
UIDAI	Unique Identification Division of All India
UMANG	Unified Mobile Application for New-age Governance
UP	Uttar Pradesh
UPI	Unified Payments Interface
URC	Unbanked Rural Centre
USOF	Universal Service Obligation Fund
USSD	Unstructured Supplementary Service Data
VDBS	Vertically Differentiated Banking System
VID	Virtual ID
VJS	Vikas Jan Shakti
VO	Village Organisation
VSATs	Very Small Aperture Terminal
WASH	Water Sanitation and Health Programme
WBES	World Bank Enterprise Surveys
WSHG	Women SHG
YES LEAP	YES Bank's Livelihood Enhancement Action Program

Foreword

Having a bank account perhaps is the starting point of financial inclusion. In India, we now boast of approximately 1.8 billion bank accounts.

All this has largely happened under perhaps, the most ambitious financial inclusion campaign ever launched - Jan Dhan Yojana, audaciously announced by the Indian Prime Minister four years ago. This is indeed an incredible accomplishment. According to the Global Findex Report of the World Bank, India has 80% of adults having a bank account. This is a significant jump when you compare it with 54% as per the 2014 Findex Report. Significantly, women saw a 30% spike in account ownership. Secretary, Department of Financial Services, Ministry of Finance, tweeting on the report, said that "of the 51.4 crore bank accounts opened from 2014-17 globally, a whopping 55% were from India". In Phase Two of the PMJDY, the Government emphasis will move from "household" to "every individual" having a bank account, which may see further spike in the number of accounts. Now of course, for fuller gains, beyond account opening, usage of these accounts, entitlements flowing into them, easy availability of loans, digitizing of payments, more cashless transactions, among the others, will need to be the new focus. An eco-system is in place to mount this next campaign, I guess.

Bulk of these PMJDY accounts, however, have been opened in the public sector banks, with only about 3 percent accounts opened by private banks. Over 75 percent account holders now have a Rupay Card and 80% have been linked to Aadhaar. While having achieved impressive numbers, usage of these accounts remains a continuing challenge. There is still a yawning gap between number of accounts and usage. According to Global Findex Report, about 48% new bank accounts were inactive in the last 12 months. A MicroSave Report indicates about 28% of the PMJDY accounts were dormant. Although the PMJDY had an important component of INR 5,000 overdraft facility as well, this too seems to have not taken off. Only one percent account holders seem to have availed this facility. Easy affordable credit is a critical component of effective financial inclusion. In the Phase Two of PMJDY that was recently announced, the OD limit has been enhanced to INR 10,000.

Within PMJDY, a few social security components too are integrated. These include two insurance and one pension scheme. While initially sluggish, there is a welcome uptake in the two insurance schemes in the recent past. Under the Jeevan Jyoti Bima Yojana, a life cover of INR 2,00,000 is provisioned for a premium of INR 330 per year. While the enrolment under the scheme has been to the extent of 5.34 crores, the claims settled were only a little over 92,000 (April 2018). The Suraksha Bima Yojana cover of INR 2,00,000 is for accidental deaths for an annual premium of INR 12. Under this, the enrolment has been over 13.50 crores with only 16,664 claims. The third social security scheme is the Atal Pension Yojana, which guarantees a minimum pension after the age of 60. As on May 15, 2018, the scheme's subscriber base has grown to about 1.1 crores. However, only about 75% of these accounts are making regular monthly contributions. For low-income households to understand and enroll under these programmes, financial education is critical. Our own experience in ACCESS under a financial literacy programme in Jaipur and Sawai Madhopur with poor women revealed that only 12 % knew of these schemes and their benefits. Apparently, it will be a long haul, before many more are able to benefit from these social security programmes.

I assume that technology is the new buzzword that is now intrinsically intertwined with financial inclusion. Not only in India, but also across the world, technology, in all its adaptations, is completely changing the means of delivering financial services, introduction of new products and the ease of access is, in fact, transforming the very economics of financial inclusion. While delivering the keynote address at the FinTech Festival in Singapore recently, the Hon'ble Prime Minister highlighted the six great benefits of fintech: access, inclusion, connectivity, ease of living, opportunity and accountability. In his speech, the Prime Minister hoped that the fintech compaies would help in improving the human condition "through direct contact with the most marginalized". With now over one billion biometric identities, over a billion bank accounts and over a billion mobile phones, India boasts of by far the biggest public infrastructure in the world, he said. In the last few years, with the Government giving a serious push to the idea of Digital India, there has been a spurt in digital financial inclusion.

Technology integration is expected to fuel financial inclusion in the coming years at a far more accelerated pace. As innovations and technologies are increasingly adapted into daily usage, we will witness more disruptive and behavior changing experiences. Starting with payment digitization, financial institutions have fast adopted technology innovations with seamless customer experience, easier customer on-boarding, introduction of new mobile applications, and now even assessing and processing loans. At a certain new bank's anniversary, a new account for me was opened under seven minutes with the aid of a fancy hand-held device.

The vision of Digital India is coming true. Over the last four years, to deliver this vision of Digital India, there have been significant efforts of the Government on building the requisite infrastructure and eco-system. Several ministries and Government agencies like UIDAI, NPCI and RBI have come together to proactively create the enabling environment for a Digital India. The coming together of the JAM trinity, simplified payments through UPI, open APIs, and other technology innovations are helping to build an open seamless eco-system with multiple leverage points to benefit a large number of financial service providers as well as clients. In recent years, there has been a spurt in adoption of digital instruments, even at low-income household levels, given the ease of transactions through UPI that allows hassle free transfer of money from one bank account to another. Using the QR Code mechanism, more than 10 million merchants will accept non-cash payments in the next couple of years. Digital giants like Google and Facebook are beginning to leverage UPI to offer seamless payment services. India is leading the fintech revolution in Asia Pacific, and around the world by creating strong economic opportunities in response to a large unbanked and underserved population. Steep smartphone penetration, increasing access to the Internet, a booming ecommerce market and availability of a large talent pool, which understands both technology and financial services, are paving the way for this digital revolution. We are indeed poised for some serious disruptions in how we manage finance, and that is bound to have equal impact across the board.

With 330 million accounts opened under PMJDY and over 1.3 billion Aadhaar numbers issued, the stage is set for a big boost to Direct Benefit Transfers. So far, during the year, the Government has successfully transferred INR 105,808 crores worth of subsidies under DBT, and the EOY figures could be to the extent of INR 140,000 crores, or 35% of all welfare schemes. This would indeed be a great accomplishment. As of August 2018, 435 schemes of 56 ministries have been covered under the DBT scheme benefiting 124 crore households. Direct transfer of benefits, while hugely bringing transparency and targeting and stemming the prospects of leakages, benefits the Government too. Till FY 2017, it is said that the Government saved around INR 57,000 crores. Due to DBT transfers, the poor will now become more viable customers of banks with subsidies flowing into their Jan Dhan accounts.

While bulk of the PMJDY accounts have been opened through efforts of the public sector banks, with private banks contributing only 3 percent of the total PMJDY accounts, it may be interesting to understand what incrementally the newly established small finance banks may contribute to the financial inclusion campaign in the country. The good part about SFBs is that while 8 of the 10 Small Finance Banks (SFBs) were previously MFIs, and understood the BOP clientele well, one more was a successful Local Area Bank prior to becoming a SFB. This has helped them roll out fairly quickly. While the MFI turned SFBs largely continue with their earlier clients, they are constantly looking at diversification, which may lead them to considering Micro and Small Enterpriese (MSE) and micro-housing loans as a viable opportunity. Some like AU SFB have diversified their loan portfolio quickly to include agri, SME loans, gold loans, home loans and consumer durable loans. The initial stage challenges for SFBs however are deposit mobilization, technology integration, portfolio diversification, and of course, good quality human resources. Based on recommendations of the High Powered Committee chaired by R Gandhi, the then Dy. Governor, RBI, the central bank announced the scheme for voluntary transition of eligible Urban Cooperative Banks (UCBs) to SFBs. There are about 54 Scheduled UCBs as on March 31 2017, of which 31 are multi-state. If a few of these UCBs offer to become SFBs, the number of SFBs will grow and perhaps greater attention to a few ignored sectors and population segments will start to see new financing. However, it is a bit early to say how effectively this group of new generation banks will contribute to overall financial inclusion in the country. Payments Banks, another category of differentiated banks, conceived at the same time as the SFBs, too have rolled out, although only 6 of the original 11 licensees remain. The mandate of these payment banks, through leveraging networks and technology, is to help in reaching out to un-served areas for money transfer and creating small deposit avenues. This is yet a largely untried model, and given that its viability will ride on technology and is likely to face a stiff on ground competition, it will be a while before its efficacy will be proved. While these are fledgling institutions, they could play a catalytic role by introducing products and services designed for low-income populations, encouraging the newly included citizens to engage with formal financial services more deeply. We need to explore how to incentivize these new banks to play this role. For instance, these banks could be considered for direct benefit transfer schemes or considered for government deposits.

As far back as in 2009, Montek Singh Ahluwalia, Vice Chairman of the erstwhile Planning Commission had commented at an ACCESS event that the best prospect for MFIs within the financial eco-system is to play the role of agents of banks, and to some extent this is turning out to be true. Several MFIs are now BCs to banks and in fact a few banks have begun to acquire MFIs to grow their Bottom of Pyramid (BOP) client base. The latest merger this year has been that of Bharat Financial Inclusion Ltd. with IndusInd Bank. Previously, Kotak Mahindra Bank, RBL Bank, IDFC Bank, among others have been a few, which have acquired MFIs. While on the one hand, this trend is likely to continue, a few big ones continue to be upbeat and have looked at the IPO route to grow.

While post demonetization, the sector saw a significant slump and high PAR values, over the last two years, the sector has begun to gradually grow again and PAR too has come down to below 4% from about 15%. The GLP grew by almost 50% at INR 48,094 crores, which is impressive and indicates a strong revival. The outreach of MFIs is impressive, as they have operations in 549 of the 712 districts of the country. However, a granular look at the outreach reveals that 6 states account for about 60% of the total portfolio. This concentration may lead to multiple lending issues. Underserved states like Bihar and Odisha have seen higher portfolio growth than the national average. As used to be the phenomenon in the past, the top 20 MFIs dominate the sector accounting for 92% of the total MFI portfolio. An interesting fallout of demonetization has been that many MFIs are moving away from cash disbursements. Due largely to PMJDY, most MFI clients now have bank accounts, hence making it easier for MFIs to disburse through their bank accounts. While MFIs have periodically seen ups and downs, the sector has been resilient to spring back after a shock, but overall, continues to be vulnerable, as seen after demonetization when local political gangs were pushing the clients not to pay. Other factors such as farm loan waivers also influence client behavior. MFIs have an important role to play in advancing financial inclusion, as has been amply demonstrated in the last two decades; and it is critical that these institutions should be woven into the larger FI vision that the government has.

Self Help Group (SHG) bank linkage programme has traditionally been the other strand that has reached out to rural poor households. While NABARD continues to claim its preeminent position in advancing the movement, which celebrated its 25th anniversary last year, the leadership role of SHG promotion has largely been taken over by the Ministry of Rural Development. Although there have been no breakthrough innovations within SBLP, the programme seems to be growing steadily over the last few years. As on March 2018, over 8.74 million SHGs with a membership of over 105 million, have been savings linked, while almost 5.02 million SHGs are credit linked with an outstanding to the extent of INR 756 billion. Fresh loans during the year showed an impressive growth of nearly 22% and the number of SHGs receiving loans during the year rose by 19%. Thanks to political influences and policies like loan waivers, the loan repayment ethics has seen a decline over the years and recoveries continue to be a cause for worry for banks.

Among innovations being fostered within the programme, digitization is being given a big push. Under the Second phase of NRLP, the World Bank will pump another 250 million USD. It is proposed to digitize the transactions of the community between SHGs and their members and the federations that are promoted under NRLM. Ideas around online loan applications are proposed. In 2015, NABARD too embarked on a pilot project to digitize the social and financial data and for online monitoring of SHGs styled as EShakti. The project has now been extended to 100 districts and will digitize about 4.5 lakh SHGs. This is likely to enhance the confidence of banks to lend more to the SHGs and track their data. These initiatives could possibly give a big boost to SHG lending by banks, which have largely remained wary of the SHG quality and lack of relevant data. NGOs, who as SHPIs played a big role in building the SHG Bank linkage programme, are now mostly marginalized. NRLM largely promotes SHGs through its own cadres and have even co-opted NGO promoted SHGs as a part of their programme. While the public sector banks and RRBs were the lead lenders till a few years ago, of late banks like ICICI have come up with their own models to lend to SHGs and demonstrate that SHG bank lending can become a good viable business proposition. Given the NRLM takeover of the SHG programme, NABARD efforts and innovations, private banks showing new interest, the SHG programme is likely to continue to grow at the steady pace.

The responsibility of bringing together the Inclusive Finance India Report is indeed daunting. For the last three years, Prof. M S Sriram deftly authored the Report, bringing new insights on how the whole financial eco-system is organized and operates, and how through policies, plans and programmes, it brings into its fold, unreached populations that can start to benefit from being financially included. This year, a new team of authors viz. Alok Misra and Ajay Tankha have taken the onerous responsibility of authoring the Report. Dr. Alok Misra is a Professor at Management Development Institute (MDI) and is the Chairperson of the School of Public Policy at the Institute. Alok has been associated with ACCESS publications in the past. For two consecutive years, Alok authored the Responsible Finance India Report that tracked and reported on responsible lending and client centricity within different channels reaching out to low-income households. Alok has deep insights on how financial inclusion has been evolving in the country, and has authored several important studies both within and outside the country. For Ajay, the challenges of bringing out the Inclusive Finance India Report are not new as he has, in the past, been a part of the team that authored two earlier Inclusive Finance India Reports and is a well-known researcher both within India and internationally. Ajay is both analytical and incisive in his understanding of the sector, which he has been tracking, now, for several years. I'm glad that Ajay agreed to take on the responsibility of writing the Report again this year. ACCESS is privileged to have both Alok and Ajay on board as authors for the 2018 Inclusive Finance India Report. During the course of writing the Report, the authors travelled extensively across the country; met with diverse stakeholders including policy makers, regulators, promoters and practitioners; copiously scanned through volumes of secondary literature to bring together truly a "State of the Sector" report. I profusely thank both the authors for painstakingly putting the Report together as a composite reference document, effectively tracking the evolution of financial inclusion in India over the last one year.

I take this opportunity to also profusely thank all the stakeholders who have helped in bringing out the Report. I would like to thank Pawan Bakhshi and Bill and Melinda Gates Foundation for continuing their support to the effort for now three years. Pawan took time off to spend several hours with the authors, scanning the technologies and innovations that were becoming a part of the FI infrastructure. I also take this opportunity to thank Porush, Head of Mastercard in India and his colleagues Rohan and Shikha in supporting the Report. Porush contributed significantly to several ideas for the Report. I would also like to thank Dr. Harsh Bhanwala and his team at NABARD for their continued long-term association with the Report. NABARD significantly helped with key data, and Harsh spared some valuable time for an exclusive interview with the authors. In addition I would like to thank Pankaj Jain and Madnesh Mishra, Joint Secretaries in the Department of Financial Services, Ministry of Finance for their valuable time and for sharing key information, data and the government's perspective with the authors. I would also like to profusely thank N S Vishwanathan, Dy. Governor, RBI for spending a whole day with the CEOs of all the SFBs and Payments Banks in IIM Udaipur at the CEO Round Table. Thanks are also due to Janat Shah, Director IIM Udaipur for hosting and facilitating the Round Table for the third year in a row. There are several others who helped with the Report, and as always, to bring together a complex Report of this nature, it would have been impossible without all-round support from many.

Finally of course, I take this opportunity to thank my team at ACCESS ASSIST that worked very closely with the Authors in bringing the Report out in time for its launch at the Inclusive Finance India Summit. Radhika and her small young team members - Keerti and Priyamvada indefatigably supported this effort throughout – dealing with the requirements of the authors, pulling down key data, coordinating with the printers, organizing meetings, et al. While this is the ninth year of Radhika's association with the process, I'm delighted with the effusive untiring energies of her colleague Keerti, who kept her patience while dealing with all related requirements for getting the Report together. Lalitha, as always was her efficient best in providing all the logistic support to the authors. Overall, I feel proud of this professional prowess within the organization.

This year's Inclusive Finance India Report is perhaps far more comprehensive, incisive and analytical as it tries to capture all the nuances as the FI scene in the country rapidly evolved. I hope the Report continues to be a good reference document for all those who are tracking and watching the India Financial Inclusion story and in some manner it informs and influences policies.

The Inclusive Finance India Report will be launched at the Inclusive Finance India Summit on December 11, 2018.

Vipin Sharma
Chief Executive Officer
ACCESS Development Services

Preface and Acknowledgements

This is the 12th edition of the annual Inclusive Finance India Report 2017, an initiative by Access Development Services to document both policy and operational aspects of financial inclusion in India. Over the years, it has emerged as a repository of financial inclusion initiatives and is referred to by policymakers, practitioners and researchers. As such, the authors are thankful to the Access leadership especially Vipin Sharma for entrusting us with this responsibility. The challenge was both intellectually stimulating as well as daunting – over the years, the financial inclusion ecosystem has evolved from being focused on microfinance to encompass a variety of players and channels like banks (Universal banks, Cooperative banks, Regional Rural banks, Small Finance Banks and Payments Banks), NBFCs, Fintechs and Banking Correspondents. The institutional diversity is compounded by a host of Government programmes like National Rural Livelihoods Mission (NRLM), Pradhan Mantri Jan Dhan Yojana (PMJDY) and its associated schemes of insurance and pension and Pradhan Mantri Mudra Yojana (PMMY) being overseen by MUDRA. The building of digital rails through Jan Dhan-Aadhar-Mobile, Unified Payment Interface (UPI) and open APIs has seen a focus on innovations in digital channels and has given rise to new generation of fintech lenders as well as increased adoption of digital technology by established players. Overall, while there has been significant progress on the agenda of financial inclusion, the complexity has made the task of narrating the sectoral progress difficult. Modularisation of financial services, wherein the design-retailing-servicing of a financial product has been decoupled across different entities and has made the compartmentalizing different channels difficult. In this backdrop, the task of narrating the progress and raising issues was humbling and led to the difficult choice of balancing depth with broader paintbrush of the entire sector.

We decided to document various institutions and channels as in previous reports but also adopted a divergent approach. Considering the growing interconnectedness between different channels, we decided to include a thematic chapter on Micro & Small Enterprises (MSE) financing in addition to the chapter on Digital Finance. The inclusion of MSE was based on the fact that MSEs have come to occupy the centerstage in public policy as evidenced through MUDRA, Prime Minister's announcement of a slew of measures for the sector in November 2018, SIDBI's renewed focus on MSE as part of its version 2.0 as also due to the fact that MSE sector referred to as the "lost middle" is the engine of broad based growth. The Small Finance Banks, which are covered separately, have also been set up to cater to the "lost middle". The other departure is to discuss a few important challenges in this push for financial inclusion based on our review of the financial inclusion landscape. Despite the significant progress as evidenced by FINDEX 2017, the landscape is dotted with critical issues of persistent regional skew in provision of financial services such as outreach of access not being matched by use; regulatory issues as different entities cater to a similar segment under different rules; discernible shift towards capital market intermediation; and the urban nature of digital innovations. While some of these issues that have been examined are new, others have been persisting for quite some time. For example, the weak health of the banking system as evidenced through the large number of banks being under PCA framework of the RBI coupled with shift towards capital markets has key implications for development policy; it is almost impossible for the smaller enterprises to access capital markets. The obsession with financial inclusion with much lesser attention to its outcomes, which is akin to celebrating the "means" is also discussed. Whereas these issues are introduced in the first chapter, the related themes are reinforced through the narrative in subsequent chapters.

The second chapter takes a deep dive into the performance of banks covering the performance of commercial banks, RRBs and Cooperative Banks. It analyses the macro environment, key policy issues and debates and their performance. Though a part of the banking system, considering the growing importance of Banking Correspondents and Government schemes like PMJDY, a separate chapter 3 was made necessary to document the status of these major initiatives. It also covers the institutional support extended by key stakeholders like RBI and NABARD for financial inclusion. Chapter four is a thematic chapter on the financing of micro and small enterprises, which covers the role of Micro and Small enterprises (MSE) in India's growth, issues faced by them especially financing constraint and analyses the effect of steps being taken to accelerate credit flow to them. It details the performance of banks as well as NBFCs in financing the sector; performance and contribution of MUDRA, new initiatives of SIDBI and Government of India as well as the growing segment of new age fintech lenders. Chapters 5 and 6, are devoted to a detailed analysis of the performance of microfinance covering both MFI model and SHG-Bank Linkage programme/National Rural Livelihoods Mission. The importance of these chapters lies in the fact that despite multiplicity of agencies being involved in financial inclusion, microfinance and the related delivery structures continue to be a dominant force with a combined outreach of nearly 100 million clients. The last two chapters focus on the new initiatives of Differentiated Banking (Small Finance Banks and Payments Banks) and Digital Finance. Between these eight chapters, the attempt is to present the performance of major parts of the financial inclusion ecosystem as well as the emerging issues. The detailing of the progress in financial inclusion makes us feel, to use a cliché - We are in interesting times- when it seems the diversity of institutions, the enabling ecosystem in terms of technology and regulation and the public policy push brings India within striking distance of achieving universal financial inclusion. However, as the journey progresses, the challenges change. It is time for a National Financial Inclusion policy which leverages the strength of each player and harmonises the efforts across channels and accords priority to needs of the customer. The institutional and policy efforts need to be tempered with the ground realities and move beyond first generation issues of outreach to usage and outcome.

The report would not have been possible without the data and insights gained from various sources and the authors will like to thank them profusely. The data from the Reserve Bank of India and other Apex financial institutions namely NABARD, SIDBI and MUDRA and other agencies like NPCI and Niti Aayog has been a key source for this report. Thanks are also due to Micro Finance Institutions Network (MFIN) and NRLM for data support as well as enriching discussions. The roundtable of CEOs of Small Finance Banks and Payments Banks organized by Access Development Services proved to be an invaluable source of information. Immense gratitude is due to a range of stakeholders like Samit Ghosh of Ujjivan SFB, Baskar Babu and Narayan Rao of Suryoday SFB, Prakash Sundaram from Fincare SFB, Raghavan of Equitas SFB, Rishi Gupta of FINO Payments Bank, Udaya Kumar of Credit Access Grameen, Jagadish and Sateesh Kumar from Vaya group, Manoj Nambiar from Arohan, Sanjay Sharma of Aye Finance, Bankers [Prakash Kumar and RK Singh from SIDBI, Surendra Srivastava of MUDRA, technical agencies [Anil Gupta from MicroSave] and policy makers like Pankaj Jain and Madnesh Mishra, Joint Secretary Department of Financial Services, Government of India for sparing their valuable time. Equally significant was the contribution of MFIs and SFBs who responded to the data request. The data provided by Parijat Garg, Crif High Mark Credit Information Services has been valuable in analyzing risks in microfinance. Porush Singh and Shikha from Mastercard provided useful perspective on digital finance trends. Thanks are also due to Swetan and Amit in MFIN for data support. Devahuti Choudhury provided immense help in stitching the piece on Payments Banks on the request of authors. Shri NK Maini, Ex DMD SIDBI provided insightful insights on MSME chapter at short notice.

As in previous years, NABARD was a source of data and inputs for the Report. Chairperson Harsh Bhanwala, K. V. Rao, G. R. Chintala, R. Srinivasan, Neeraj Verma and P. K. Das were generous with their time to discuss policy matters and current issues. Subrata Gupta and Vinod C, NABFINS provided details of the NABFINS model and future plans, Chattanathan Devarajan and Anjali Mahajan, ICICI Bank and Abhijit Maitra and Ruski Mahal YES Bank outlined the strategy of private banks in rural financial inclusion. Satyanarayana Rao, Andhra Bank, Anil Kumar P., Canara Bank, B. Jinesh and Gayathri, Karnataka State Cooperative Bank and D.K. Malhotra, Indian Banks' Association shared insights into their work on inclusive finance.

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Alok Misra
Ajay Tankha

Financial Inclusion: Progress and Challenges

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OVERVIEW OF THE PAST YEAR

Financial inclusion and related issues continued to be at the forefront of national policy and the operational agenda during 2017 and in the first half of 2018. Though the frenzied pace of new institutions and policies seen since 2014—starting from the launch of the Prime Minister's Jan Dhan Yojana (PMJDY) and its associated pension and insurance schemes, and new institutions like MUDRA, small finance banks (SFBs) and payment banks (PBs)—is in the process of getting grounded, the focus on financial inclusion continues. The emphasis now is more on taking the initiatives to the last mile, ensuring the viability of channels as well as usage of services, and harnessing technology—termed digital—to tackle last-mile challenges. New generation players (SFBs, PBs and fintechs) have built their operations around lean, digitally assisted models, and established players like banks are jumping on the bandwagon by building their own mobile phone-based applications as well as by partnering with new players. The partnerships, building on relative strengths, like the reach of microfinance institutions (MFIs), or PBs with banks and insurance companies, are throwing up interesting models for the future. The financial architecture of India has become more complex now, with elements of horizontally differentiated and vertically differentiated banking systems,[1] and the variety of institutions (universal banks, regional rural banks [RRBs], cooperative banks—urban and rural, non-banking finance companies [NBFCs], SFBs, PBs, non-banking finance companies-microfinance institutions [NBFC-MFIs], insurance companies, wallet operators) is bewildering even for an insider. Further, it is getting increasingly complex, with digitally enabled interconnectedness between different players. However, before these new generation institutions can stabilise and prove their business case, due to public policy's eagerness to achieve last-mile financial inclusion, there is news that newer institutions or transformations are being thought of. A news item on the government considering setting up a bank for financing self-help groups (SHGs) appeared recently[2]—though it must be admitted that there has been discussion on similar lines in the past too. There is now a move by the Reserve Bank of India (RBI) to allow the transformation of urban cooperative banks (UCBs) into SFBs, based on the recommendations of the R. Gandhi committee.

As the report goes to print there have been policy-level developments which will have far-reaching implications. First is the Supreme Court ruling on the constitutionality of Aadhaar (Targeted Delivery of Financial and Other Subsidies, Benefits and Services) Act, 2016 (the Aadhaar Act, in short) in *K.S. Puttaswamy v. Union of India.* While the Supreme Court upheld the constitutionality of the Aadhaar unique identity project, noting its usefulness in enabling the delivery of state subsidies and direct benefits, it struck down Section 57 of the Act, thereby prohibiting private parties from seeking authentication based on Aadhaar. Aadhaar authentication by private parties has played a crucial rule in enabling financial inclusion for millions of underserved Indians. Aadhaar's contribution in financial inclusion has been significant—India's remarkable jump in financial inclusion by having a bank account penetration of over 80 per cent is mainly because of the PMJDY; MFIs which provide financial services to nearly 30 million underserved clients started using Aadhaar as a robust means of authentication as well as for checking debt levels with credit bureaus; banking correspondents (BCs) in rural areas were using the Aadhaar-enabled payments system (AEPS) to undertake transactions; and many fintechs started on the premise of Aadhaar and its ecosystem, which made small ticket offerings to excluded sections of society financially viable for the first time. The ruling will also have an adverse impact of the Jan Dhan-Aadhaar-Mobile (JAM) trinity as the delinking of Aadhaar from bank accounts and mobile phones makes the trinity fall apart. The Supreme Court judgement has affected major parts of the financial inclusion landscape, with institutions trying to come up with alternative processes as well as representing to the RBI and the government. It is learnt that the Indian Banks Association (IBA) has made a representation to the RBI on the subject. The situation remains fluid at the ground level as institutions are interpreting the ruling in their own way. In addition, the instructions keep changing—it is reported that the UIDAI has asked banks to continue with the AEPS facility as this mode of withdrawal is part of the Direct Benefit Transfer (DBT) scheme where the use of Aadhaar is allowed.[3]

The JAM trinity and financial inclusion efforts could be adversely affected by the Supreme Court ruling

During the last year, all entities given licences for SFBs commenced operations, with Janalakshmi Bank being the last in April 2018. Similarly, six PBs—Airtel, Paytm, Fino, India Post Payment Bank and Aditya Birla—are now operational, and one more is likely to be operational soon, that is, NSDL, which is in the user application testing phase.

The year saw quite a bit of activity in the microfinance space by way of IPOs and a merger. Bandhan Bank, which is now a universal bank, had a hugely successful initial public offer (IPO). Credit Access Grameen (an NBFC-MFI) also had its successful IPO, but more important was the merger of Bharat Financial Inclusion Limited (BFIL), the largest NBFC-MFI, with IndusInd Bank. The BFIL will now work as a BC of IndusInd Bank, which effectively means a continuance of its pre-merger model, albeit with the risk being transferred to IndusInd Bank. Mainstream banks continued their financial inclusion push through the expansion and strengthening of the BC network, the implementation of the government's PMJDY scheme, and the pursuit of targets set under financial inclusion plans and priority sector. The efforts and their outcomes are evident, with the RBI reporting 533 million basic banking savings accounts, or no frills accounts, aimed at excluded sections—a phenomenal eightfold jump from 73 million in 2010—and 5,98,093 banking outlets in villages.[4] The later figure needs to be seen in perspective as reaching banking services to excluded sections of society, especially rural and residing in 6,40,867 villages, has often been described as policy utopia, pursued since the bank nationalisation of the late 1960s—this seems to be nearing reality now, thanks to the policy push seen in recent times.

The RBI continued its focus on financial inclusion through four essential pillars: (i) priority sector and MSME lending; (ii) financial inclusion plans; (iii) strengthening of the BC network; and (iv) financial literacy. While continuing to monitor performance under the priority sector, the RBI has now operationalised a platform to enable trading in priority sector lending certificates (PSLCs) through its core banking solution (CBS) portal (e-Kuber). The PSLC trading mechanism allows the market mechanism to drive priority sector lending by leveraging the comparative strength of different banks—a bank overachieving its target in a particular sector can sell the excess portion to another bank, which can buy it to meet its target in that sector. The sub-targets under the priority sector, with respect to small and marginal farmers and microenterprises, were made applicable to foreign banks with more than 20 branches in March 2018. From 2018–19, foreign banks with 20 branches and above will have to achieve the sub-target of 8 per cent of adjusted net bank credit (ANBC) or credit equivalent amount of off-balance-sheet exposure (CEOBE) for small and marginal farmers and the sub-target of 7.50 per cent lending to microenterprises.[5] Further, version 2 of the National Mission for Capacity Building of Bankers for Financing the MSME Sector (NAMCABS), employing newer and more comprehensive training material covering the latest developments in the sector, was initiated by the RBI in collaboration with the College of Agricultural Banking, Pune. The public policy push for higher credit flow to the MSME sector was visible throughout the year. On 2 November 2018, Honourable Prime Minister dedicated the new portal (https://www.psbloansin59minutes.com/signup) – a digital initiative to ease the application and sanction process for MSME loans up to Rs 1 crore. The PSB Loans in 59 minutes is an online marketplace, which will enable In-Principle approval for MSME loans up to INR 1 Crore in 59 minutes from Public Sector Banks. Along with it, the Prime Minister also announced a slew of supporting measures like 2% interest subvention, increase in Government's mandatory procurement from micro and small enterprises from 20 to 25% and compulsory onboarding of PSUs and companies with turnover of more than Rs500 crore on TReDS - online electronic institutional mechanism for facilitating the financing of trade receivables of MSMEs through multiple financiers.

The Banking Correspondent model continued to be primal in the central bank's pursuit of financial inclusion, as of the total 5,98, 093 banking outlets in villages, BCs accounted for 91 per cent share. Based on the recommendations of the Committee on Medium-term Path on Financial Inclusion (2015), the RBI issued instructions to the IBA for setting up a BC registry as well as a certification framework for BCs. The BC registry is intended to be a one-stop repository of all BCs, expected to help in having a holistic view of underbanked and less penetrated areas in a region to facilitate the designing of suitable policy interventions. The registry has been open to participating agencies like banks but still not accessible to the public, which might be the next stage.

Government of India accelerated the pace of digitally enabled financial inclusion through various supporting measures in digitising services, development of applications and ecosystem changes. In November 2017, the UMANG app was launched which provides a unified platform where multiple government services (central, state and regional) can be accessed by the user. The versatility of the app comes from providing access to services as diverse as passport, provident fund and crop insurance. The app can be accessed from a smartphone, computer and tablet, and is integrated with popular customer-centric services like Aadhaar and Digilocker. As a post-remonetisation exercise, in order to boost digital payments, the government through gazette notification took a bold policy decision to reimburse merchant discount rate (MDR) charges on digital transactions below Rs 2,000 for a period of two years.

Figure 1.1: Screenshot of UMANG app

The digital push has been accelerated by open application programming interfaces (APIs) for various financial and know your customer (KYC) services enabling various fintechs to build platforms linking customers with diverse services or use KYC and credit bureau records to offer their own products and services. Fintech is the flavour of the season, with numerous entities having sprung up in the last two years.

The government's creation of a facilitating ecosystem as well as the provision of basic banking services through the JAM trinity have almost reached their numerical targets. Aadhaar enrolments have covered 88.5 per cent of the population by 30 April 2018[6] (the figure is lower because of a few northeast states and Jammu & Kashmir). The PMJDY bank accounts, which are a subset of accounts categorised as basic savings bank deposit account (BSBDA) by the RBI, have now covered 315 million people with Rs 81,307 crore of deposits as on 2 May 2018.

The dynamics of financial inclusion has seen a paradigm change in the last three years. With ubiquitous bank accounts, biometrics-based national ID, penetration of cell phones, 360-degree credit bureau records, start of SHG credit reporting and new payment systems, it can be rightly said that India has leapfrogged into creating the necessary building blocks of financial inclusion. The overall picture of financial inclusion as gleaned through various official sources shows significant progress, especially if seen in the backdrop of the not so recent past.

While much of these follow the conventional focus on needed areas, what holds promise for the future relates to the preparation of a National Strategy for Financial Inclusion by the RBI, and the mention of the RBI's intent of moving towards activity-based regulation. In India, a very elaborate and diversified structure of financial services has been put in place—as mentioned above, there are 5,98,093 banking outlets in villages[7] (which include BCs) as of 31 March 2017 and 1,46,282 branches of scheduled commercial banks (SCBs) as of March 2018.[8] This is further supplemented by nearly a lakh primary agricultural credit societies (PACS), 9,838 branches of NBFC-MFIs,[9] 1,54,965[10] post offices (including Grameen Dak Sewak post offices) and branches of SFBs, UCBs, physical touchpoints of PBs and 8.7 million SHGs. The diversified architecture at present seems to move towards a 'do all' through technology and the BC route, which often leads to suboptimal results for both financial institutions and clients, and more importantly leaves no room for building on synergies. A national-level strategy on financial inclusion which outlines clear objectives for each player, with outcome-based monitoring, ties the different pieces together, and furthers the cause of financial inclusion, with each player playing to its strength is the need of the hour.

COMPOSITE PICTURE OF INCLUSION: FINDEX 2017[11] AND INCLUSIX 2018[12] : AN UPSWING

The policy push of financial inclusion, especially opening of accounts under the PMJDY, has been vindicated by Findex, with the survey showing 80 per cent of adults above the age of 15 in India having a bank account, as compared to the global average of 69 per cent. The enormity of the change that has happened in India is evident from the fact that Findex 2014 reported 54 per cent account ownership in India, and the figure for 2011 was even lower at 35.2 per cent (Figure 1.2).

The 80 per cent account ownership among adults also does not show much variation across gender and income classes, with 76.6 per cent women as well as 77.1 per cent adults belonging to the poorest 40 per cent having accounts in a financial institution. This is a very positive development, reflecting gender equality and the spread of bank accounts across the entire economic spectrum of the population. It is noteworthy that in a span of three years, bank account ownership has become ubiquitous in India and the position of India is almost near the highest scoring countries of the developed world. The data for India from Findex 2017 is given in Annexure 1.1.

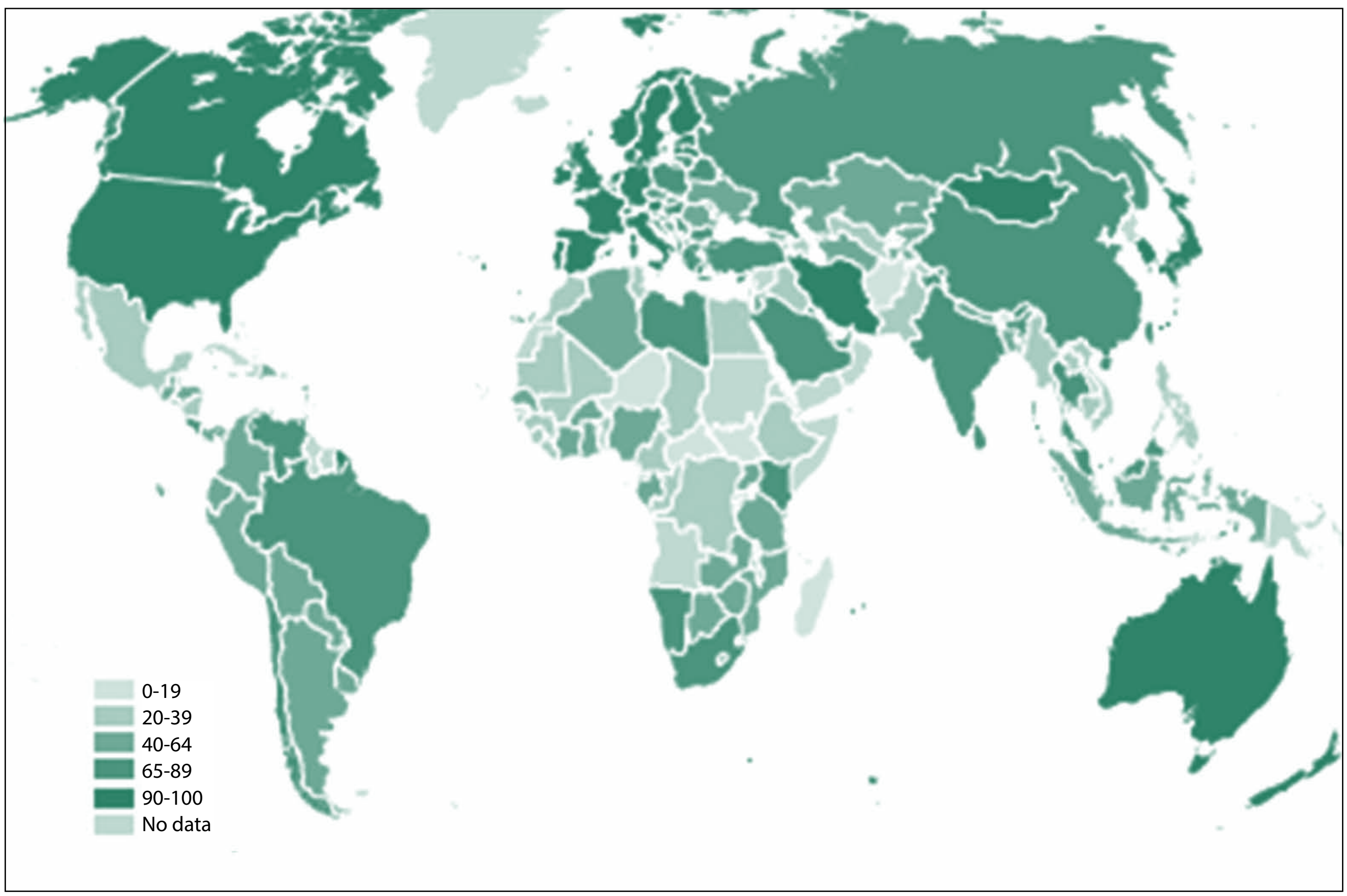


Figure 1.2: Account Ownership (adults with an account) (in per cent))

Source: World Bank Group, *The Global Findex Database 2017* (Washington, D.C.: World Bank Group, 2018).

CRISIL's Inclusix 2018, released in February 2018, also testifies to the progress made under financial inclusion in India. While Findex is a consumer-based survey, Inclusix is based more on macro numbers reported by the RBI, IRDA, MFIN and other agencies. Put together, both provide comprehensive supply-side and demand-side perspectives. CRISIL's methodology takes data up to the district level on four counts (deposit, credit, insurance, branches) to arrive at a composite score. The scores are to be interpreted as given in Figure 1.3.

The all-India Inclusix score has seen an uptick since 2014. However, the figures post-2013 have also included credit accounts of MFIs, and the 2016 data includes insurance figures. The score has gone up to 58, classifying India's financial inclusion progress as above average. The reasons attributed to the increase are the Jan Dhan accounts as also the increase in credit accounts across regions.

CRISIL INCLUSIX SCORE	LEVEL OF FINANCIAL INCLUSION
>65.0	High
Between 50.1-65.0	Above average
Between 35.0-50.0	Below average
<35.0	Low

Figure 1.3: CRISIL Inclusix Score

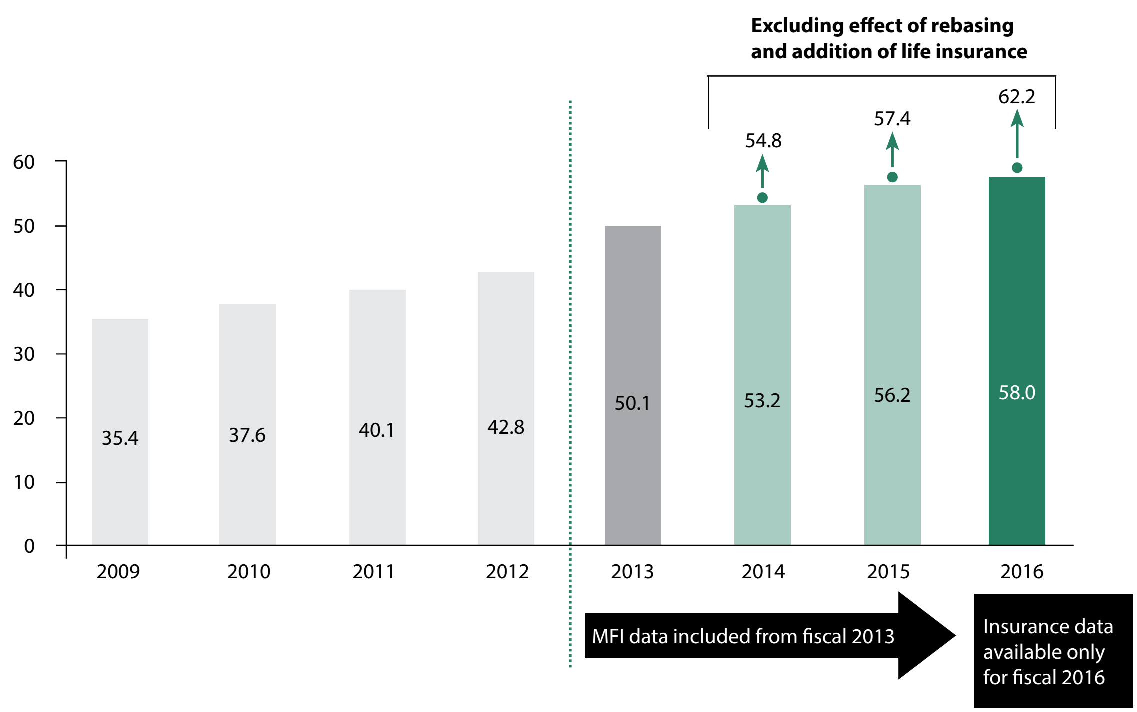


Figure 1.4: Inclusion Index of CRISIL's Inclusix

Source: CRISIL Inclusix, Volume 4 (Mumbai: CRISIL, 2018).

'Mutual Funds Sahi Hai'[13] (Mutual funds Are the Right Choice): Capital Market Inclusion

Financial inclusion through capital markets has also come to the fore in recent times, supplementing the inclusion push through the traditional banking services paradigm. The surge of interest has been boosted through multiple factors like falling interest rates on small savings and bank deposits, demonetisation, depressed returns in other asset classes like real estate, and more importantly, the publicity done through print media and television. An Association of Mutual Funds in India (AMFI) promoted advertisement, with its catchy punchline, 'Mutual Funds Sahi Hai', is seen frequently on television, highlighting the suggestion that small value placements of Rs 500 ($8) are also suited for mutual funds investment. The market intermediary's view is also supported by government publications. In an investor's handbook, the secretary in the Ministry of Corporate Affairs in 2010 writes:

> Buoyant and participative financial and capital markets are not only one of the most important requirements for growth of corporate economy, but are also an important instrument of financial inclusion. The buoyancy in these markets is as much dependent on the performance of the corporate sector as is on the participation of informed investors in the market operations.[14]

On account of these multiple factors, there has been a surge in financial savings flowing into capital market through the mutual fund route. The AMFI data on assets under management (AUM)—an indicator of aggregate level of funds under various mutual fund schemes, both equity and debt—shows exceptionally high growth during last year (Figure 1.5). AUM grew by 85 per cent in the last three years (September 2015 to September 2018). While this points to overall growth reflecting the growing importance of capital markets in the Indian economy, its impact on financial inclusion can be seen through growth in retail participation, disaggregated by geography and size of individual holdings.

However, as these data points are not available, the AMFI data on type of investors and place of origin of investments can act as proxy. As of 31 December 2017, nearly 90 per cent[15] of the investments in mutual funds come from retail investors (other categories are corporates, banks, FIs, high net worth individuals).

While this shows that capital market participation across retail segments has spread wide, the place of origin data clearly points out that at present this is mainly accounted for by the top 15 centres, which are urban centres (Figure 1.6). The top 15 centres account for 72 per cent of individual investments, while all other centres (indicated by B-15 or Beyond 15) have 28 per cent share. Historical data is not available to compare the growth in the market share of B-15 over the years. The data point clearly indicates that 85 per cent of retail investments are still through distributors, which shows the need for proper enforcement of the distribution guidelines of SEBI and the code of conduct of AMFI. The other point of caution relates to 68 per cent of holdings being in equity mutual funds and the balance being accounted for by debt, liquid/money market and exchange traded funds, which are considered safer for capital protection. It would be worthwhile to analyse the growth of distinct retail investors over the years; the available data being on folios does not allow this, as one individual could have multiple folios.

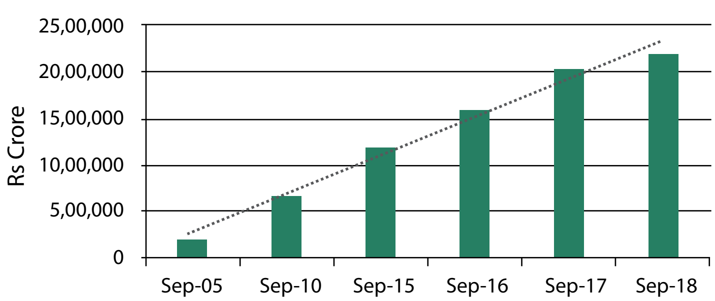


Figure 1.5: Growth in Mutual Funds Assets Under Management

Source: https://www.amfiindia.com/research-information/aum-data/age-wise-folio-data. Accessed on 20 October 2018.

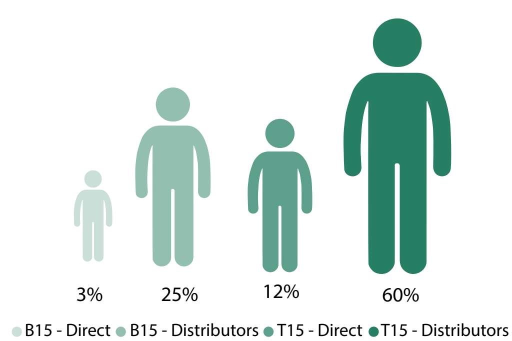


Figure 1.6: Retail Investment Spread across Centres in India

Source: https://www.amfiindia.com/Themes/Theme1/downloads/home/IndividualInvestor-mar2018.pdf. Accessed on 12 June 2018.

It is likely that this increased flow will not only grow in width (coverage of more geographies and excluded segments) but also depth (per capita capital market investment). The advent of fintech companies like Scripbox, Kuvera and Arthayantra focused on middle classes will accelerate this progress as they combine risk profiling, advisory based on risk profile and ease of investments through one channel. The period 2017–18 also saw new fintech companies further expanding the canvas by targeting low-income customers. Paytm Money Limited, registered with SEBI as an investment advisor, plans to launch a dedicated app, Paytm Money, which will facilitate investments in mutual funds.[16] The unique proposition offered by it relates to the fact that apart from selling mutual funds, the app will also provide portfolio services to investors where they can view complete details of their investment through the app. According to reports, it plans to start operations soon and is also looking at tapping microfinance customers through MFIs.

Kaleiodofin, a fintech started in 2017–18, aims to provide a bouquet of products: investment, savings, credit, and insurance products through hand-picked partnerships with financial institutions, which include banks, insurance companies and mutual funds. Its intent seems to be to reach bottom of the pyramid customers, as an NBFC-MFI and an urban cooperative bank are its network partners.[17] It is quite likely that in the era of fintech and app-based solutions, there will be more such initiatives marrying the client reach of one institution with financial product providers through an app-based solution company.

On the face of it, the concept of broadening the ambit of savings from banks to capital markets, thereby enabling a vast majority to benefit from a different asset class, seems laudable as micro-savings has been a neglected area. On the flip side, there are several questions like: (i) How will the enormous challenge of making people aware of various types of mutual funds be met? (ii) Will these providers clearly state the downside risk associated with market fall considering that normally the statement 'subject to market risk' goes unnoticed even by educated people? (iii) Will the awareness of front-line staff in dealing with clients on the complexities of capital market be carefully examined to ensure that clients' interests are protected?

Besides customer protection, there is a developmental aspect to this change in financial intermediation. This shift from what Storm[18] calls the 'visible hand' of relationship banking to the 'invisible hand' of financial markets can have critical implications for growth, inequality and poverty—the purpose of financial inclusion. In a country like India, nationalisation of banks and the phase of social banking were aimed at correcting market failures and directing resources to needed sectors. The challenges of inequality and poverty remain and the policy also continues to reinforce the social objectives of finance through measures like the PMJDY and MUDRA loans, but the landscape is changing in financial intermediation. Moving of domestic financial resources towards capital markets will lower the capacity of banks to provide services to the excluded or weaker sections, and this segment cannot take credit from capital markets. While it is still in its early phase in India, the policy has to factor this in. Storm, while summarising the findings from various papers, says: 'the macro and microeconomic impacts of the rise to dominance of financial markets on capital accumulation, growth and distribution have overwhelmingly found to be deleterious'.[19] It would be apt to say that it is more so in a developing country like India. While news items[20] on this shift have begun to appear frequently, the need is to have a policy response in time.

CRITICAL DIMENSIONS OF FINANCIAL INCLUSION PROGRESS: AGENDA FOR THE FUTURE

The progress seen over the last decade in India's journey towards financial inclusion is commendable, and the rubric that has been established in the form of biometrics-based Aadhaar identification, innovations in payment systems, the advent of fintech marrying finance with technology like big data, and the availability of bank accounts open up immense possibilities of innovative services and products. Progress and possibilities for the near-term future also carry with them certain legacy issues as well as emerging issues. The real success of India's quest for universal financial inclusion will come from tackling these issues proactively. These issues are operational, policy related as well as in the domain of the development discourse. The following sections briefly outline the issues and challenges, and the remainder of the report aims to integrate them, while outlining the progress and initiatives of various channels. It is amply clear that financial inclusion efforts in India have to shift from first generation issue of outreach and access to usage. Simultaneously, the broader debate has shifted from transparency in provision of financial services to privacy of customer data.

Moving from Outreach to Usage

The bedrock of progress in recent years has been a phenomenal increase in bank accounts, enabling people to save with the formal sector, receive DBT under various central and state government schemes as well as make remittances. The global development discourse now recognises that outreach is only a part of financial inclusion and development, and the true measure of financial development has to capture both financial institutions and capital market on three parameters—depth, access and efficiency.[21] This seems logical as markets are now playing an important role in India, and mere accounts do not mean much unless these are used effectively. Back in 2006 the Rangarajan Committee also mentioned this aspect succinctly: 'The Committee, on several occasions, deliberated at length the need for arriving at a working definition of the term 'Financial Inclusion'. In these deliberations, a consensus emerged that merely having a bank account may not be a good indicator of financial inclusion'.[22]

If the lens of usage is applied to the Indian financial inclusion story so far, it shows that much work is needed. Data from Findex 2017 shows that the positive side of outreach and numbers do not reflect in other critical parameters of usage, credit off-take and digital payments (Table 1.1).

Table 1.1: India's Key Parameters of Financial Inclusion

	2017	2014
Mobile money account (% age 15+)	2	2.4
Made or received digital payments ((% age 15+)	28.7	19.3
Inactive accounts in the past year (% age 15+)	38.5	NA
Saved at a financial institution (% age 15+)	19.6	14.4
Borrowed from a financial institution or used a credit card	8.1	9.1

Source: World Bank Group, *The Global Findex Database 2017* (Washington, D.C.: World Bank Group, 2018).

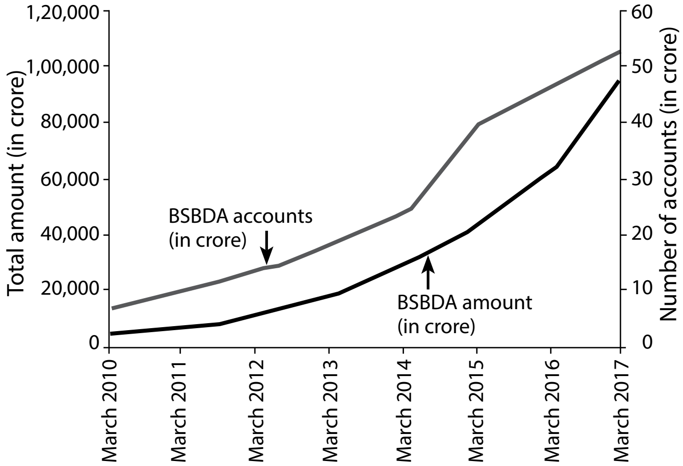
Table 1.1 shows that while approximately 80 per cent adults in India do have a bank account, only 19.6 per cent saved at least once in a year and 28.7 per cent received at least one digital payment during a year. Though the figures on savings and digital payments have moved up from 2014, there is a wide gap compared to account ownership.

Evidence of this also comes from an article in March 2018 which analysed the performance of the PMJDY[23] contrasting the surge in the number of BSBDA accounts (of which Jan Dhan accounts are a subset with additional features like RuPay debit card and overdraft facility) with accounts having zero balance or those not in operation. It is noteworthy that the PMJDY scheme since February 2017 does not track zero-balance accounts and has shifted to monitoring inoperative accounts, defined as accounts not having any customer-induced transactions for the last 24 months, a very liberal definition of such accounts.[24]

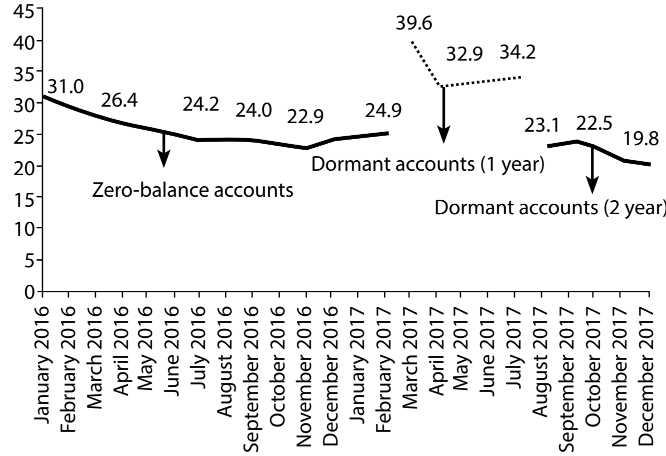
Figure 1.7 and 1.8 clearly show the disconnect between access and usage. While the BSBDA accounts recorded a steep increase post-2014 (the figures include approximately 30 crore PMJDY accounts making up almost the entire growth post-2014), 24.9 per cent of the PMJDY accounts were zero-balance accounts as of Feb 2017—the last time such a measure was used to monitor PMJDY accounts. It can be argued that zero balance is on a date and does not accurately gauge the usage as the poor often withdraw the entire amount from the account and hence inoperative/dormant account is a better measure. On this count also, even after taking the liberal definition of dormancy post-August 2017, around 20 per cent of the PMJDY accounts were dormant in December 2017. There have also been reports of bank officials depositing one rupee from their side to avoid the account being termed zero balance.[25]

The problem related to low usage of bank accounts is also seen across composite financial services (insurance and pension) formulated as part of the PMJDY package. Atal Pension Yojana (APY) was launched in June 2015 for all bank and post customers and the primary target of it is people working in the unorganised sector. Typically, most such customers would be out of the banking sector's outreach but thanks to the PMJDY now most have bank accounts and are hence eligible for coverage under the APY. The APY's objective is laudable, as a majority of the Indian population, estimated between 80 to 90 per cent, falls under its ambit and pension after working life provides the much-needed social security. The APY's attractiveness is enhanced by the fact that it is a 'defined benefit' pension scheme and also comes with government contribution for certain categories of people.

The progress under this is reported by the Pension Fund Regulatory and Development Authority (PFRDA). It is seen that while the website[26] says the scheme is nearing 10 million subscribers, the persistency of the APY measured as policies with regular premium contribution is steeply falling in the second year itself (Figure 1.9).



Source: RBI Data (https://dbie.rbi.org.in/).



Source: Indiastat (from Ministry of Finance) for ZBA, response to Rajya Sabha question for dormant accounts.

Figures 1.7 and 1.8: Progress and Dormancy of Basic Banking Savings Accounts

Source: Dipa Sinha and Jyoti Azad, 'Can Jan Dhan Yojana Achieve Financial Inclusion?' Economic & Political Weekly, 31 March 2018.

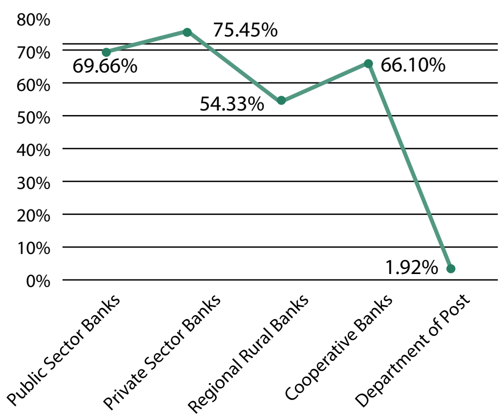


Figure 1.9: Persistency under the Atal Pension Yojana as of 31 December 2016

Source: http://www.pfrda.org.in//MyAuth/Admin/showimg.cshtml?ID=1070. Accessed on 22 June 2018.

Public sector banks (PSBs) account for 70 per cent share of the APY accounts but had a persistency level of 69.66 per cent by December 2016, implying that 30 per cent policies are not regular. All other agencies fare similarly, though the Department of Post stands out as an exception with 1.92 per cent persistency.

A word of caution: It is nobody's contention to undermine the humongous achievement of the account opening drive under the PMJDY, its associated insurance and pension schemes. The discussion is aimed at ensuring that we move to next generation issues of usage to make financial inclusion work for the poor. The focus has to shift to understanding the reasons for less usage and addressing them through suitable policy interventions. Field visits of the authors show there are multiple reasons, ranging from duplicate accounts, lack of saveable surplus, to distance from access points. Inactive accounts neither serve the cause of customers nor institutions as banks have to bear the cost of maintaining such accounts. This requires not only a change in focus but also credible data on a pan-India basis. The Committee on Comprehensive Financial Services for Small Businesses and Low-Income Households (2014) had recommended:

> RBI should mandate two surveys of consumers, to gain a more appropriate picture of progress towards achieving the desired outcomes outlined in the vision statements. The Financial Access & Usage Survey should be a nationally representative survey of consumers, undertaken annually to collect data on access and usage of financial services, and can be incorporated in the form of additional modules in the nationally representative surveys that are being undertaken for other purposes by institutions such as the National Sample Survey Organisation (NSSO) and the Centre for Monitoring Indian Economy (CMIE).

Though there has been little traction on addressing the causes for low usage, thereby taking us beyond the first generation issue of outreach, the outreach is receiving fresh attention with the government announcing coverage of the remaining 120 million excluded adults under the PMJDY's second wave.

The Challenge of Credit-Side Inclusion

The financial sector policy in India has always placed strong emphasis on extending credit to the excluded segment (even before savings and remittances started to be stressed), often at subsidised rates, and concepts like priority sector lending and service area approach were evolved after bank nationalisation. While instruments of the past like priority sector lending continue, new initiatives in recent times focus on credit-side inclusion. Setting up of MUDRA to cater to enterprise loans up to Rs 1 million; prescription of a higher, 75 per cent priority sector target to SFBs; and interest subvention on farm loans are examples of the focus on boosting credit flow to small borrowers. The PMJDY, which is primarily aimed at opening of bank accounts, also has a provision for extending overdraft facility up to Rs 5,000.

Despite the policy push, Findex 2017 shows that the situation remains suboptimal. The percentage of adults reporting borrowings from a financial institution or having used a credit card during the last one year fell to 8.1 per cent, a 1 per cent dip from 9.1 per cent in 2014. As the Findex methodology does not capture borrowers with loans taken before one year, the trend data for SCBs in the case of loans below Rs 1 million (the MUDRA cap) throws up critical insights.

The data clearly shows that in both the number of loan accounts and loan amount outstanding, the annual growth in the case of loans below Rs 25,000 had wide swings—both negative and positive. In other categories there is no unusual spike and the trend of around 10 per cent annual growth continues (Figure 1.10 and 1.11). It is noteworthy that the number of loan accounts of SCBs below Rs 25,000 as of 31 March 2017 is less than the figure of 31 March 2011. Banks have also been reluctant to extend overdraft facility under the PMJDY, with only 1 per cent of PMJDY account holders having been provided the facility as of December 2017. This segment—loans below Rs 1 million—covers the most excluded sections, i.e., small and marginal farmers and small businesses.

Microfinance through both MFIs and the SHG-Bank linkage programme has been instrumental in providing credit facilities to the weaker sections with loans typically below Rs 40,000. The total outreach under MFIs and the SHG-Bank linkage programme reached around 100 million clients by March 2018, not counting the overlap. If microfinance outreach is compared with loan accounts below Rs 25,000 of SCBs, the outreach of SCBs is lower than that of MFIs, which underlines the underachievement of

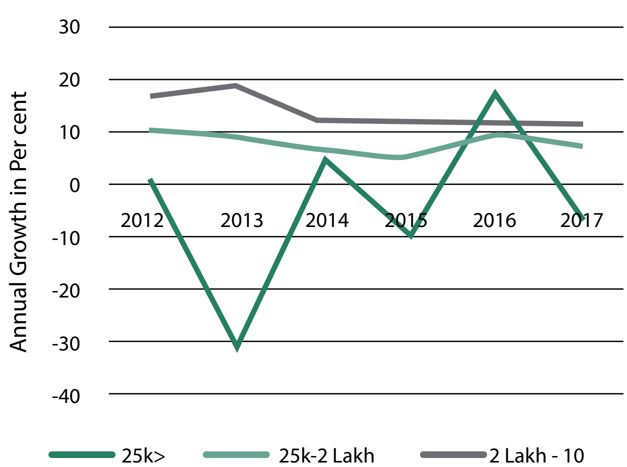


Figure 1.10: Annual Growth in No. of Loan Accounts of Small Loan Sizes of SCBs (2012–17) (in per cent)

Source: RBI, Basic Statistical Returns. https://rbi.org.in/Scripts/AnnualPublications.aspx?head=Basic%20Statistical%20Returns. Accessed on 24 June 2018.

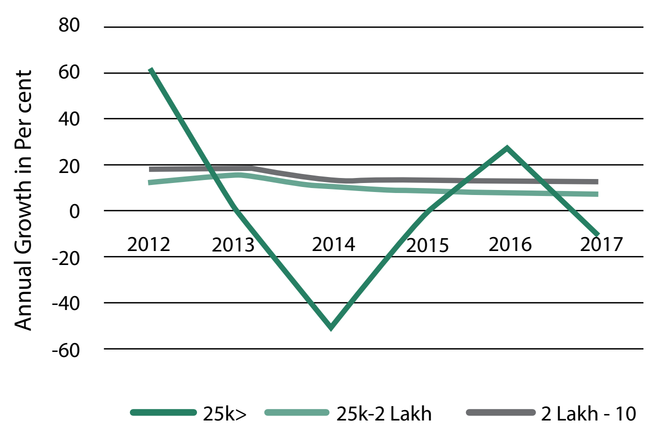


Figure 1.11: Annual Growth in Loan Outstanding under Small Loan Sizes of SCBs (2012–17) (in per cent)

Source: RBI, Basic Statistical Returns. https://rbi.org.in/Scripts/AnnualPublications.aspx?head=Basic%20Statistical%20Returns. Accessed on 24 June 2018.

banks in poverty lending. The continued growth in microfinance despite the moving away of major players in the recent past as universal banks and SFBs points to the model advantage in catering to small borrowers. The credit-side problem is more acute in the case of the 'lost middle', the segment which is beyond microfinance and below the normal loan size of a bank. CRISIL Inclusix put the total loan accounts in India including MFIs at 196 million in 2016, which, seen with possible overlap of clients or loans from multiple agencies to a single client, reflects deficiency in credit intermediation. It will be worthwhile for policy to examine the segment advantage of specific players and stitch a policy that allows each player to focus on its segment strength.

The role of credit in enabling clients to harness their productive potential is at the core of financial inclusion, and the same has been documented through multiple studies. Raghuram Rajan, in his paper on East Asian economies,[27] cites the correlation between bank credit and economic growth. A recent paper[28] analysing data for 21 states of India for the period 2001–2014 also found a bidirectional causal relationship between bank credit and economic growth—bank credit causes and is also caused by economic growth. The Committee on Comprehensive Financial Services for Small Businesses and Low-Income Households (2014), citing various studies, observed that a 10 percentage point increase in the private credit-to-GDP ratio reduces the percentage of population in poverty by 2.5–3 percentage points. The committee cited that high-income countries had attained an average credit-to-GDP ratio of close to 200 per cent and recommended that India should plan to take its credit-to-GDP ratio to a number over 100 per cent.

However, domestic credit provided by the financial sector as a percentage of GDP has hovered around 75 per cent in India during the five years from 2012 to 2016[29] with a slight dip of 1 per cent in recent years. The bank credit, after a steep dip in 2017, has recently started going up. The implementation of the new insolvency and bankruptcy code and recent efforts towards recapitalisation have the potential to ease stress on the banking sector and reinvigorate bank credit. While banks will continue to be the major source of credit to individuals, from a financial inclusion perspective the role of MFIs, NBFCs, SFBs and emerging fintech players will be crucial in extending credit to small borrowers.

Persistence of Regional Skew

Issues of usage and deficiencies in credit intermediation are also compounded by regional differences in financial inclusion. Much of the recent progress in digital technology-led inclusion efforts have been towards payments, followed to a smaller degree towards savings. The regional tilt is evidenced across channels, be it banks, MFIs or SHG-Bank linkage (channel-wise details in subsequent chapters).

The Rangarajan Committee in its 2008 report analysed credit gap across India and found that out of 583 districts, as many as 256 districts (spread over 17 states and 1 union territory) fall in the above category. Almost all major states in the northeastern, eastern and central regions exhibited credit gap as well as a few districts in states like Gujarat, Rajasthan and Maharashtra. The recent Inclusix shows that despite improvements the problem of regional skew continues to persist. It observes, 'Six of the top 10 states/union territories are from the south, while six of the bottom 10 states/union territories are from the North East'. The credit penetration and composite Inclusix score across regions shows the tilt towards south and west (Table 1.2).

Across states, the credit penetration picture captures the gap visually. Fifteen states come under below average or low category. It is noteworthy that the figure also includes microfinance loans (Figure 1.12).

Table 1.2: Credit Penetration Compared with Composite Inclusix Score at the Regional Level

Region	Credit penetration score	Composite Inclusix score
South	91.6	79.8
West	59.1	62.8
North	44.8	51.7
East	42.5	48.2
Northeast	47.7	46.5

Source: CRISIL Inclusix, Volume 4, February 2018, Mumbai

Figure 1.12: State-wise Credit Penetration, 2016

Source: CRISIL Inclusix, Volume 4, February 2018, Mumbai

Barring a few states like Gujarat, a clear link between low Human Development Index (HDI) scores and low credit penetration has been established by studies. A 2014 study[30] of 16 major states of India in terms of population covered per branch, banking business (deposit plus advances) per branch, and credit-deposit ratio, also examined the impact of the indicators on socio-economic development in these states in terms of per capita Net State Domestic Product (pcNSDP) and HDI. The analysis was based on the time series data from 1991 onwards, and the results show a significant link between banking indicators and development indicators.

In channels like joint liability group-based microfinance, over a period of time, regional concentration has been replaced by state and/

or district concentration, but the skew persists. Financial institutions' views on this disparity have been primarily based on economic activity concentration in these areas, and credit is a logical corollary. It is a plausible argument and public policy should focus on providing basic catalysts for economic growth in these areas, like infrastructure (physical and digital) and stable law and order. At the same time, however, it is difficult to justify around 45 per cent of the microfinance portfolio in 50 districts or southern and western states accounting for 62 per cent of SCBs' outstanding credit as of 31 March 2017.[31] On the other hand, central, eastern and northeastern states put together account for a mere 16.5 per cent of SCBs' outstanding credit. This regional skew is further compounded by other forms of skew, like occupational and gender. This is a major challenge which has to be tackled by policy, regulation and institutions together for achieving inclusive growth. As an example of the interplay, the policy of capping interest rates in microfinance or loan waivers can be cited, which have not achieved the intended objectives.

Regulation: The Blurring of Boundaries

The Mor Committee (2014) talked about the concept of horizontally and vertically differentiated banking structures and the merits of each segment operating in its area of strength. Regulations post-2014 show a move towards a vertically differentiated structure, which can be broadly defined as limited functions at the bottom and a full suite of functions at the top. NBFC-MFIs and PBs are examples of the most limited functions institutions, with NBFC-MFIs being allowed to only lend to a particular set of clients, and money transfer and limited deposits being the primary function of PBs. Regulatory oversight also gets progressively steep with the increase in functions on the lines of proportionate regulation. Apart from banking regulations the financial inclusion landscape has to also deal with the insurance regulator, and now capital market regulation as well.

Apart from the interplay of insurance and capital market regulation with banking regulation, the concept of differentiated banking is emerging in a very different way in the field—thanks primarily to technology and partly due to the concept of BC. To illustrate the point, let us consider an MFI. Though regulations vest it with a limited lending function, it can collect savings as a BC, offer insurance and mutual funds in tie-up with an insurance company and a fintech, respectively—additional functions not being on its books, but on the books of primary players like banks for savings. Similarly, a PB can become a BC of the bank and retail loans to its depositors. By doing so, while the differentiation in players defined by regulation is at the back end, for customers it is the unified front end which is providing all these services.

These developments have also been termed 'modularisation' of financial services, wherein the various functions represent modules, with technology enabling separation of origin, distribution and service functions. It has also been defined as: 'In a modular financial system, each module contains a set of functions which may now be performed by different institutions. This allows specialised firms to combine their offerings together and provide a financial product to the end customer.'[32] Within this broad framework, there are multiple models. A bank using MFIs or PBs as BCs to originate loans can be termed a component supplier model, while fintech players and e-commerce sites like Amazon can be termed a platform provider model, wherein the platform links customers to multiple suppliers.[32] While it seems like a good proposition for customers, there are implications for customer protection and regulatory jurisdiction.

The issue of regulatory boundaries can be seen in the case of a fintech working on a platform provider model, linking microfinance customers to savings/investment providers. It is quite likely that to keep it viable, in place of the fintech as distributor the staff of the financial institution will do the client interaction and selling, which is going beyond activities permitted by the regulation governing its legal form. While the MFI is regulated by the RBI, the fintech as distributor is regulated by SEBI. How to deal with the overlap of regulatory jurisdictions of the RBI and SEBI at the field level is an important question, which needs to be addressed. Similarly, considering the multiplicity of schemes under any one asset class, like ultra-short term or liquid mutual fund, addressing the suitability of the scheme being offered to the client is critical—whether it is based on sound fundamentals and technical analysis or influenced by commissions. Does SEBI have the regulatory bandwidth to monitor such micro-level investments?

The conference on financial systems design in 2017 discussed the issue of modularisation and regulatory challenges, and the proceedings note:

> As we see modularisation unveil, we are witnessing a significant increase in the number of market participants. Currently, as it is the case that several of these entities remain unregulated, such as data aggregators and alternative credit scoring companies…. Regulatory design should consider whether the exact function of the modular firm justifies a need for regulatory oversight, and if so, what (is) the optimal channel to apply regulations.

It would be worthwhile to add to it the need for an integrated oversight over the new trend of players with limited licences providing a range of services in tie-up with other players. These are challenging times for regulation in a dynamic environment. Normally, the regulation is either ex post or ex ante and both approaches have their pros and cons.[33] While countries like Kenya in the case of digital finance have preferred to set rules ex post, as services and their providers evolve, rather than impose a strict ex ante regime that might later prove a poor fit, Indian regulation has veered towards an ex ante approach. In the case of modularisation, regulatory guidelines have to combine elements of an ex ante approach to avoid unfair practices taking advantage of the regulatory grey area as well as an ex post approach so as not to hinder flexibility and innovation.

> Modularisation of financial services and regulatory arbitrage due to form-specific regulation pose critical issues related to client protection

To add to the complexity is the issue of 'legal form' based regulation versus 'activity regulation'. While modularisation also impinges on this issue as discussed above, especially at the field level, technically the retailing of other regulated players' financial products does not leave a regulatory vacuum—it is more of an implementation challenge for silo-based regulation. The real issue of 'legal form' based regulation lies in regulatory arbitrage created between different players catering to a similar segment or activity. From the perspective of financial inclusion, microfinance lending is a suitable example. At present, NBFC-MFIs, NGOs, banks and SFBs do microfinance lending but each operates under a different regulatory framework. While NBFC-MFIs have limitations on pricing, client income level and indebtedness threshold, other players do not have such restrictions. This creates an uneven playing field and is also detrimental to the interests of microfinance clients. This issue was raised in the *Responsible Finance Report*.[34] It is heartening that the issue has received the attention of the regulator, and the RBI in its *Trend and Progress of Banking Report* for 2016–17 notes: 'The medium-term goal is to move towards activity-based regulation rather than entity-based regulation'.

Customer at the Core

The global focus on microfinance in the 1990s, and later, on financial inclusion is based on the premise that the poor and excluded need broad-based financial services to realise their economic potential and thereby contribute to economic growth. At the foundation of microfinance was 'client centricity', as it covered clients hitherto excluded by the formal sector. The commercialisation and rapid growth of microfinance not only in India but also in other countries brought the topic of responsible finance into the global development discourse. While several definitions and frameworks have been put forth to define responsible finance, in a simpler lexicon it can be defined as the provision of financial services to low-income clients in a fair and transparent manner, not being detrimental to the client's economic or social well-being, and above all, charging a fair price. CGAP, in its note on responsible finance, asks:

> Is it responsible when a financial co-operative tells its clients that their loan's interest rate is 'only 3 per cent' (without mentioning that this price is per month, is calculated on a flat basis, and excludes the fees and a premium for high-priced credit life insurance)? How about when 'dormancy fees' erode a depositor's account balance every month?[35]

Client-centricity is to be achieved through the three basic pillars described in Figure 1.13.

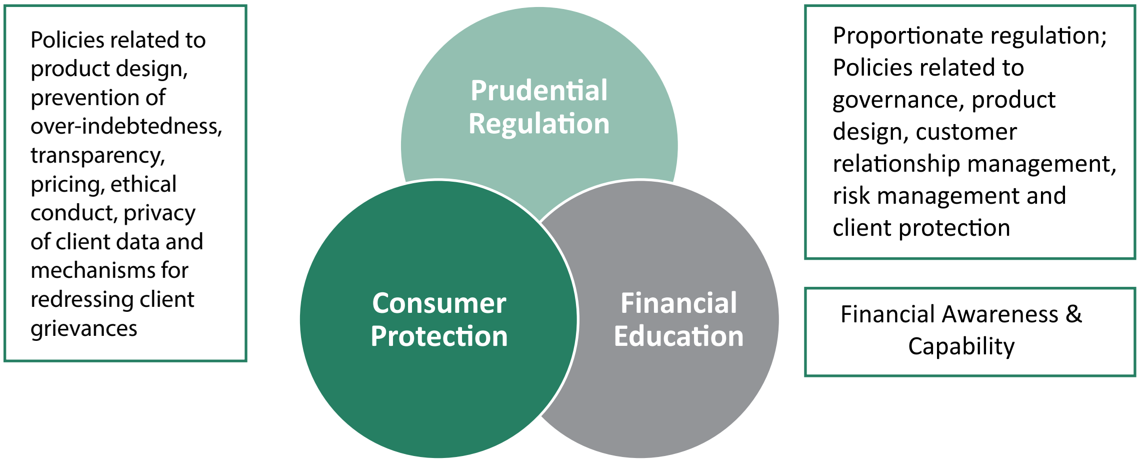


Figure 1.13: The Three Pillars of Responsible Finance[36]

Source: Footnote 36

While the regulatory aspect has been discussed above, the issues of financial literacy and customer protection need to be stressed. The digital push and modularisation of financial services have compounded the issues of consumer protection in a low financial literacy environment. The RBI undertook a pan-India financial literacy and inclusion survey based on the OECD/INFE (International Network on Financial Education) Toolkit across 29 states and 5 union territories. Financial literacy was measured across three components, namely financial knowledge, attitude and behaviour. OECD/INFE considers the threshold score as 5 out of 7 for financial knowledge, 3 out of 5 for financial attitude and 6 out of 9 for financial behaviour. India's average scores in the three components are 3.7, 2.6 and 5.6, respectively. The low financial literacy scores are a sign of concern as in the recent past there has been a concerted effort by institutions, the RBI and the government to inculcate financial literacy.

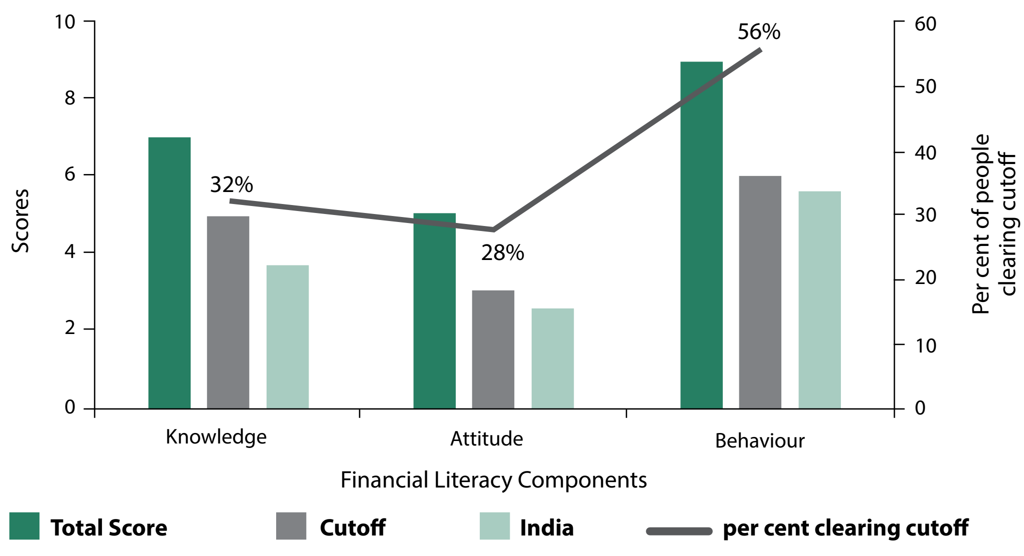


Figure 1.14: Financial Literacy Survey Results

Source: Reserve Bank of India, *Annual Report, 2016*–17 (Mumbai: RBI, 2017)

In this backdrop, the digital push has further complicated the situation. Clients get confused as differing technologies are being used, ranging from debit cards, prepaid cards, PIN-based authentication, Aadhaar-based authentication, mobile phone-based transfers, to different levels of KYC requirements. While there is no argument on the merits of the digital push, it has to be placed in the backdrop of levels of financial literacy and the availability of infrastructure. One bank official rightly points to this by saying:

> The problem today is not on the part of acceptance from the consumer side. The problem today is of plenty now. If you give too much choice to a customer, she will get confused. Not every customer is financially literate to understand all the products now. Rather than giving too many options to the customers, let us just pick up the best few products which are convenient for the consumer, and are scalable. That would be the best way to go non-cash.[37]

The chapter on digital finance discusses more on this.

Grievance redressal is a key part of consumer protection and the situation is getting challenging with the cross-sell of third-party products, or modularisation of financial services, and the shift to digital with its associated charges/fee. Further, while banks come under the scheme of Ombudsman which in itself is not suitable for low-income clients, there are institutions like NBFCs which do not. In a situation where there is a rush to increase the share of fee income, low financial literacy makes mis-selling or unfair practices go unreported. Regulation has been more focused on pricing or rate of interest, while these practices also contribute to cost escalation for the client. Grievance redressal for low-income clients has to be a single source rather than making the client approach different agencies for different products, simple in interface and procedures, with a well-defined resolution time. In 2009, the Raghuram Rajan Committee on financial sector reforms brought out the regulatory gaps, overlaps, inconsistencies and regulatory arbitrage in the financial sector due to the many laws and agencies. It suggested that regulators work through a collective process to protect consumers and raise financial literacy levels. The recent report of the task force to establish a financial redress agency, which recommended that the agency be sector neutral, is a step in the right direction. However, the key will be to keep it simple and one source so as to make it suitable for low-income clients, and backed up by a national-level awareness campaign.

Financial Inclusion as a Means, Not an End in Itself

The failure of the formal financial system to reach vast segments of society, especially the low-income population, provided the ground for the emergence of microfinance. Microfinance overcame the limitations of the formal sector, which had included profitably retailing bite-sized loans, insistence on physical collateral and absence of customised product. The rise of microfinance started in the 1980s after the demonstrated success of Grameen in Bangladesh. Its ability to be profitable and yet reach the excluded and the poor was lapped up by the global community. World Bank integrated it into its structural adjustment programmes (SAPs), donors started investing money in it, and the culmination came with the United Nations declaring 2005 as the International Year of Micro-Credit. The global praise of microfinance can be attributed to the theoretical assumption that access to finance enables clients to better their economic lives and thereby promote broad-based growth.

Over time the claims of microfinance on impact have come under the critical scrutiny of researchers, and there have also been critical views on its focus on credit and high interest rates on lending. Empirical studies have provided a mixed view. Khandker[38] in his study of the Grameen Bank and BRAC; Hulme and Mosley[39] in their study of micro-lending across countries such as India and Indonesia; Chen and Snodgrasss[40] in their study of SEWA Bank clients; and more recently, Samar K. Datta et al. in their study of Bandhan[41] found a positive impact of microfinance on its clients. On the other hand, some studies like Duvendack et al.[42] and Banerjee, Karlan and Kinnan[43] did not find any significant impact, and a few studies also showed negative impacts like over-indebtedness. The microfinance industry responded positively to these challenges by broadening the ambit of financial services (though in India it could not do so due to regulatory guidelines), mainstreaming outcome/impact assessments as part of MIS under social performance management and focusing on double bottom line objectives. The moot point was that the impact of provision of financial services moved centre stage, and rightly so.

In recent times, in line with the concentration on broader financial services in place of credit, financial inclusion has emerged as the new focus area. Its scope is wider, as it embraces banks, community-based programmes, cooperative institutions as well as MFIs. Financial inclusion has now become the dominant theme in development finance and is also the subject of this report. Financial inclusion is mentioned by 5 of the 17 sustainable development goals (SDGs), and the Alliance for Financial Inclusion (AFI) brings together policymakers and regulators from nearly 100 countries under the aegis of the G20. Back home, the drive for financial inclusion under the PMJDY, MUDRA and other programmes like Startup India are also part of this global initiative. Mader,[44] in his review of literature from 1997 to 2015 on the subject, graphically shows how financial inclusion has replaced microfinance in the development finance discourse. Financial inclusion is considered to be promoting inclusive growth by enabling excluded people to be part of financial markets; the Maya Declaration under the aegis of G20 says: 'Recognise the critical importance of financial inclusion to empowering and transforming the lives of all our people, especially the poor, its role in improving national and global financial stability and integrity, and its essential contribution to strong and inclusive growth.'[45]

Financial inclusion, in being a wider form of microfinance, is rightly based on making a positive change in peoples' lives. However, the broadening of the canvas has not correspondingly converted into empirical evidence for positive outcomes, and much of the evidence comes from macroeconomic studies. For example, World Bank's *Global Financial Development Report 2014* bases much of its reasoning on correlations between certain measures of financial inclusion (such as account ownership) and positive macroeconomic and social outcomes.[46] There is a complex issue: macroeconomic growth may not always be equally distributed or might even exacerbate income inequality. Hence, robust micro (client level) economic studies are needed to establish the link between financial inclusion and positive outcomes. There are key variables in local economies, like access to markets, entrepreneurial skills and natural resource context, which influence outcomes, and it needs to be kept in mind that financial inclusion per se cannot lead to the desired outcome. The weaving of the digital narrative into the financial inclusion narrative has further complicated the issue, as digital illiteracy and non-availability of the digital ecosystem can lead to negative outcomes.

However, the global and national push for financial inclusion seems to be being pursued as an end in itself and outcome indicators have reverted to the pre-microfinance situation. Even Findex is all about outreach (number of people having an account, credit etc.) and not about outcomes. In the absence of a demonstrated outcome, there is huge room for questions on the validity of this seemingly seamless link between financial inclusion and inclusive development. Recent discussions on jobless growth in India and the counterpoint of MUDRA loans having created 72.8 million[47] jobs is an example of that. It was critiqued on account of it being based on proxy indicators like the number of loans rather than on any empirical study. It is critical that the push for financial inclusion be backed by evidence on outcomes—mere financial inclusion numbers do not mean much and any public or private investment has to be subjected to outcome monitoring. Outcome monitoring is also likely to throw insights into what part of financial services works where and what the other enabling factors that need to be addressed are. Financial inclusion per se also leaves room for it being termed a neo-liberal ploy to divert attention from the real issues of poverty and inequality.

> Financial inclusion is a 'means' and should not become an 'end' in itself

REPORT STRUCTURE: OVERALL FOCUS AND COVERAGE IN CHAPTERS

Overall Focus

This report is an attempt to document the various pieces of the financial inclusion ecosystem in India, and both its policy and operational aspects. In order to provide an integrative framework, the issues mentioned in section 3 are woven into the narrative across chapters. The report covers all the major financial institutions—banks, RRBs, cooperative banks, MFIs, SHGs, SFBs and PBs. The various schemes of financial inclusion, like the PMJDY and MUDRA as well as relevant studies and publications are embedded in the relevant chapters. The coverage of SFBs and PBs does not take into account the entire spectrum as many institutions in these categories have recently started operations, as well as due to lack of data. As a point of departure from earlier reports, this report also tries to analyse a thematic issue in financial inclusion by documenting initiatives to address the persistent challenge of financing small entrepreneurs—the lost middle. Being a thematic chapter, the discussion on small entrepreneurs cuts across institutions. Besides that, the contemporary focus on digital finance is also discussed in a separate chapter as a theme on the lines of previous year's report. In each chapter, we have discussed emerging new trends and initiatives, to the extent possible, subject to limitations of availability of data and reports. The other departure has been that based on the review of data and reports, opinions and views have been expressed on the progress and its impact on financial inclusion and the ecosystem.

The report intends to be a reference document for sector-level trends, data-based analysis and significant happenings in the financial inclusion space. While there is much research happening which cuts across many years, care has been taken to look at outputs that emerged between October 2017 and mid-October 2018—largely to keep the report current and avoid repetitions. The report draws on all the key available sources of data and information in piecing together the financial inclusion narrative, like the RBI's annual report, *Basic Statistical Returns* and *Trend and Progress of Banking*; NABARD, SIDBI and MUDRA publications; annual reports of individual institutions; World Bank's Findex 2017; CRISIL Inclusix; and NABARD All India Financial Inclusion Survey (NAFIS); among others.

The authors haxe also made use of their in-person interactions with key stakeholders, field visits, conference proceedings, and newspaper and journal articles. However, as is inevitable, some subjective opinions might have crept in. Wherever data or narrative of individual enterprises is presented, it is either due to the fact that sector-level data is not available (for example, SFBs) or to illustrate or demonstrate a point.

Coverage in Chapters

Chapter 2 of the report ('The Banking System and Inclusive Finance') takes a deep dive into the performance of banks. Institution-wise, the chapter covers commercial banks, RRBs and cooperative banks. Starting with an analysis of the macro-environment and policy issues, the chapter analyses the performance of commercial banks in priority sector lending, small borrowal and deposit accounts and financial inclusion plans. RRBs and cooperative banks are also studied on similar lines. Key policy issues, like current restructuring of PSBs, merger of RRBs and delayering cooperative credit structure and its likely impact on financial inclusion, are also examined.

Though BCs and programmes like the PMJDY are part of the banking architecture, considering their growing importance as well as complexity, a separate chapter was considered necessary. Chapter 3 ('Financial Inclusion: Agents, Programmes and Institutional Support') discusses BCs, the PMJDY and its associated schemes, namely the Pradhan Mantri Jeevan Jyoti Bima Yojana (PMJJBY), APY and Pradhan Mantri Suraksha Bima Yojana (PMSBY). The growing scale of these schemes and their role in providing security to the marginalised needed a separate section. Under BCs, the focus is on presenting their diversity, viability of operations as well as various innovations being carried out in the BC space. The concluding section of the chapter covers the institutional support extended by key stakeholders like the RBI and NABARD for financial inclusion.

Chapter 4 ('The 'Lost Middle': Engine of Inclusive Growth') is a thematic chapter on the financing of micro- and small enterprises (MSEs), which has been an area of policy focus in recent years. The chapter covers the role of MSEs in India's growth, the issues faced by them, especially financing constraint, and the effect of steps being taken to accelerate credit flow to them. It discusses the performance of banks as well as NBFCs in financing the sector. The performance and contribution of MUDRA is presented in detail as it is focused on this segment. New initiatives of SIDBI and Government of India as well as the growing segment of new-age fintech lenders are also covered. The separate coverage of this segment is based on the belief that MSEs are the foundation on which inclusive and broad-based growth can happen.

Chapter 5 ('Microfinance Institutions: Recovery and Growth') and Chapter 6 ('Self-help Groups, Bank Linkage and the National Rural Livelihoods Mission Factor') cover between them the important topic of microfinance having an outreach of nearly 100 million clients. The coverage not only talks about the performance and the important initiatives/innovations during the year but also flags crucial policy issues. Chapter 5 covers issues of the microfinance space seeing the involvement of multiple agencies and the consequent regulatory arbitrage, the concentration of operations and the weakening of client relationship. The issues of the NRLM and its interplay with NABARD's SHG-Bank linkage programme at the ground level, the NRLM assuming the leadership of women SHGs that constitute over 80 per cent of SHGs in the country, the digitisation of SHG records (EShakti) project of NABARD, and the NRLM approach of putting emphasis on the role of federations is examined in Chapter 6.

Chapter 7 ('Small Finance Banks and Payments Banks: Struggle for Differentiation and Business Model Continues') is about the recent players in the financial inclusion space. This chapter suffers from the absence of recent sector-level data, and as such, the discussion in the chapter is based on institutional examples tied together by the common theme of challenges being faced and the possible opportunities. As differentiated banks the policy objective for them was to accord primacy to financial inclusion and the chapter examines whether they have been able to rise to the expectations.

The concluding chapter of the report, ('Digital Finance: Progress and Challenges') is again a thematic chapter and is in addition to the digital initiatives covered in other chapters like in the section on BCs, contactless platform for MSE lending and other fintech initiatives, the EShakti project and the cashless project of MFIs. The focus of the chapter is on capturing the ecosystem and sector-level trends like progress in digital transactions across payment channels, the AEPS and DBT. Key issues like ground-level challenges in pushing digital and privacy concerns surrounding Aadhaar are also discussed. The Supreme Court ruling in late-September 2018 on the Aadhaar Act came in just as the report was going to print and hence its wide impact on financial inclusion could not be integrated across chapters. Moreover, the situation is still fluid and its real impact will only become clear in the days to come.

Overall, the financial inclusion space continued to be a dynamic space with sustained policy focus from the government, regulators (especially the RBI) and apex agencies like NABARD and SIDBI. A variety of players such as traditional banks, fintech start-ups, private sector entities like private banks, NBFCs and NBFC-MFIs, NGOs, cooperatives, government programmes (PMJDY and NRLM), and new-age banks (SFBs and PBs) now operate in the financial inclusion space. The multiplicity of institutions and the policy thrust backed by advances in technology make for a very interesting time as financial inclusion efforts move towards next generation issues. Compared to the vastness of the area intended to be covered by the report, this is a small effort to document the current landscape of inclusive finance.

ANNEXURE 1:1
Comparative Picture of India with South Asia and Lower middle income countries

Population, age 15+ (millions)	950.8	GNI per capita ($)	1,670
	Country data	**South Asia**	**Lower middle income**
Account (% age 15+)			
All adults	79.9	69.6	57.8
All adults, 2014	53.1	46.5	41.9
All adults, 2011	35.2	32.4	28.9
Financial institution account (% age 15+)			
All adults	79.8	68.4	56.1
All adults, 2014	52.8	45.6	40.6
All adults, 2011	35.2	32.4	28.9
Mobile money account (% age 15+)			
All adults	2.0	4.2	5.3
All adults, 2014	2.4	2.6	3.2
Account, by individual characteristics (% age 15+)			
Women	76.6	64.1	53.0
Adults belonging to the poorest 40%	77.1	65.6	50.7
Adults out of the labor force	75.1	61.7	50.8
Adults living in rural areas	79.3	69.2	57.6
Digital payments in the past year (% age 15+)			
Made or received digital payments	28.7	27.8	29.2
Made or received digital payments, 2014	19.3	16.7	19.7
Used an account to pay utility bills	6.5	7.1	7.5
Used an account to receive private sector wages	5.4	4.8	5.5
Used an account to receive government payments	8.1	7.1	8.3
Used the internet to pay bills or to buy something online	4.3	4.5	6.8
Used a mobile phone or the internet to access an account	5.3	7.1	8.3
Used a debit or credit card to make a purchase	12.3	10.0	10.0
Inactive account in the past year (% age 15+)			
No deposit and no withdrawal from an account	38.5	31.2	21.6
No deposit and no withdrawal from a financial institution account	38.7	31.6	22.0
Domestic remittances in the past year (% age 15+)			
Sent or received domestic remittances through an account	7.4	7.6	10.1
Sent or received domestic remittances through an OTC service	0.8	1.9	4.7
Sent or received domestic remittances through cash only	8.3	8.3	8.8

Population, age 15+ (millions)	950.8	GNI per capita ($)	1,670
	Country data	**South Asia**	**Lower middle income**
Saving in the past year (% age 15+)			
Saved at a financial institution	19.6	17.2	15.9
Saved at a financial institution, 2014	14.4	12.7	14.4
Saved using a savings club or person outside the family	8.4	10.2	13.0
Saved any money	33.6	33.2	39.7
Saved for old age	11.2	11.4	13.2
Credit in the past year (% age 15+)			
Borrowed from a financial institution or used a credit card	8.1	7.8	9.8
Borrowed from a financial institution or used a credit card, 2014	9.1	8.6	10.0
Borrowed from family or friends	32.7	31.3	30.4
Borrowed any money	42.4	41.5	42.9
Outstanding housing loan	4.6	5.1	5.0

Source: FINDEX, 2017

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The Banking System and Inclusive Finance

2

MAINSTREAM BANKING AND THE FINANCIAL INCLUSION DISCOURSE

Financial inclusion is a term of relatively recent origin, which has emerged as the successor to development initiatives such as cooperatives, regional rural banks (RRBs), targeted lending through Integrated Rural Development Progamme (IRDP), and banking through self-help groups (SHGs) in reaching the poor and the underbanked population. The focus on financial inclusion can be traced to the finance minister's budget speech of March 2005 and the guidelines issued by the Reserve Bank of India in January 2006 for outsourcing of financial services by banks through business correspondents (BCs) and business facilitators (BFs). The subsequent discourse initiated by the Rangarajan Committee of 2007 continues to describe and define the domain of financial inclusion in India.

The Department of Financial Services, the Reserve Bank of India (RBI) and the Indian Banks' Association (IBA) adopted a bank-led model for financial inclusion through the Swabhimaan programme in 2010 which sought to leverage technology and the existing banking infrastructure, as it was felt that only the banks had the ability to offer the suite of products required to bring in meaningful financial inclusion. This has further been elaborated in the form of the Prime Minister's Jan Dhan Yojana and associated products and schemes such as Pradhan Mantri Surakha Bima Yojana (PMSBY), Pradha Mantri Jeevan Jyoti Yojana (PMJJY), Atal Pension Yojana (APY) and Pradhan Mantri Mudra Yojana (PMMY), designed to offer a wider range of financial services covering savings, credit, insurance, remittances and pensions. Nevertheless, the inclusive strategy did not until recently recognise and adequately spell out the role for several significant entities such as microfinance institutions (MFIs), SHGs and their federations and cooperatives that had created and consolidated delivery channels and provided financial services to fulfil the same objectives.

The last 10 years or so have not only been characterised by the financial inclusion project towards global access and use of financial services, but it also attempts to recast the banking architecture to serve both the target population and the wider banking clientele as also the economy as a whole. Thus, various ideas have been floated recently about the desirable structure of the banking system in India to cater to the varied needs of economic agents for financial services.[1] These have involved recommendations ranging from casting apex development banks such as National Bank for Agriculture and Rural Development (NABARD) in a retail banking role (now abandoned); consolidation and merger of public sector banks (PSBs) in which State Bank of India (SBI) and a few other banks have since been involved, the most recent being the proposed merger of Bank of Baroda, Vijaya Bank and Dena Bank; the ongoing amalgamation of regional rural banks; the concept of 'differentiated banking' and the launch of small finance and payments banks; as indeed the case being made out for wholesale and niche banks. In the current climate of high non-performing assets (NPAs) and shaken confidence in the banking system, the pressure of privatisation of PSBs as well as the putting forward of the idea of a regime of 'narrow' banks that would be allowed to offer savings products and not lend have also emerged. A recent addition to the list has been the proposal for a 'bad' bank to help clean up the balance sheets of existing banks. This has resulted in conflicting viewpoints, contending interests and uncertainty for clients of the banking system, not least the targets of inclusive finance.

As per RBI data for 31 March 2018, the total bad loans of banks (loans which haven't been repaid for a period of 90 days or more) stood at Rs 10,35,528 crore or 11.6 per cent of the total advances made by these banks. The gross NPA ratio for PSBs as a category was 14.6 per cent. In fact, many banks have on their own implemented a programme of 'narrow banking' by focusing on the retail sector, particularly motor vehicle and housing loans, for which the ratio of bad loans is only around 2 per cent. Nearly half the bank loans during 2017–18 were to the retail sector.[2]

There is an impression that several of the recent measures by the government to address the problem of NPAs and other structural issues have been undertaken without major consultation with stakeholders which would have helped to restore confidence in the banking system. In fact, it appears that the process of institutional reform of the banking space is still a work in progress which requires greater clarity on the part of the government and the regulator. Notwithstanding the achievements in recent years towards extending banking outreach, the effect of this deficiency is felt on the financial inclusion strategy and the many players involved in the provision of financial services. There has been for some time, since the introduction of Financial Inclusion Plans (FIPs), the stamp of authority of the Department of Financial Services, Ministry of Finance, Government of India (DFS) on the banks, which is mediated through the RBI and the Indian Banks Association (IBA), where target-chasing in inclusive finance continues to be the norm even as more schemes and products are centrally devised and implemented. Banks are further constrained by a set of RBI criteria that determine priority-sector lending and the freedom to open bank branches. Where PSBs have sponsored RRBs, successive rounds of amalgamation and calls for privatisation have similarly affected their ability to adopt an independent course in serving the target population. The cooperative banking structure is characterised by limited and sporadic initiatives that too have focused on recasting the upper layers of the multi-tier delivery system at the expense of addressing grassroots level challenges.

RESTRUCTURING OF THE BANKING SYSTEM AND THE CURRENT MELTDOWN

The last year has undeniably been one where the banking system (particularly PSBs) has come in for unparalleled exposure and scrutiny for the large NPAs that have been generated over the years, and the several instances of scams and malpractices through which large corporate borrowers have exploited weaknesses in banking systems and processes. It is clear that the rot is quite deep and the problems of NPAs and the resultant weak performance and extensive losses have led to a flurry of attempts to find the means to contain the problem. The RBI's Financial Stability Report of June 2018[3] noted that the stress in the banking sector continues as the gross non-performing advances (GNPA) ratio has risen further, and that the profitability of scheduled commercial banks (SCBs) has declined, partly reflecting the increased loan provisioning. In fact, it is reported that all PSBs, barring two, incurred losses in 2017–18,[4] and the combined loss in 2017–18 is estimated at Rs 85,166 crore, which is more than the profits made in the last five years.[5] Though credit growth of SCBs picked up during 2017–18, notwithstanding sluggish deposit growth, Financial Stability Report suggests that the GNPA ratio of SCBs could rise from 11.6 per cent in March 2018 to 12.2 per cent by March 2019. It further warns that the overriding shadow of cyber risk, adoption of innovative technologies like fintech and data analytics for financial intermediation have created new frontiers in regulatory and supervisory challenges that may need to be attended to.

According to the report, macro-stress tests on PSBs under the Prompt Corrective Action (PCA) framework suggest worsening of their GNPA ratio from 21.0 per cent in March 2018 to 22.3 per cent by March 2019, with six PCA PSBs likely to experience capital shortfall. However, the report asserts that the capital augmentation plan announced by the government will go a long way in addressing potential capital shortfall, as also play a catalytic role in credit growth at healthier banks. In parallel, the PCA framework, by addressing the vulnerabilities of weaker banks will help in improving the health of the banking sector. Governance reforms would not only improve the financial performance of the banking sector but also help reduce operational risks.

The 11 banks under PCA are Dena Bank, Allahabad Bank, United Bank of India, Corporation Bank, IDBI Bank, UCO Bank, Bank of India, Central Bank of India, Indian Overseas Bank, Oriental Bank of Commerce and Bank of Maharashtra. Under the revised guidelines of the RBI for prompt corrective action dated 13 April 2017,[6] operative for three years with effect from 1 April 2017, banks face restrictions on distributing dividends and remitting profits. The owner may be asked to infuse capital into the lender.

In addition, lenders are stopped from expanding their branch networks and need to maintain higher provisions. Management compensation and directors' fees are also capped.[7] However, this is not expected to solve the problem, which is quite deep-rooted, even as the Insolvency and Bankruptcy Code (IBC) towards tackling big cases of loan defaults, 'haircuts' to clean the balance sheets of banks and greater accountability of management are invoked. The idea of a 'bad bank' in the form of an asset reconstruction company to take over the toxic loans of PSBs, however, has apparently been rejected by the government.[8]

At the same time, the restrictions on deposits and borrowings by the various banks placed under PCA undoubtedly adversely affect the general public. Besides, as noted by certain commentators, with PCA financial inclusion suffers an irrevocable setback and the massive public investment in financial literacy and opening of bank accounts goes waste.[9]

In October 2017, the government had announced plans of massive capital infusion into PSBs of Rs 2.11 lakh crore spread over two fiscals—2017–18 and 2018–19.[10] On July 2018 an infusion of Rs 11,336 crore was announced in five state-owned lenders including Punjab National Bank (PNB), Corporation Bank and Andhra Bank to help them meet their regulatory capital requirement.[11] This would form part of the remaining Rs 65,000 crore of capital to be infused into PSBs over the two financial years. It is claimed that there is already evidence that the most affected PSBs are back on track and that seven of them have registered profits during the first quarter of the financial year 2018–19 as against only two in the previous year.[12]

The past couple of years have also been a period of consolidation, mergers and acquisitions in both the public sector and private banking space. The merger of five SBI associates and Bharatiya Mahila Bank with the parent bank has been accomplished as of 1 April 2017 in order to streamline their banking portfolio. The cabinet-approved takeover of a 51 per cent majority shareholding in the debt-ridden IDBI Bank by the Life Insurance Corporation of India has set a new precedent of a non-banking corporation exercising ownership and control of a bank. This is expected to synergise and create mutual strengthening of the banking and insurance business under the new entity. Still other models address the question of viable banking and meeting agriculture and priority sector targets in the private banking space. There have been around half a dozen takeovers by private banks of well-performing non-banking financial company-microfinance institutions (NBFC-MFIs).[13] These NBFC buyouts address the financial inclusion challenge even as the microfinance sector engages with its own issues of legal forms and the merits of borrowing for direct retail intermediation as against off-balance sheet lending. These developments, however, are too recent for the impact to be fully felt on the already rising managed and BC portfolio component of MFI loans.

Finally, an RBI decision in August 2018 has allowed banks to co-originate loans with large NBFCs to enable priority sector lending (PSL). This would combine the outreach of the NBFCs with the resources of the banks through risk- and reward-sharing and also help the latter to meet their priority sector targets. While most MFIs in the past have been selling their portfolio to the banks, this could happen now even with the individual loan facility.[14] This is expected to give a boost to financial inclusion among others by benefiting borrowers under the priority sector segment in terms of the cost of credit availed by them.

OUTREACH OF THE BANKING SYSTEM FOR INCLUSIVE FINANCIAL SERVICES

Commercial Banks: Lending and Deposits Up but NPAs Reach Alarming Levels

Table 2.1 illustrates the progress of commercial banking in India as of 31 March 2018. Out of 151 commercial banks in India, there were 149 SCBs, of which 56 were RRBs. Besides these, there were two non-scheduled commercial banks. The number of offices of SCBs was 1,46,282, of which 49,848 were in rural areas. The deposits of these banks amounted to Rs 1,14,793 billion, while the credit outstanding was Rs 86,826 billion, representing a credit deposit (CD) ratio of 75.6 per cent.

The overall share of PSL in the total credit of SCBs was 40 per cent, as mandated. Despite the steady growth in all these indicators, as noted earlier, the last year has been a difficult one for commercial banks with respect to their profitability and the accumulated NPAs that have reached crisis proportions, with only two PSBs having positive profits during 2017–18. The fact that PSBs have been a burden on the exchequer has led commentators to propose an increase in the number and size of private banks, which have performed better than PSBs, though not in terms of their contribution to inclusive financial services. The coexistence of public and some sizeable private banks has created an anomalous situation by which the increasing

Table 2.1: Progress of Commercial Banking at a Glance

Important indicators	June 1969	March 2014	March 2015	March 2016	March 2017	March 2018
Number of commercial banks	89	151	152	152	152	151
• SCBs	73	146	148	149	150	149
o RRBs	-	57	56	56	56	56
Non-scheduled commercial banks	16	5	4	3	2	2
Number of offices of SCBs in India*	8,262	1,17,280	1,25,672	1,32,587	1,37,770	1,46,282
(a) Rural	1,833	45,177	48,498	46,577	48,232	49,848
(b) Semi-urban	3,342	31,442	33,703	36,464	37,880	39,476
(c) Urban	1,584	21,448	22,997	23,867	24,877	27,213
(d) Metropolitan	1,503	19,213	20,474	25,679	26,781	29,745
Population per office (in '000s)	64	11	10	9.4	9.05	9.61
Deposits of SCBs in India (in Rs billion)	46	79,134	88,989	96,599	1,07,514	1,14,793
(a) Demand	21	8,272	7,801	35,190	44,144	
(b) Time	25	70,862	81,188	61,409	63,370	
Credit of SCBs in India (in Rs billion)	36	61,390	64,998	75,209	79,270	86,826
Deposits of SCBs per office (in Rs million)	5.6	675	708	728	780	785
Credit of SCBs per office (in Rs million)	4.4	524	517	567	575	594
Average per account deposits of SCBs (in Rs)	88	64,854	61,963	58,316	58,742	
Average per account credit of SCBs (in Rs)	68	4,52,759	4,76,878	4,63,291	4,59,316	
Deposits of SCBs as percentage of national income (NNP at factor cost, at current prices)	16	86	80	102.84	98.83	
SCBs' advances to PSL (in Rs billion)	5	21,549	23,782	27,577	29,302	
Share of PSL in total credit of SCBs (in %)	14	35	37	41	40	
Share of PSL in total non-food credit of SCBs (in %)	15	36	37	31		
Credit deposit ratio	78	78	73	77.9	68.78	75.6
Investment deposit ratio	29	28	29	31.45	31.62	
Cash deposit ratio	8	5	6	5.59	5.99	

Notes: *Excludes administrative offices.
Numbers pertaining to 2016, 2017 and 2018 are on population statistics based on Census 2011; the other years are based on Census 2001.
Source: Reserve Bank of India, Basic Statistical Returns of Commercial Banks in India, Volumes 43, 44, 45 and 46 (Mumbai: RBI, 2015, 2016, 2017, 2018).

share of private banks in deposits, which has reached a third of the total deposits, could also create a crisis if a big private bank failed.[15]

Nevertheless, it is instructive to examine in greater detail the outreach and performance of the banking system in achieving the objectives and outcomes of the relatively new thrust towards financial inclusion. Despite much discussion and debate, confusion and lack of consensus seem to persist on what constitutes inclusive finance. Many would point to the underbanked and unbanked, and more specifically, the poor and weaker sections excluded from the benefits of development as being the subject of the discourse and the initiative. At the same time, the influential IBA during a meeting with one of the authors could take the view that all financial services other than to the corporate sector would constitute inclusive finance. Accommodating this view, PSL which requires a portion of the portfolio of all SCBs to be earmarked for selected sectors and segments—such as agriculture, weaker sections, micro, small and medium enterprises (MSMEs)[16]—represents a starting point for examining the achievements of banks towards areas

Table 2.2: Achievement under PSL Advances by Categories of Banks, March 2017

Particulars	March 2016				March 2017			
	Public sector	Private sector	Foreign banks	Total	Public sector	Private sector	Foreign banks	Total
ANBC (in Rs billion)	49,178	14,352	3,367	66,897	51,040	17,877	3,756	72,672
Off-balance sheet exposure (in Rs billion)	8,069	2,345	1,807	12,222	7,697	4,157	1,793	13,646
Total agriculture (in %)	18.4	18.59	1.94	17.61	18.55	16.63	4.96	17.38
Weaker sections (in %)	11.14	9.48	1.19	10.28	11.77	9.25	2.13	10.65
MSME (in %)	14.93	20.37	8.55	15.77	14.54	19.90	8.96	15.57
Housing (in %)	5.58	6.41	1.06	5.53	5.76	5.44	0.96	5.44
Educational (in %)	7.35	1.08	0	5.06	1.18	0.16	0.00	0.86
Total priority sector (in %)	40.37	46.13	32.79	41.22	40.04	42.44	34.08	40.32

Note: ANBC: adjusted net banking credit
Source: Statistical Tables Relating to Banks in India (STRBI) (Table 17). http://dbie.rbi.org.in/DBIE/dbie.rbi?site=publications#!3. Accessed on 13 June 2018 for March 2017 data.
March 2016 data as per Inclusive Finance India Report 2017 (IFI 2017).

of the economy that merit special attention. The RBI has over the years streamlined PSL norms, making them stricter. For example, the new PSL targets and sub-targets for lending to small and marginal farmers and to microenterprises have been made applicable even to foreign banks with more than 20 branches.

PSL—On target

Table 2.2 shows the achievements under PSL advances by various categories of banks during the year ending 31 March 2017, the latest data for which is available. The overall performance of the different categories of banks is in accordance with targeted levels. There are only very minor variations over the previous year. During 2016–17, private sector banks appeared to have failed to achieve their sub-target for lending to agriculture with an achievement level of only 16.63 per cent. Similarly, the position of lending to weaker sections and for education is low for private banks, especially in comparison to the PSBs.

However, it would appear that the private sector banks have done well in terms of advances to the MSME sector, as compared to the PSBs. The under-achievement of targeted levels of PSL has to be met through Priority Sector Lending Certificates (PSLCs) acquired from the trading platform established for all banks as of April 2016.[17] Overall, banks are achieving their PSL targets with small shortfalls met through buying obligations through the PSLCs. However, this positive achievement of lending targets needs to be set against the build up of NPAs of various categories of banks in recent years, particularly during the latest year for which data is available.

Non-performing Assets under PSL: Rising, but slower than non-PSL

As noted earlier, the level of NPAs of banks, particularly the PSBs, have come in for a great deal of attention, criticism and alarm, especially in the context of bank scams involving a few large borrowers. Besides, the confusion created by statements from the finance minister about the bail-in clause under the proposed Financial Resolution and Deposit Insurance (FRDI) Bill, as it purportedly allows failing banks to use deposited money to cut losses, understandably triggered a scare among bank depositors. Despite subsequent reassurances about the scope and intention of the Bill, and the bail-in provision, the record NPAs of banks during the past year and the poor performance of all PSBs barring a couple, continues to be a source of great unease about the banking system.[18]

When we consider the gross NPAs as a percentage of gross advances of all SCBs (excluding foreign banks) over the three-year period 31 March 2014 to 31 March 2017, we find that these have increased steadily from 4 per cent to 10 per cent (Table 2.3). The performance of the priority sector has, however,` not been quite as dismal, with the NPA ratio rising from 4 per cent to 6 per cent over this period. This represents in effect a decline in

Table 2.3: Advances and NPAs of Domestic Banks by Priority and Non-Priority Sectors* (in Rs billion)

Year	PSL			Non-PSL			Total		
	Gross advances	Gross NPAs	Gross NPAs (in %)	Gross advances	Gross NPAs	Gross NPAs (in %)	Gross advances	Gross NPAs	Gross NPAs (in %)
Public sector banks									
2017	19,599	1,543	8	31,823	4,868	15	51,422	6,411	12
2016	18,737	1,281	7	32,084	3,740	12	50,822	5,021	10
2015	16,860	937	6	31,593	1,691	5	48,453	2,627	5
2014	15,193	792	5	30,712	1,375	4	45,905	2,167	5
Nationalised banks**									
2017	14,062	1,242	9	20,704	3,459	17	34,765	4,700	14
2016	13,418	989	7	21,000	2,890	14	34,418	3,879	11
2015	12,507	680	5	21,718	1,239	6	34,224	1,919	6
2014	10,711	530	5	21,249	877	4	31,960	1,407	4
SBI group									
2017	5,538	301	5	11,119	1,409	13	16,657	1,710	10
2016	5,320	292	5	11,084	849	8	16,404	1,142	7
2015	4,353	257	6	9,875	451	5	14,228	709	5
2014	4,482	261	6	9,463	499	5	13,944	760	5
Private sector banks									
2017	6,520	133	2	14,529	605	4	21,049	738	4
2016	5,620	101	2	12,297	382	3	17,917	484	3
2015	4,428	72	2	9,946	244	2	14,373	316	2
2014	3,831	61	2	8,287	167	2	12,117	227	2
All SCBs (excluding foreign banks)									
2017	26,119	1,676	6	46,352	5,473	12	72,471	7,149	10
2016	24,357	1,383	6	44,381	4,122	9	68,738	5,504	8
2015	21,287	1,009	5	41,539	1,934	5	62,826	2,943	5
2014	19,024	852	4	38,998	1,542	4	58,022	2,395	4

Notes: * Excluding foreign banks ** Includes IDBI Bank Ltd.
Constituent items may not add up to the total due to rounding off.
Source: STRBI (Table 18). https://dbie.rbi.org.in/DBIE/dbie.rbi?site=publications. Accessed on 14 June 2018.

gross PSL NPAs from 36 per cent of gross advances (Rs 852 billion out of Rs 2,395 billion as of 31 March 2014) to 22 per cent (Rs 1,676 billion out of Rs 7,149 billion as of 31 March 2017).

In the case of all PSBs, the increase in the gross NPA ratio (PSL and non-PSL) has risen from 5 per cent to 12 per cent over the period 2014–17. However, there has been a smaller increase in PSL NPAs from 5 per cent to 8 per cent of gross advances over this period. In the case of the SBI group, while the percentage of total gross NPAs has gone up from 5 per cent to 10 per cent during the period under review, for priority sector advances, the gross NPA percentage has in fact declined slightly from 6 per cent to 5 per cent. Similarly, in the case of private sector banks where the gross NPA percentage for all lending has gone up from 2 per cent to 4 per cent of gross advances over the three years, the NPA percentage for priority sector advances has remained unchanged. It may be thus observed that the NPA percentage of priority sector advances, though rising, continues to be at a much lower level than that for the non-priority sector advances.

The year 2016–17 was the period during which the demonetisation exercise was undertaken. While we find that the gross NPA percentage of the PSL portfolio of all SCBs (excluding foreign banks) did not worsen during 2016–17, that of the non-PSL sector became particularly alarming, with gross NPAs as a percentage of gross advances in 2017 rising to 12 per cent as against 9 per cent the previous year. In the case of nationalised banks (PSBs other than the SBI group), gross NPAs in 2017 reached as high as 17 per cent of gross advances as against 14 per cent the previous year. It would appear that despite the effect of demonetisation on sectors such as agriculture and small enterprise, PSL NPA levels were still contained within relatively reasonable limits as of March 2017, especially compared to the non-PSL sector, with perhaps the full impact of lending performance likely to be felt during the subsequent year 2017–18.

3.1.3 Analysis of small borrowal accounts (SBAs)

3.1.3.1 Loans: Stagnation in share of SBA category but share of smaller loans negligible

It is necessary to go beyond the PSL component towards a more detailed examination of inclusive finance parameters. One parameter that has been subjected to analysis over the years has been the SBAs of banks, which pertain to loan accounts with a sanction limit of Rs 2,00,000. Within this a sub-category represents a smaller slab of up to Rs 25,000, which was the definition of SBAs until 1999. When the data for the two types of accounts—represented by SBAs and the subset of loans of Rs 25,000 or less—is examined, it is observed that there has been over the years a more or less consistent decline in

Table 2.4: Details of Credit to Small Borrowal Accounts over the Years

	Year ending March 2013	Year ending March 2014	Year ending March 2015	Year ending March 2016	Year ending March 2017
Loan amount less than Rs 25,000					
Number of accounts (in million)	30.88	32.57	29.86	35.29	33.25
Percentage of total accounts	24.10	23.50	20.70	21.70	19.30
Limit sanctioned (in million)	4,28,593	4,36,318	4,29,595	5,19,372	5,23,963
Percentage of total amount	0.50	0.50	0.40	0.50	0.40
Amount outstanding (in million)	7,36,827	4,36,318	3,59,945	4,58,836	4,12,941
Percentage of total outstanding	1.30	0.60	0.50	0.60	0.50
Loan amount Rs 25,000 to Rs 2,00,000					
Number of accounts (in million)	71.43	76.66	81.27	89.65	97.01
Percentage of total accounts	56	55.20	56.30	55.20	56.30
Limit sanctioned (in million)	57,34,745	61,70,673	66,45,862	72,52,009	78,60,234
Percentage of total amount	6.90	6.50	6.40	6.50	6.40
Amount outstanding (in million)	44,11,501	48,95,252	53,15,041	57,48,489	61,73,323
Percentage of total outstanding	8.00	7.80	7.70	7.60	7.80
Total up to Rs 2,00,000					
Number of accounts (in million)	102.31	109.23	111.13	124.94	130.26
Percentage of total accounts	80	79	77.00	76.90	75.60
Limit sanctioned (in million)	61,63,337	66,06,991	70,75,457	77,71,381	83,84197
Percentage of total amount	7.40	7.00	6.80	7.00	6.80
Amount outstanding (in million)	51,48,328	53,31,569	56,74,536	62,07,325	65,86264
Percentage of total outstanding	9.30	8.40	7.75	8.20	8.30

Note: The gender-wise break-up of the small borrowal accounts and the amounts indicate that 67.8% of the loan accounts and 71.8% of the loan amounts have been made to men in 2017. 69.9% of the loan accounts and 73.1% of the loan amounts were to men in 2016.
Source: Reserve Bank of India, *Basic Statistical Returns* (BSRs) (Mumbai: RBI, 2013, 2014, 2015, 2016 and 2017).
Gender data for 2017 is from BSR Table 1.14. http://dbie.rbi.org.in/DBIE/dbie.rbi?site=publications#!9. Accessed on 25 June 2018.

the percentage of loans of less than Rs 25,000. Total SBAs declined from 24.1 per cent as of 31 March 2013 to 19.3 per cent as of 31 March 2017 (Table 2.4). The share of accounts with loans in the range of Rs 25,000 to Rs 2,00,000 remained nearly constant at about 56 per cent of total accounts. When the amount outstanding in loan accounts of less than Rs 25,000 as a percentage of total outstanding under SBAs is considered, there is a decline from an already low figure of 1.3 per cent as of 31 March 2013 to as little as 0.50 per cent as of 31 March 2017. On the other hand, if the total number of accounts of up to Rs 2,00,000 is considered, these SBAs rose in number from 102.31 million or 80 per cent of total bank loan accounts to 130.26 million, though they declined to 75.6 per cent of total bank accounts during the same period. Further, for these accounts the total bank loan outstanding in all SBAs as a percentage of total outstanding in all accounts declined from 9.3 per cent in 2014 to 8.3 per cent in 2017.

Finally, if the purpose-wise break-up of SBAs as of 31 March 2017 (Table 2.5) is considered, there is a decline in the number of agricultural accounts of loans under Rs 25,000, the number of which has come down from 17.3 million as of 31 March 2016 to 15.84 million as of 31 March 2017.[19] This is matched by an increase in the accounts of loans between Rs 25,000 and Rs 2,00,000, whose numbers went up from 51.56 million to 54.61 million. In terms of the percentage in total loan accounts for agriculture, the share of the accounts of less than Rs 25,000 declined from 22 per cent to 19 per cent, while those of Rs 25,000 to Rs 2,00,000 increased marginally from 64 per cent to 66 per cent even as the share of SBAs in overall agriculture loans remained relatively unchanged.

With regard to the amount of bank loans outstanding for agriculture, SBA accounts of up to Rs 25,000 contributed Rs 274.77 billion or 2.76 per cent of total agriculture loans as of 31 March 2016. This declined to Rs 244.93 billion, or only 2.27 per cent of total agriculture loans as of 31 March 2017. Total loans outstanding for SBA accounts in the range Rs 25,000 to Rs 2,00,000 increased marginally from Rs 3,824.47 crore to Rs 4,098.28 crore. Thus, the overall picture is one of stagnation and decline in small loans for agriculture, the major purpose of loans and a priority sector for bank lending. It contributed about 54 per cent to the total SBA loan accounts and 66 per cent to the loan amount outstanding in SBAs.

Looking at it another way, the 70.46 million SBAs for agriculture constituted about 85 per cent of total accounts for agriculture, but only about 40 per cent of the loan outstanding. Significantly, SBAs for all purposes constituted about 75 per cent of all loan accounts but only a dismal 8.5% of loan outstanding.

It is evident that SBAs, which are the major banking product of inclusive finance, still do not make a significant contribution to overall bank lending to the poorer and more deprived sections whose share both in the number of loans and in the loan amount of outstanding has at best remained unchanged, if not declined, over the years. The number and share of SBAs of less than Rs 25,000 have been consistently declining. While the number of accounts as well as the amount outstanding has been growing for the segment of borrowers between Rs 25,000 and Rs 2,00,000, their percentage in total accounts too has not registered any change. Similarly, though the amount outstanding under accounts in this sub-category over the four years has registered a substantial increase, the percentage share in total outstanding has only declined marginally.

SBAs are not necessarily to be conflated with accounts of the 'poor'. They would nevertheless represent the bottom rung of the clientele of banks. Several measures have been undertaken during the last couple of years that serve to direct a larger proportion of loans to this segment with a concomitant increase in the number of accounts. This includes the arrival of new players in the banking space, which consists of small finance banks and the Bandhan Bank. The latter has emerged from serving small loanees and continues to maintain a portfolio heavily weighted in favour of SBAs. For the present, small ticket loans do not appear to have taken off despite the comprehensive outreach of the PMJDY and the major effort of the newly designated Micro Units Development and Refinance Agency (MUDRA) loans under the PMMY. It is anticipated that the small loans of less than Rs 50,000 under the Shishu component of the PMMY and even a significant proportion of the medium-size Kishor loans, ranging from Rs 50,000 to Rs 5,00,000, would probably add to the numbers and volume of SBAs during 2017–18.

The slow increase in the number and off-take of SBAs needs further research, even as it should be kept in mind that the efforts of banks in serving clients are supplemented by the large and expanding outreach of microfinance institutions (the NBFC-MFIs) serving the small borrower. Data for these entities is not captured under these accounts, as indeed that of SHGs that are increasingly being supported under a mission mode through state agencies. However, several banks have acquired NBFC-MFIs. The portfolio of the thus-acquired MFIs would now be

Table 2.5: Purpose-wise Break-up of Small Borrowal Accounts as of 31 March 2017

	Accounts up to Rs 0.025 million						Accounts between Rs 0.025 million and Rs 0.2 million						Total small borrowal accounts		
	Accounts (in million)	% of Total	Sanction (in million)	% of Total	Out-standing (in million)	% of Total	Accounts (in million)	% of Total	Sanction (in million)	% of Total	Out-standing (in Rs billion)	% of Total	Accounts (in million)	Sanction (in Rs trillion)	Out-standing (in Rs trillion)
Agriculture	15.84	19	272.79	2.11	244.93	2.27	54.61	66	4,284.33	33.14	4,098.28	38	70.46	4.56	4.34
Direct	14.71	18	250.76	2.17	228.22	2.32	53.34	66	4,193.60	36.34	4,017.38	41	68.05	4.44	4.25
Indirect	1.13	41	22.03	1.58	16.71	1.79	1.28	46	90.73	6.53	80.90	9	2.41	0.11	0.10
Industry	2.18	36	36.64	0.08	29.15	0.10	2.08	35	141.61	0.30	114.35	0	4.26	0.18	0.14
Transport operators	0.11	5	1.94	0.08	0.83	0.05	0.85	38	81.46	3.46	55.34	3	0.96	0.08	0.06
Professional and other service	1.17	25	19.78	0.23	14.95	0.25	2.23	47	159.67	1.88	123.36	2	3.39	0.18	0.14
Personal loans	8.34	14	108.88	0.49	57.85	0.37	30.19	50	2,663.29	11.93	1,361.57	9	38.54	2.77	1.42
Housing	0.14	2	2.42	0.02	1.99	0.02	1.46	19	140.45	1.31	105.20	1	1.61	0.14	0.11
Consumer durables	0.15	16	2.01	1.08	1.23	0.94	0.49	53	44.44	23.92	30.26	23	0.64	0.05	0.03
Other personal loans	8.05	16	104.45	0.91	54.63	0.76	28.24	55	2,478.40	21.70	1,226.10	17	36.29	2.58	1.28
Trade	3.33	31	57.78	0.47	43.68	0.57	5.16	48	369.32	2.99	294.05	4	8.49	0.43	0.34
Wholesale trade	0.10	17	1.59	0.02	1.62	0.04	0.17	29	15.06	0.21	11.85	0	0.27	0.02	0.01
Retail trade	3.23	32	56.19	1.10	42.05	1.12	4.99	49	354.26	6.92	282.20	7	8.21	0.41	0.32
Finance	0.19	19	2.89	0.03	2.71	0.05	0.47	49	44.72	0.49	33.59	1	0.66	0.05	0.04
All others	2.10	49	23.27	0.30	18.86	0.94	1.42	33	115.82	1.49	92.79	5	3.51	0.14	0.11
Total	33.25	19	523.96	0.43	412.94	0.52	97.01	56	7,860.23	6.38	6,173.32	8	130.27	8.38	6.59

Source: Reserve Bank of India, Basic Statistical Returns of SCBs in India 2017, Volume xx (Table 3.4) (Mumbai: RBI, 2018).

Table 2.6: Small (<Rs 25,000) Term Deposits from Customers over the Years

	Year ending March 2012	Year ending March 2013	Year ending March 2014	Year ending March 2015	Year ending March 2016	Year ending March 2017
Number of accounts (in million)	53.85	55.70	66.80	62.97	73.56	63.93
Percentage of total number of accounts	32.80	30.90	33.30	32.0	33.9	35.00
Growth (in %)	2.30	3.32	16.61	–5.73	16.81	–13.09
Amount (in Rs billion)	1,375.19	1,387.30	1,130.10	421.06	704.16	1716.8
Percentage of total deposits collected	3.60	3.10	2.20	1.4	2.1	1.60
Growth (in %)	–23.01	0.87	–22.76	–62.73	67.2	143.81

Source: Reserve Bank of India, Basic Statistical Returns of SCBs in India 2017 (Mumbai: RBI, 2018). For 2017, data calculated from Table 1.7 (Total deposits and total number of deposit accounts), and Table 1.27 (Percentage for <Rs 25,000 deposit).

shown on the books of banks even as the MFIs act as BCs under the new relationship. Further, the use of credit BCs by private banks, and now even by PSBs (with the SBI adding to the list of banks seeking credit BC partners), also serve to significantly enhance bank lending for financial inclusion by targeting the underbanked segment with relatively small-size loans.

Small deposits accounts: Decline in numbers but more than doubling of deposit amount during 2016–17

Quite a different picture emerges when we look at small deposits. The number of small (up to Rs 25,000 term deposit) accounts of bank customers over the years is given in Table 2.6.

These numbers rose steadily until 2016; however, during 2016–17, small-term deposit accounts registered a significant decline in number from 73.56 million to 63.93 million, representing a drop of over 13 per cent. Interestingly, the amount deposited in these of small-term deposits as of 31 March 2017 increased by 143.81 per cent from Rs 704.16 billion to Rs 1,716.8 billion. In fact, the pattern of growth of deposits in these account over the past few years has been rather erratic and difficult to explain.[20] This staggering increase in deposits combined with a decline in the number of customers with term deposits suggests the impact of demonetisation, including the possibility of benami deposits in BSBDA and smallholder accounts.[21] This phenomenon came into focus in the months after demonetisation and an inquiry into 18 lakh such accounts had been ordered.[22] The findings of the inquiry are still awaited.

The year 2016–17 has thus had several unexpected and contrarian results in respect of small borrower and small customer data. Demonetisation led both to the breakdown of credit flows to the small sector but also served up the unexpected massive inflow of funds into some of these hitherto unused and under-used accounts. The Department of Financial Services is yet to put out a comprehensive analysis of the effect of demonetisation on savings and deposits of the small account holders of the Indian banking system.

Developments pertaining to these accounts both reflect as well as have an implication for the financial inclusion drive undertaken in mission mode since 2014. Though credit flows would have been restored during the year 2017–18, the hangover of the suspension of credit flows and the larger impact on small business and the workforce in the informal sector have possible negative consequences for the level of NPAs in the subsequent period for which the data is not yet available. The impact of demonetisation on the small business sector is also evident in the performance of MFIs and intermediaries such as NABARD Financial Services Ltd (NABFINS) lending to MFIs and SHGs through various partnership models.

Financial inclusion plans and performance of banks

The inclusive banking thrust of nearly the past decade aimed at taking banking to the maximum number of small villages and geographically remote locations through bricks-and-mortar branches as well as through various forms of models based on information and communication technology (ICT), notable among which was the introduction of BCs. All public and private sector banks were required to draw up a three-year FIP with effect from April 2010. This significantly contributed to an increase in the penetration of banking services in the rural areas through various modes and types of banking outlets such as bank branches, ATMs, BCs and satellite branches. A second round of FIPs for the period 2013–16 focused more on deeper penetration and increased volume of transactions in the large number of accounts opened. Since 2014, the PMJDY sought to ensure various financial services like the availability of a basic savings account, need-based credit, insurance, pension and remittance services to all at an affordable price through the effective use of technology. Under the PMJDY mission, all villages across the country were to be mapped to ensure at least one fixed-point banking outlet catering to 1,000 to 1,500 households, called a sub-service area. The issues and challenges related to the implementation of the PMJDY are discussed in Chapter 3.

For a third phase from April 2016 to March 2019, the FIP template was revised incorporating new parameters, keeping in view the emerging financial inclusion landscape. Banks have been asked to provide district-level data across population groups—metro, urban, semi-urban and rural. The progress made in the development of the commercial bank branch network and the various parameters tracked by FIPs is presented in this section.

Commercial bank branch network: Small increase in all segments

To begin with, the progress in the development of the banking branch network is examined. It is, therefore, necessary to consider the latest RBI guidelines on the opening of bank branches and outlets. On 18 May 2017, the RBI notified new guidelines for bank branch authorisation. This significantly changed the definition of a branch and quota requirements for opening branches in unbanked rural centres (URCs). As a consequence of this, a banking outlet for a domestic scheduled commercial bank (DSCB), a small finance bank (SFB) and a payments bank (PB) was redefined as a fixed-point delivery unit, staffed either by bank personnel or its BC where services of acceptance of deposits, encashment of cheques, cash withdrawal or lending of money are provided for a minimum of four hours per day for at least five days a week.[23]

The RBI has directed that 25 per cent of new branches have to be opened in URCs, that is, a rural (tier V and VI) centre that does not have a 'banking outlet' enabled with Core Banking Solution (CBS) for carrying out customer-based banking transactions. The new guidelines came into operation during the year under review.[24]

Table 2.7 shows the outreach of the commercial banking system as of 31 March 2018. During the two years since 31 March 2016 there has been an increase in the number of branches in semi-urban, urban and metropolitan areas even as the number of rural branches has declined. Indeed, the most significant increase has been in metropolitan areas. Nevertheless, when the change in 2017–18 is considered, there has been a small increase in the number of rural bank branches of SCBs from 48,232 to 49,384 branches.[25] Banks are not considering further expansion of branches in villages, since most banks are running at losses, and PCA directives in the case of PSBs bar them from opening branches in rural areas. The new definition of banking outlets in identified villages with BCs will allow banks to extend their branch network. So far banks have generally not notified BC outlets as branches, pending fulfilment of some requirements like accommodation, signage, etc.

At the same time, the number of metropolitan bank branches that had increased during 2016–17 from 22,187 to 26,781 has registered only a negligible increase from 26,781 to 26,961 during the year 2017–18.

Table 2.7: Branches of Scheduled Commercial Banks

	March 2015	March 2016	March 2017	March 2018
All SCBs	148	149	150	149
• RRBs	56	56	56	56
		No. of reporting offices		
Rural	48,033	49,902	48,232	49,384
Semi-urban	33,523	35,704	37,880	38,481
Urban	23,522	24,794	24,877	25,307
Metropolitan	20,785	22,187	26,781	26,961
TOTAL	125,863	1,32,587	1,37,770	1,40,133

Source: Reserve Bank of India, 'Quarterly Statistics on Deposits and Credit of SCBs'. https://dbie.rbi.org.in/DBIE/dbie.rbi?site=publications#!4. Accessed on 13 June 2018.

Progress of financial inclusion plans: Pace of growth of infrastructure arrested though ICT transactions rise steadily

Over the years, with the growth in outreach of the banking system and the provision of various types of banking outlets and other devices such as ATMs, e-kiosks, mobile branches, points of sale (POS) terminals, etc., the physical infrastructure for the conduct of banking operations has significantly improved. Table 2.8 provides a summary of the progress of the parameters tracked by the FIPs of banks, which represent the cross-section of banking products and channels.

Table 2.8: Financial Inclusion—Summary of Progress

Particulars	Year ending March 2014	Year ending March 2015	Year ending March 2016	Year ending March 2017	Year ending March 2018
Banking outlets in villages—Branches	46,126	49,571	51,830	50,860	50,805
1Banking outlets in villages—Branchless mode*	3,37,678	5,04,142	5,34,477	5,43,472	5,18,742
• BCs in villages less than 2,000 population				4,38,070	4,14,515
Banking outlets in villages—Total	3,83,804	5,53,713	5,86,307	5,98,093	5,69,547
Urban locations covered through BCs	60,730	96,847	1,02,552	1,02,865	1,42,959
BSBDAs through branches (in million)	126	210	238	254	247
BSBDAs through branches (in Rs billion)	273	365	474	691	731
BSBDAs through BCs (in million)	117	188	231	280	289
BSBDAs through BCs (in Rs billion)	39	75	164	285	391
Total BSBDAs (in million)	243	398	469	533	536
Total BSBDAs (in Rs billion)	312	4440	638	977	1121
OD facility availed in BSBDAs (in million)	6	8	8	9	6
OD facility availed in BSBDAs (in Rs billion)	16	20	14.8	17	4
KCCs (in million)	40	43	47	46	46
KCCs (in Rs billion)	3,684	4,382	5,131	5,805	6096
GCCs (in million)	7	9	11	13	12
GCCs (in Rs billion)	1,096	1,302	1,493	2,117	1498
ICT a/c BC transaction during the year (in million)	329	477	827	1,159	1489
ICT a/c BC transaction during the year (in Rs billion)	524	860	1,687	2,652	4292
ATMs of banks (public, private, foreign banks)			1,99,099	2,14,554	2,05,201
ATMs of India Post				982	0
ATMs of PBs					4,847
ATMs of SFBs				724	1,207
ATMS of RRBs			1,024	1,038	1,000*
ATMs of cooperative banks (both urban and rural)			4664	5,829	2,343**
White label ATMs			14,169	14,447	15,197

Notes: The branchless mode outlets include business correspondents (BCs), Automated Teller Machines (ATMs), Point of Sale (PoS) points, Ultra Small Branches (USBs) and mobile vans
BSBDA: basic savings and bank deposit account; OD: overdraft; KCC: Kisan credit card GCC: General Credit Card
*Excludes data for Gujarat, Maharashtra, Uttar Pradesh and West Bengal.
**Rural cooperative banks only.
ATM statistics for 2018 are as of June 2018 from https://rbi.org.in/SCRIPTS/StateRegionATMView.aspx. Accessed on 15 September 2018.
ATM statistics for RRBs and rural cooperative banks for 2018 are as of 31 August 2018, provided by NABARD.
Source: Reserve Bank of India, *RBI Annual Report, 2014, 2015, 2016, 2017* and 2018 (Mumbai: RBI), NPCI, NABARD.

This reveals that during 2017–18 the infrastructural gains registered over the previous years were arrested. A brief review of the performance of banks under the FIPs up to the year ending March 2018 reveals the following:

- *The number of banking outlets in villages* at the end of March 2018 was 5,69,547. Of this, the number of bank branches in villages by the end of March 2018 was 50,805, which represents a small decline from a figure of 50,860 in the previous year. This number is likely to go up in the future on account of the revised RBI guidelines for the definition of bank branches.
- *Branchless banking outlets in villages,* whose number had been growing at a brisk pace over the previous years, declined slightly from 5,43,472 at the end of March 2017 to 5,18,742 at the end of March 2018—a small drop of under 5 per cent. Issues related to branchless banking through through business correspondent agents (BCAs) are discussed more extensively in Chapter 3. Overall, this channel appears to have stabilised as a viable delivery mechanism for financial services. The number of BC outlets opened in urban locations during the year, however, appears to have registered a massive increase from 102,865 to 1,42,959.
- The *number of BSBDAs* at the end of March 2018 was 536 million, representing a net addition of only 3 million accounts. Of this, 54 per cent were facilitated through BCs. The massive increase in BSBDAs too appears to be easing off as saturation levels are reached throughout the country.[26] Earlier estimates of high levels of non-utilisation of these accounts have now given way to more modest figures of under 20 per cent of BSBDAs. Those availing of the overdraft facility are still only a small fraction of the total BSBDAs, that is, a little over 2 per cent of all such accounts as of the end of March 2018. This is one component of the PMJDY package that continues to remain grossly unimplemented.
- *Kisan credit card (KCC)* numbers also appear to have virtually stagnated at around 4.6 lakh over the past couple of years and the amount outstanding has only increased by about 4 per cent during 2017–18. In the year under review, these cards were to be converted into the more broad-based RuPay ATM cum debit KCCs (RKCCs). Conversion of KCCs into RKCCs will facilitate farmers to undertake financial transactions on the digital platform.[27] The use of RKCCs may increase the frequency of funds accessed by the farmer as there will be ease in withdrawing cash as and when required. This periodic withdrawal of small amounts will help in reducing the interest burden on the farmers and enable them to access credit as per their needs. However, the NABARD All India Rural Financial Inclusion Survey (NAFIS)[28] study 3 suggests that only 10.5 per cent of agricultural households had valid KCCs with progressively increasing coverage in the higher landowning size classes. Only 31 per cent of those with holdings of over 0.4 hectares and taking loans for agricultural purposes had valid KCCs.
- The *number of ATMs* has declined or at least stagnated for commercial banks, with only modest increases for other categories of financing agencies. Annexure 2.2 gives a sector-wise analysis of ATMs of public sector commercial banks for the quarters ending June 2017 and June 2018. Despite the addition to the numbers by new private banks, payments and small finance banks, all sectors—metro, urban, semi-urban and rural—registered a decline or virtually no increase in the number of ATMs. The small increase in the rural centres was more than accounted for by one PB, Fino Payments Bank, in the absence of which there would have been a decline both in the total number of ATMs of banks over this one-year period as well as in the number of ATMs in the rural areas.
- It is in the *number of ICT transactions by BCs* that there has been an impressive increase from 1,159 million for the year ending March 2017 to 1,498 million for the year ending March 2018, or an increase of over 29 per cent as compared to the previous year—which in turn had registered a 40 per cent increase over the period ending March 2016. Even more spectacular has been the value of transactions in these accounts that has increased by 62 per cent during 2017–18 to Rs 4,202 billion as compared to Rs 2,652 billion in 2016–17.

The parameters described above only partly cover the wide range of institutional initiatives and technological innovations in financial inclusion undertaken by leading public sector and private commercial banks towards building the infrastructure and fulfilling the objectives of the plans. A summary of the financial inclusion initiatives of some leading banks is given in Annexure 2.3. Most of these initiatives have been uncoordinated across banks with each bank favouring one or the other programme or campaign, partnership or device based upon its own corporate identity and strategy.

Table 2.9: Performance Indicators of Regional Rural Banks (as of 31 March) (in Rs crore)

Particulars	2017	2018
No. of RRBs	56	56
No. of branch networks	21,422	22,014
Owned fund	29,501	31,578
Deposits	3,71,910	4,00,459
Borrowings	51,588	63,344
Investments	2,10,984	2,33,936
Gross loan outstanding	2,26,175	2,52,669
CD ratio	60.81	63.09
Accumulated losses	1,147	1,829
RRBs in profit	49	45
Profit amount	2,604	2,625
RRBs in loss	7	11
Loss amount	386	1,005
Net position of profit	2,218	1,620
Gross NPA amount	18,255	24,059
Gross NPA (in per cent)	8.07	9.52
Recovery percentage (as of 30 June of previous year)	80.68	77.81
Net worth	29,115	29,749

Source: NABARD, Regional Rural Banks: Key Statistics as on 31 March 2018 (Mumbai: NABARD, 2018).

Regional Rural Banks

Performance during the year: Satisfactory but with slippage in profitability

Regional rural banks were established under the RRB Act, 1976 with a view to providing credit for the development of the rural economy. In the initial stages, they were seen as primarily catering to the below poverty line (BPL) population by lending to them for their investment needs. The recapitalisation of RRBs during 1994–2000 along with a reorientation towards profitable functioning helped to put the RRBs on a more or less sound footing. A process of amalgamation, which was started in 2005, resulted in the number of RRBs being brought down in two phases from a peak of 196 to the present level of 56 at the end of 31 March 2018. The 56 RRBs presently have, as of 31 March 2018, a branch network of 22,014, deposits of Rs 4,00,459 crore and gross loan outstanding of Rs 2,52,669 crore (Table 2.9).

Forty-five RRBs were in profit with overall profit being Rs 2,625 crore during 2017–18, while 11 RRBs were in loss (as against 7 RRBs during the previous year) to the extent of Rs 1,005 crore. The accumulated losses of the RRBs stood at Rs 1,829 crore. The net position of profit was thus Rs 1,620 crore. This was down from a figure of Rs 2,218 crore during the previous year.

The gross NPA percentage of the RRBs as a whole was 9.52 per cent as of 31 March 2018, as against 8.07 per cent the previous year.[29] Despite the slippage in terms of profits and NPAs, it can be said that in comparison with other financing agencies, their profitability, growth of credit and control of NPAs is better, especially as compared to commercial banks. This has been achieved despite 90 per cent of their lending being directed to the priority sector. Given their charter, cross-subsidisation of lending operations is not really possible; nevertheless, they have been able to show creditable performance.

Branch network and outreach: Overall increase, but decline in share of rural branches

When some of the parameters of financial inclusion are taken into account, it is seen that the RRB branch network has been growing at a steady pace in recent years, with the total numbers reaching 21,593 by 2017 and 22,014 by 2018 (Table 2.10).

Table 2.10: RRB Branch Network over the Years (According to Region)

	1996	2012	2013	2014	2015	2016	2017	2018
North	1,980	2,312	2,469	2,618	2,849	3,014	3,074	3,159
Northeast	667	696	696	721	822	849	870	879
East	3,610	3,796	3,836	4,057	4,424	4,467	4,616	4,502
Central	4,670	5,127	5,440	5,821	6,146	6,259	6,460	6,473
West	1,022	1,142	1,192	1,294	1,378	1,436	1,469	1,492
South	2,723	3,556	3,849	4,028	4,644	4,879	5,104	5,509
Total	14,672	16,629	17,482	18,539	20,263	20,904	21,593	22,014

Source: Reserve Bank of India, *Basic Statistical Returns of SCBs in India* (Mumbai: RBI, various years); NABARD, *Regional Rural Banks: Key Statistics as on 31 March 2018* (Mumbai: NABARD, 2018).

Table 2.11: RRB Branch Network over the Years (According to Location)

	2012	Share of RRBs in the banking network (2012) (in %)	2013	2014	2015	2016	2017	2018	Share of RRBs in banking network (2018) (in %)
Rural	12,263	36.23	12,850	13,609	14,644	15,606	14,862	15644	30.7
Semi- urban	3,192	11.82	3,362	3,569	4,011	3,846	4,710	4628	11.5
Urban	1,009	5.06	1,080	1,153	1,345	1,282	1,595	1414	5.1
Metro	165	0.74	190	208	260	170	426	328	1.1
Total	16,629	16.11	17,482	18,539	20,263	20,904	21,593	22014	14.8

Source: Reserve Bank of India, *Basic Statistical Returns of SCBs in India* (Mumbai: RBI, various years); NABARD, *Regional Rural Banks: Key Statistics* as on 31 March 2018 (Mumbai: NABARD, 2018).

At the same time, there has been a substantial growth in the ultra-small branches, which numbered 10,900 in 2017, especially in the relatively underbanked east, north and central regions. While the RRB bank network grew by over 32 per cent during the period 2012–18 from 16,629 to 22,104, its growth was lower than that of the overall banking system. Thus, its overall share in bank branches declined from 16.1 per cent to 14.8 per cent (Table 2.11).

Interestingly, the relative share of RRBs grew slightly over this period in the urban and metropolitan locations, rather than in the rural segment. This is further evidenced by the fact that the share of the RRB branch network in rural bank branches, in fact, declined substantially from 36.2 per cent in 2012 to 30.7 per cent in 2018. RRBs have tended to grow in urban areas rather than rural areas in the interest of viability and profitability at the expense of further deepening their outreach in rural areas towards inclusive financial services delivery.

The progress of RRBs in expanding their ATMs and debit-card network over the years has been slow; in fact, it reflects a level of stagnation during 2016–17. It will be seen that only about six RRBs accounted for around 80 per cent of the ATMs that had been launched by 2017 (Table 2.12). However, during 2017–18 at least five RRBs are understood to have made additions to the number of ATMs and a similar number launched their first set of ATMs.[30]

Table 2.12: ATM Networks of RRBs

S. No.	Name of the Bank	ATMs 2016	ATMs 2017
1.	Allahabad UP Gramin Bank	154	154
2.	Andhra Pradesh Grameena Vikas Bank	3	3
3.	Andhra Pragathi Grameena Bank	67	67
4.	Baroda Gujarat Gramin Bank	8	8
5.	Baroda Rajasthan Kshetriya Gramin Bank	10	10
6.	Baroda Uttar Pradesh Gramin Bank	9	9
7.	Chaitanya Godavari Grameena Bank	29	33
8.	Deccan Grameena Bank	2	2
9.	Dena Gujarat Gramin Bank	8	8
10.	Karnataka Vikas Grameena Bank	83	83
11.	Kashi Gomti Samyut Gramin Bank	43	43
12.	Kaveri Grameena Bank	1	1
13.	Kerala Gramin Bank	277	280
14.	Maharashtra Gramin Bank	10	4
15.	Malwa Gramin Bank	2	2
16.	Odisha Gramya Bank	25	25
17.	Pragathi Krishna Gramin Bank	250	249
18.	Prathama Bank	42	42
19.	Rajasthan Marudhara Gramin Bank	5	5
20.	Sutlej Gramin Bank	10	10
21.	Chhattisgarh Rajya Gramin Bank	0	0
22.	Sarva Haryana Gramin Bank	0	0
23.	Kaveri Grameena Bank	0	0
24.	Telangana Grameena Bank	0	0
25.	Tripura Gramin Bank	0	0
Total		1,024	1,038

Source: Inclusive Finance India Report 2017.

Overall performance: Steady progress but with areas of concern

Table 2.13 shows the overall performance of RRBs during the six years since the last round of consolidation. It may be observed that the net profit has tended to stagnate in recent years, and

Table 2.13: Performance of RRBs over the Years (Figures for March 31 of Each Year)

	2012	2013	2014	2015	2016	2017	2018
No. of RRBs	82	64	57	56	56	56	56
No. of branches	16,914	17,867	19,082	20,024	20,924	21,593	22,014
Net profit (in Rs billion)	18.86	22.73	26.94	29.21	22.06	29.49	26.25
Profit/loss-making RRBs	79/3	63/1	57/0	51/5	50/6	50/6	45/11
Deposits (in Rs billion)	1,863	2,054	2,333	2,730	3,135	3,718	4,005
Loans and advances (in Rs billion)	1,130	1,359	1,589	1,810	2,065	2,286	2,527
CD ratio (in %)	63.3	64.82	66.56	66	66	61	63.09
Share of CASA in deposits (in %)	58.51	57	56.88	52	51	53	53
Share of priority sector advances (in %)	80	86		84	87	90	90
Share of agricultural advance to total (in %)	53	63		59.5	64.3	68	69
Share of advances to small and marginal farmers (in %)					42.31	44.97	45.9
Advances to weaker sections (in %)					52.61	54.73	55.85
Gross NPA (in %)	5.03	6.08	6.09	6.15	6.58	7.71	9.52
Net NPA (in %)	2.98	3.59	3.52		3.94	4.73	3.77
Branch productivity (in million)				226	249	280	297
Staff productivity (in million)				53	59	60	72

Notes: CASA: current account savings accounts.
Source: Reserve Bank of India, Trend and Progress of Banking India (Mumbai: RBI, various years); NABARD, Financial Statements of RRBs (Mumbai: NABARD, 31 March 2017); NABARD, Regional Rural Banks: Key Statistics as on 31 March 2018 (Mumbai: NABARD, 2018).

the number of loss-making RRBs has increased. Deposits increased steadily to a level of Rs 4,003 billion, and loans and advances followed as well to Rs 2,527 billion, though with the credit:deposit (CD) ratio registering a not very impressive 63 per cent as of 31 March 2018.

Nevertheless, there has been a small increase in the share of agriculture, small and marginal farmers, and the weaker sections. The share of agriculture in the total portfolio of RRBs continues to be high and increasing, with the figure as of 2018 standing at 69 per cent. This has meant that there is pressure on RRBs to diversify their portfolio in order to avoid concentration risk. Still, with the advent of the SFBs, RRBs may also experience competition in this component of their portfolio.

The share of current account savings accounts (CASAs) in deposits has consistently been over 50 per cent in RRBs, though declining slightly, indicating access to low-interest borrowing by RRBs. However, this has been matched not by increased share of loans and advances but by the high level of investment in treasury bills; and in undertaking risk-free deployment of resources with sponsor banks. This in turn has served to limit the flow of loans to the originally intended beneficiaries of RRBs. As a result of this investment pattern, recourse to borrowings by RRBs has also been very limited with even NABARD refinance constituting no more than about 20 per cent of net loans and advances during 2017–18.

Further, in terms of their contribution to the PMJDY, introduction of BCs and digital operations, RRBs have tended to perform at a somewhat lower level than commercial banks.

Priority sector lending by RRBs: Less inclusive of small borrower segment

In this section, the achievement of PSL targets and other parameters related to financial inclusion is reviewed.

Table 2.14 shows the purpose-wise break-up of credit accounts of RRBs as of 31 March 2017, the latest date for which data is available. The PSL sector target of 75 per cent has been exceeded, and a large proportion of the RRB portfolio, that is, 64.41 per cent, is directed at agriculture. Of this, direct finance is 61.18 per cent. These figures have remained

Table 2.14: Purpose-wise Break-up of Credit Accounts of RRBs as of 31 March 2017

Purpose	No. of accounts (in million)	Relative % to total	Credit limit (in Rs billion)	Relative % to total	Amount outstanding (in Rs billion)	Relative % to total
I. Agriculture	17.18	71.24	1926.54	64.12	1479.60	64.41
1. Direct finance	16.23	67.28	1833.54	61.03	1405.36	61.18
2. Indirect finance	0.96	3.97	93.00	3.10	74.24	3.23
IV. Professional and other services	0.59	2.45	92.94	3.09	72.44	3.15
V. Personal loans	2.02	8.37	398.38	13.26	312.42	13.60
1. Housing	0.51	2.12	167.26	5.57	135.86	5.91
2. Consumer durables	0.06	0.27	11.77	0.39	8.03	0.35
3. Vehicles	0.13	0.52	31.34	1.04	23.32	1.02
4. Education	0.10	0.42	26.54	0.88	24.30	1.06
6. Others	1.22	5.05	161.48	5.37	120.90	5.26
Vi. Trade	1.53	6.36	166.23	5.53	130.05	5.66
2. Retail trade	1.47	6.09	157.19	5.23	124.27	5.41
VII. Finance	0.34	1.41	75.62	2.52	47.00	2.05
VIII. All others	2.45	10.16	344.70	11.47	255.53	11.12
Total bank credit	24.12	100.00	3004.41	100.00	2297.04	100.00

Source: Reserve Bank of India, *Basic Statistical Returns of SCBs in India*, Volume 46 (Table 5.5). Accessed at https://dbie.rbi.org.in/DBIE/dbie.rbi?site=publications on 21 June 2018.

virtually unchanged in relation to the previous year, with only a small decline in the percentage of direct finance. The high share of agriculture in the RRB portfolio is also, as noted earlier, a source of risk since it not only represents a concentration of the RRB portfolio in a particular sector, but also the geographical area of the state in which it functions. This leaves it open to a phenomenon such as debt waivers by state governments, having an adverse effect on the loan portfolio.

Credit: Decline in share of SBAs in outstanding loans

Data on the deployment of credit by RRBs is given in Table 2.15.

This data for the year ending 31 March 2017 has details of loans made to SBAs (of up to Rs 2,00,000), and sub-categories of loans (i) up to Rs 25,000 and (ii) in the range Rs 25,000–Rs 2,00,000. In the category of loans less than Rs 25,000 there is a steady decline in the number of such accounts, which as of 31 March 2017 stood at 5.45 million, or only 22.5 per cent of total accounts. The amount outstanding in such accounts too has steadily declined and has dipped sharply during the year 2016–17, to a total of Rs 89.23 billion or 3.88 per cent of total loan outstanding of RRBs.

In the next sub-category of SBAs—accounts with loan amount of Rs 25,000 to Rs 2,00,000—there has been a steady increase and the number of such accounts was 15.59 million on 31 March 2017. The amount outstanding too grew steadily to a total of Rs 1,107.14 billion or 48.20 per cent of total outstanding of RRBs. Thus, SBAs accounted overall for 21.04 million accounts or about 87.23 per cent of total RRB loan accounts. This too represents a steady decline over the past four years from 92.30 per cent of total accounts, even as the amount outstanding reached Rs 1,196.37 billion or 52.08 per cent of total outstanding of RRBs as of 31 March 2017. One cannot but reach the conclusion that within the RRB clientele, which would ordinarily constitute the lower segment of rural clients, the percentage as well as numbers of small borrowers with loans less than Rs 25,000 are steadily declining. The fall is not so great when the entire category of small borrowers with loans of under Rs 2,00,000 is considered, and the amount outstanding has actually increased. However, even the outstanding amount for SBAs as a percentage of total outstanding to RRBs has shown a substantial decline during the four-year period. This leads to the inescapable conclusion that RRB lending is steadily becoming less inclusive over the years, contrary to its original mandate.

Table 2.15: Details of Credit to Small Borrowal Accounts over the Years

	Year ending March 2013	Year ending March 2014	Year ending March 2015	Year ending March 2016	Year ending March 2017
Loan amount less than Rs 25,000					
Number of accounts (in million)	7.77	6.89	6.33	6.05	5.45
Percentage of total accounts	38.32%	32.07%	28.48%	25.92%	22.59%
Limit sanctioned (in Rs billion)	115.31	115.24	105.71	102.07	91.10
Percentage of total amounts	5.27%	4.98%	4.84%	3.74%	3.03%
Amount outstanding (in Rs billion)	142.52	108.92	102.07	109.83	89.23
Percentage of total outstanding	10.49%	6.86%	5.63%	5.31%	3.88%
Loan amount Rs 25,000 to Rs 2,00,000					
Number of accounts (in million)	10.95	12.6	13.62	14.69	15.59
Percentage of total accounts	53.98%	59%	61.29%	62.89%	64.63%
Limit sanctioned (in Rs billion)	794.58	915.14	1014.79	1108.58	1217.91
Percentage of total amounts	36.30%	40%	46.42%	40.58%	40.54%
Amount outstanding (in Rs billion)	696.36	812.91	912.86	1,032.21	1,107.14
Percentage of total outstanding	51.26%	51%	50.37%	49.90%	48.20%
Total up to Rs 2,00,000					
Number of accounts (in million)	18.72	19.49	19.95	20.75	21.04
Percentage of total accounts with RRBs	92.30%	91%	89.77%	88.80%	87.23%
Limit sanctioned	909.89	1,030.37	1,120.5	1,210.64	1,309.01
Percentage of total amounts	41.56%	44.52%	51.25%	44.31%	43.57%
Amount outstanding (in Rs million)	838.89	921.84	1,014.93	1,142.03	1,196.37
Percentage of total outstanding with RRBs	61.75%	58.02%	56.00%	55.21%	52.08%

Source: Reserve Bank of India, *Basic Statistical Returns of SCBs in India,* Volume 46 (Table 4.7) (Mumbai: RBI, 2018).

3.2.4.2 Deposits: Term deposits more significant

Table 2.16 gives the data on deposits of RRBs according to the location of branches as of March 2017.

While RRB-wise data is not available, it is observed that the bulk of the accounts are savings accounts followed by term deposit accounts, with a total of 204.57 million savings accounts with

Table 2.16: Deposits of RRBs Classified According to the Location of Branches as of March 2017

Type of deposits		Current		Savings		Term		Total	
Population group	No. of offices	No. of accounts (in thousand)	Amount (in Rs billion)	No. of accounts (in thousand)	Amount (in Rs billion)	No. of accounts (in 'thousand)	Amount (in Rs billion)	No. of accounts (in 'thousand)	Amount (in Rs billion)
Rural	14,775	1,120	38	1,46,151	1,178	10,966	769	1,58,237	1,985
Semi-urban	4,655	690	29	47,174	481	4,630	432	52,494	942
Urban	1,514	322	25	9,468	190	2,240	359	12,029	575
Metro	414	39	9	1,780	38	371	108	2,191	156
All India	21,358	2,171	101	2,04,573	1,887	18,207	1,669	2,24,951	3,657

Source: Reserve Bank of India, Basic Statistical Returns of SCBs in India, Volume 46 (Table 3.3). Accessed at https://dbie.rbi.org.in/DBIE/dbie.rbi?site=publications on 21 June 2018.

Table 2.17: Deposits of RRBs Classified According to Ownership of March 2016 and 2017

	March 2016		March 2017		March 2016		March 2017	
	Accounts (in million)	% of total	Accounts (in million)	% of total	Amount (in billion)	% of total	Amount (in billion)	% of total
Male	105	50.7%	107	48%	1,578	51.7%	1,878	51.4%
Female	61	29.6%	70	31%	692	22.7%	860	23.5%
Institutions	41	19.8%	48	21%	785	25.6%	919	25.1%
Total	207	100.0%	225	100%	3,055	100.0%	3,657	100.0%

Source: Reserve Bank of India, *Basic Statistical Returns of SCBs in India*, Volume 46 (Table 1.20). Accessed at https://dbie.rbi.org.in/DBIE/dbie.rbi?site=publications on 21 June 2018.

deposits of Rs 1,887 billion, and 18.21 million term deposit accounts with deposits of Rs 1,669 billion. However, while the number of savings accounts is over 11 times the total number of deposit accounts, the total amount of term deposits is nearly as much as the amount in savings deposit accounts. Rural deposit accounts constitute 70 per cent of total deposit accounts but only 52 per cent of the total amount in these accounts. Thus, nearly half the deposits of RRBs are mobilised from semi-urban, urban and metropolitan areas.

The ownership of deposit accounts in RRBs too displays an interesting, if expected, pattern (Table 2.17). As of March 2017, 48 per cent of deposit accounts were owned by men and 31 per cent by women, with around 21 per cent of accounts being owned by institutions. The corresponding shares in the amount of deposits were 51 per cent, 24 per cent and 25 per cent.

RRBs and financial inclusion: Diverse initiatives undertaken

The RRBs involved are all engaged in their own innovative efforts at financial inclusion. They note that financial inclusion is not new and has always been a part of their work and objectives. As in the case of commercial banks, RRB schemes, campaigns and products represent a rich diversity in design and intent.

Apart from standard savings and credit products, RRBs have also introduced life, health and livestock insurance products developed by their own sponsor banks or in partnership with other service providers. It is inevitable that their approach, innovations and the technology adopted are all influenced by the views and strengths of the sponsor bank. Thus, the RRB of a sponsor bank that had introduced doorstep banking has also initiated doorstep collection of savings in villages (see below) and direct lending to individuals instead of through SHGs as a means of financial inclusion. Where technology has been the strength of a sponsor bank, it has reflected in multiple products developed at the RRB level. Where large-scale lending operations involving SHGs are a sponsor bank's hallmark, these are carried over to the RRB's approach.[31]

Uttar Bihar Grameen Bank (UBGB), one of the largest RRBs in terms of branches and area covered, has been involved in a high degree of innovation with respect to BC operations. It has also developed a host of innovative cards for different sections of its clientele, for example, MUDRA card and fisheries card. It has also been very active in financial literacy in a relatively backward region. The UBGB has been operating ultra-small branches and BC centres called Sunehra Sapna Kendras with a viable business model. Its Samriddhi 400 programme ensures a minimum level of remuneration of Rs 10,000 for Bank Mitras.

Kashi Gomti Samyut Gramin Bank took the national lead in the introduction of IT-based applications. It was the first Gramin bank to become fully operational on the CBS platform, start interoperable ATM facility, introduce the fully indigenous RuPay ATM cards and initiate mobile banking. It has thus been at the cutting edge of various technological innovations in RRBs. It was also the first Gramin bank to introduce the solar microgrid and integrated (light and stove) energy system.

In the case of Karnataka Vikas Grameena Bank (KVGB), the Pygmy Deposit Scheme of Syndicate Bank, which used to provide doorstep services has been enhanced under the Vikas Jan Shakti (VJS) into a scheme for daily collection of loan repayments and savings deposits. The BC channel too has incorporated this dual function in the interest of BC income and viability. The scheme is being implemented through NDAs (Nirantar Deposit Agents) who were part of the recurring deposit scheme of the Syndicate Bank (sponsor bank of KVGB)—the Pygmy Deposit Scheme of yesteryears. Now it has become a loan-linked deposit scheme. KVGB also started a financial literacy helpline through a tie-up with IndianMoney.com. Thirty modules were prepared with pre-recorded messages by celebrity voices providing information on schemes according to caller requirements.

The Andhra Pradesh Grameena Vikas Bank viewed the SHG structure as appropriate for financial inclusion but one that was not being utilised properly. The bank looked to BCs to stabilise the SHG system. This, in effect, involved a different type of bank–SHG linkage relationship—through the BC as intermediary—as in the case of individual clients. The Gramin Bank of Aryavart in UP and the Narmada Jhabua Gramin Bank pioneered the use of SHG members as Bank Sakhis or BCs—a pilot that has since been extended to several states under the National Rural Livelihoods Mission. In fact, RRBs have been the agencies that have enabled the tie-up of the SHG programme with the bank–BC relationship and the financial inclusion project.

NABARD for its part has also been supporting RRBs through a wide range of capacity building measures and technical support. Box 2.1 provides an example of the micro ATM-based operations facilitated by NABARD and Kerala Gramin Bank.

Box 2.1: BCs Equipped with Micro ATMs in Rural Kerala

NABARD funded Kerala Gramin Bank to equip BCs with micro ATMs at 50 BC points in rural Kerala. Tablet micro ATMs, thermal printers and fingerprint scanners with GSM SIM cards were provided at BC points serving 45 villages; and Aadhaar- and card–based transaction services were enabled either through fingerprint or one-time password (OTP).

The bank's BCs are usually located outside the branches for providing banking services to their clients such as withdrawal of government payments like MNREGA wages. Some BCs have set up an office using their own resources at a location convenient for the clientele. They also provide doorstep banking services. Micro ATMs support real-time transactions such as account opening and cash deposit. The transactions on these 50 tablet-based micro ATMs are given below.

No. of accounts opened	Deposit		Withdrawal		Funds transfer	
	No.	Transaction amount (in Rs)	No.	Transaction amount (in Rs)	No.	Transaction amount (in Rs)
7,596	1,64,875	22,26,04,765	55,851	21,81,25,114	2,793	19,04,986

Aadhaar-based transactions have become more popular than card-based ones due to the facility of secured biometric authentication and ease of transactions across bank accounts.

Source: NABARD, *NABARD Annual Report 2017–18* (Mumbai: NABARD, 2018). Information provided by the Department of Financial Inclusion and Banking Technology, NABARD in June 2018.

Amalgamation, recapitalisation and privatisation: Challenges and prognosis for RRBs

Notwithstanding their contribution to financial inclusion, as far as RRBs are concerned, there are three simultaneous processes of rationalisation and consolidation that are under way, namely, amalgamation, recapitalisation and privatisation or commercialisation through dilution of the capital ownership structure. Overall, however, there is the inescapable conclusion that these processes singly and collectively could serve to further distance RRBs from their original mandate.

As of 31 March 2017, five RRBs—Utkal Grameen Bank, Madhyanchal Gramin Bank, Ellaquai Dehati Bank, Nagaland Rural Bank and Sutlej Gramin Bank—were flagged for recapitalisation. Recapitalisation assistance of Rs 422.18 crore for these banks, with a Government of India (GoI) share of Rs 211.09 crore, was recommended by NABARD to the GoI. During 2017–18 the GoI released recapitalisation amount of Rs 5.51 crore to three RRBs—Ellaquai Dehati Bank (Rs 2.60 crore as the residual amount of the GoI share sanctioned during 2015–16), Manipur Rural Bank (Rs 2.33

crore) and Arunachal Pradesh Rural Bank (Rs 0.58 crore of the GoI share of recapitalisation assistance of Rs 3.05 crore).[32]

The government on 4 July 2018 approved the extension of recapitalisation support to RRBs, whose capital to risk-weighted assets ratio (CRAR) was below 9 per cent during three years from 2017–18 to 2019–20, in order to maintain the minimum prescribed CRAR level and to enable them to play a greater role in financial inclusion. Out of the government's share of Rs 1,450 crore for the recapitalisation scheme, Rs 1,107.20 crore had been released till March 2017. The remaining Rs 342.80 crore will be released during the three-year period.[33] Four RRBs did not have the target minimum CRAR of 9 per cent as of 31 March 2018 and will be due for recapitalisation in the coming years.

The process of amalgamation and consolidation of RRBs, which had been stalled during the past several years, is to be resumed with another round of mergers being planned by the government. The number of RRBs is to be brought down further to 38. A roadmap has been prepared by which 33 RRBs spread across 11 states will be brought together into 14 banks.[34] The third phase of the amalgamation process is being undertaken to enable RRBs to cut overheads, improve their capital and use of technology, and help them achieve scale efficiency and higher productivity. The merger is envisaged across sponsor banks with the intention of consolidating RRBs at the state level. Thus, three RRBs of Gujarat are to be brought under the aegis of the SBI. Two RRBs of Tamil Nadu would then come under the Indian Bank. Amalgamation across sponsorship banks is also being attempted in Haryana and Uttar Pradesh. The move for the further merger of RRBs, however, has been described by the All India RRB Officers' Association as a regressive move which will create umpteen problems for rural people and hamper efforts towards providing better banking services for them.[35] They instead favour recapitalisation and consolidation through a merger of RRBs with their respective sponsor banks.

Despite their satisfactory performance according to conventional indicators, there are some disquieting features of the financial operations of RRBs. They undertake substantial investments in government securities and sponsorship banks such that a large proportion of deposits mobilised are not lent to the intended beneficiaries in rural areas. For example, as of 31 March 2018, investments were Rs 2,33,936 crore as against Rs 2,52,669 crore of gross loan outstanding. The credit deposit ratio too was a disappointing 63.09 per cent. The investment–deposit ratio, on the other hand, was as high as 57 per cent as of 31 March 2018.

Keeping aside questions regarding their current financial and operational practices, the role of RRBs in financial inclusion policy is somewhat unclear and nebulous even as new entities such as SFBs and PBs are being created to function in the rural banking space. The implementation of 'differentiated banking' raises the question of how the activities of these entities with overlapping functions and clientele as RRBs would impact the functioning of the latter. It would seem that the proposals for further amalgamation of RRBs into state-level entities could further distance them from their original mandate and clientele.

The amendment to the RRB Act, passed in April 2015, further facilitated raising the share capital of RRBs from Rs 5 crore to Rs 2,000 crore, and infusing capital from sources other than the present owners to the extent of 49 per cent.[36] The proposed changes were expected to pave the way for privatisation and commercialisation of RRBs, which would ignore the very purpose of their birth, and help to further distance the rural poor from access to institutional credit. However, these changes do not appear to have resulted thus far in sponsor banks moving in the direction of initial public offerings of shares and usher in greater private ownership.

In his union budget 2018–19 speech, Finance Minister Arun Jaitley had proposed to allow strong RRBs to raise capital from the market to enable them to increase their credit to the rural economy. It is understood that draft guidelines for initial public offerings (IPOs) for RRBs have been prepared by NABARD, and the government has identified four or five RRBs for listing on stock exchanges. The guidelines cover details such as the quantum of stake dilution, instruments to be floated, and category of possible investors in the public issue. A public issue is likely during the financial year 2018–19. In assessing the suitability of RRBs for accessing the market for growth capital, NABARD will be taking into account profitability, return on assets, return on expenses, etc. The guidelines are sponsor-bank neutral, though it is understood that RRBs promoted by the SBI, Indian Bank and Punjab National Bank are in the fray. The following RRBs are understood to be in the running for issuing IPOs: Kerala Gramin Bank, Prathama Bank (Uttar Pradesh), Andhra Pragathi Grameen Bank, and Baroda Rajasthan Kshetriya Gramin Bank. Andhra Pradesh Grameena Vikas Bank (APGVB), promoted by the SBI, had also been a contender for raising capital through an IPO. It has since received notice from the government for its bifurcation, whereby the Telangana operations will merge with the Telangana Grameena Bank in five districts of the state. APGVB will be restricted to three districts of Andhra Pradesh.

In the budget of 2018–19 it had also been proposed that RRBs be allowed to raise funds for lending not only through IPOs but also through issue of bonds. RRBs have thus far not been allowed by the RBI to issue bonds, unlike commercial banks and cooperative banks. The Department of Financial Services has constituted a committee on the raising of capital by RRBs. As such, developments on the future direction of RRBs are hardly a subject of public debate or even apparently of substantive consultations with the bank staff. The RRBs of today are scarcely recognisable from the more local banks intended for providing services to families well below the poverty line. It is far from clear how privatisation as envisaged under the RRB Act with its objectives of professionalisation and efficiency will serve to restore the original mission and clientele of RRBs.

Three issues outstanding for RRBs are governance, technology and human resources. Technology development is moving fast, and it is a problem for RRBs to cope. Thus, according to NABARD sources, only 36 RRBs have introduced mobile banking and only 10 to 12 RRBs offer internet banking. The RBI requirement is that the technology should be robust. Besides, there is competition from private players, including SFBs, which as yet have only a small fraction of RRB business.

The purpose of mergers is to facilitate cross-subsidisation within the geographical area of the states. However, merger brings with it the issue of differing banking culture across sponsor banks. As regards human resources, parity in pay scales for RRB employees has had implications for profit. However, it has enabled recruitment of competent personnel. NABARD refinance has also become more expensive and the average cost of funds for RRBs has gone up.

Towards greater financial inclusion, RRBs are engaging BCs on a large scale. Where the SBI is a sponsor bank it is engaging retired officers as BCs. On 18 May 2017, the RBI introduced a relaxation in commercial bank branch norms through the designation of 'banking outlets', which function for four to five hours a day through BCs. A similar relaxation is being demanded for RRBs.

Overall, it would appear that both the proposals for differentiated banking and universal banking by adopting a multi-tiered approach have given little thought to the role and place of RRBs. In fact, the newly evolving focus on financial services to medium-scale enterprises and middle-income groups could mean that not only RRBs but also the new SFBs could direct their products more to the bankable entrepreneurial section of the not-so-poor.

Though the merger of RRBs is supported on grounds of the reduction in overheads and the optimal use of technology, the question arises whether consolidation and centralisation will not be detrimental to the customer interest. The process of merger seems to have been carried out without consulting the boards of the RRBs or the respective state governments.[37] This is particularly unacceptable because RRBs have links and relationships with the sponsor banks, which get uprooted and undermined as a result. A case is in fact being made for first divesting a share in the banks to new investors who could then look at mergers and acquisitions based on the market needs, rather than have government bureaucrats determining the fate of these commercial and market-based institutions.[38]

Ironically, the clamour of RRBs has been for a level playing field with commercial banks and towards greater freedom in their operations, which implies a move to increasingly serve the urban sector. However, they are handicapped, being saddled with high pay scales and human resource constraints, as well as greater priority sector commitments. Given the new developments, RRBs could soon end up being neither regional nor rural banks.

Rural Cooperatives and Financial Inclusion

The *Inclusive Finance India Report* for 2017 raised the question whether it is meaningful to report the progress and state of play in regard to the rural cooperative structure. As represented by state cooperative banks (StCBs) and district central cooperative banks (DCCBs) operating primarily through the short-term credit channel or primary agricultural societies (PACS), cooperatives are nevertheless an integral part of the banking system in India, contributing to financial inclusion and the development of agriculture and the rural economy. As of 31 March 2017 there were 33 StCBs and 370 DCCBs operating in the country. Along with 95,595 PACS, they constitute a formidable network and delivery channel for financial services that rival the network of commercial and regional rural bank branch outlets.

The cooperative credit structure is basically a three-tier structure that largely finances short-term credit needs. All cooperative banks are now on the CBS platform and are thus technologically enabled to be part of the FIPs of the banking system. Data provided by NABARD for 31 August 2018 reported that 393 cooperative banks were on the CBS and operated 2,343 rural ATMs. There is a compelling need to include cooperative banks in the FIPs. PACS are not banking entities within the RBI framework and only some of them accept deposits. The cooperative structure has not seriously been seen as contributory to the financial inclusion project even as SFBs and PBs and the recently launched postal bank enter the rural banking space. However, they can be incorporated within the framework as and when PACS are brought into the ambit of the CBS. Apart from the delivery of working capital loans for agricultural and non-agricultural activities through PACS, DCCBs have been active in lending to SHGs directly and through PACS, as pioneered by the Bidar Central Cooperative Bank and replicated in most DCCBs of Karnataka and other states such as West Bengal. The cooperative banks contribute a respectable 14.9 per cent to the number of SHGs saving with banks and over 9 per cent of SHGs borrowing from banks. For all the ills of cooperative banks, their NPAs for this channel are only about 7.5 per cent, not significantly higher than the average for all banks of a little over 6 per cent. At present, some PACS are also functioning as BCs of commercial banks, but it is not acceptable for them to act as BCs of cooperative banks in view of the conflict of interest. However, non-credit societies such as milk federations and fishery cooperatives are acting as financial intermediaries of DCCBs and StCBs. A fuller discussion of the outreach and performance of the rural cooperative structure follows.

Primary agricultural cooperative societies: Only two-thirds are viable

NABARD does not collect data for PACS; it is collected by the National Federation of State Cooperative Banks Ltd (NAFSCOB), the common forum for StCBs to address problems of banking and cooperative credit, apart from liaising with the state and central governments, the RBI, NABARD and other financial institutions on behalf of member banks, and contribute to policy decisions. The latest data is for the year March 2017.

The number of PACS in India as of March 2017 was 95,650 (Table 2.18). This represents a small increase over the previous year's figure of 93,490. The share of the western region was the largest with 29,780 PACS. The eastern region contributed the next largest share of PACS with 18,570. Of the total number of PACS only 64,440 were viable, that is, two-thirds of the total PACS. Around another 18,100 PACS were potentially viable. Another 8,850 PACS were multipurpose societies with the remaining dormant or defunct. In any event a fair proportion of PACS were viable and functional and a significant percentage potentially viable. In view of this, the PACS network represents a part of the financial infrastructure that needs to be nurtured rather than neglected.

Further analysis shows that PACS have a membership of 131.25 million (Table 2.19) It is observed that a significant proportion of members (over 75 per cent) are small and marginal farmers (and others) along with another 5 per cent membership of rural artisans. While Scheduled Caste (SC) and Scheduled Tribe (ST) members are recorded as exclusive to the two farmer categories, the coverage of what can be described as the relatively deprived sections of rural society, though not necessarily the poorest, can be inferred to be reasonably high. In terms of membership the southern region leads, followed by the eastern region.

Table 2.18: Number of PACS as of March 2017 (in '000s)

Region	Total PACS	Viable PACS	Potentially viable PACS	Dormant PACS	Defunct PACS	Others
Central	13.39	10.78	1.99	0.39	0.16	0.07
Eastern	18.57	14.12	2.86	0.58	0.41	0.59
Northeastern	3.52	1.95	0.41	0.67	0.38	0.11
Northern	15.54	5.76	2.18	0.12	0.10	7.38
Southern	14.79	10.82	2.96	0.32	0.13	0.56
Western	29.78	21.00	7.70	0.61	0.34	0.14
Total	95.60	64.44	18.10	2.68	1.53	8.85

Source: NAFSCOB, 'Performance of PACS 2016–17'. http://nafscob.org/pacs_f.htm. Accessed on 8 August 2018.

Table 2.19: Membership Details of PACS as of March 2017 (in million)

	Membership	Scheduled castes	Scheduled tribes	Small farmers	Rural artisans	Marginal farmers and others
Central	8.00	2.93	1.15	2.34	0.28	1.30
Eastern	28.49	2.55	3.38	7.92	0.72	13.91
Northeastern	3.69	0.48	0.74	0.85	0.11	1.50
Northern	19.77	1.65	1.02	4.79	0.83	11.48
Southern	53.17	6.28	1.92	19.85	5.14	19.99
Western	18.13	1.11	1.10	4.49	0.53	10.90
Total	131.25	15.00	9.32	40.25	7.60	59.08

Source: NAFSCOB, 'Performance of PACS 2016–17'. http://nafscob.org/pacs_f.htm. Accessed on 28 September 2018.

Table 2.20: Position of Advances and Overdues from PACS as of March 2017 (in Rs billion)

	Loans disbursed	Loans outstanding	Demand	Collection	Balance	Overdues (in %)
Central	55.3513	55.1379	72.0274	49.5525	22.4749	31.20
Eastern	82.9154	76.2639	94.8221	68.6798	26.1422	27.57
Northeastern	0.3205	0.7629	0.5541	0.2371	0.317	57.21
Northern	388.9912	329.9617	420.1942	210.3948	209.7994	49.93
Southern	1,221.8875	990.1588	1,072.0273	944.4634	127.5638	11.90
Western	257.318	252.3074	345.0133	198.3807	146.6325	42.50
Total	2,006.7839	1,704.5925	2,004.6383	1,471.7085	532.9298	26.58

Source: NAFSCOB, 'Performance of PACS 2016–17'. http://nafscob.org/pacs_f.htm. Accessed on 8 August 2018.

Table 2.20 shows the position in respect of advances and overdues of PACS as of March 2017. Loans disbursed were in excess of Rs 2,000 billion and loans outstanding over Rs 1,700 billion. However, the overdues percentage was a high 26.58 per cent. The disappointing feature of this portfolio performance was that with the exception of the southern region the overdues percentage in the rest of the country was above the national average. It was in excess of 40 per cent in the northern, northeastern and western regions. The figure for overdues percentage as of March 2016 by comparison was 19 per cent. Thus, there has been a clear deterioration in the portfolio performance during 2016–17. In some respects, this was anticipated in view of the demonetisation undertaken in November 2016. A negative impact on repayments to the cooperative sector was generally expected since it was not allowed, unlike other financing agencies, to collect old currency during the stipulated period. This affected both collections in the immediate aftermath and the repayment discipline in general.

Table 2.21: Details of Performance of PACS and Physical Infrastructure, March 2016

	Profit-making PACS	Loss-making PACS	PACS with godowns	Number of villages covered	Staff strength	Societies with full-time secretary
Central	6,689	4,097	12,007	1,67,153	24,521	4,095
Eastern	4,262	9,810	11,459	1,94,105	37,889	12,006
Northeastern	708	829	1,205	32,522	8,529	2,160
Northern	11,063	4,316	6,532	78,401	23,327	9,108
Southern	8,909	5,366	12,159	89,825	64,955	13,415
Western	14,955	13,618	9,281	42,882	13,342	6,612
Total	46,586	38,036	52,643	6,04,888	1,72,563	47,396

Source: NAFSCOB, 'Performance of PACS 2016–17'. http://nafscob.org/pacs_f.htm. Accessed on 8 August 2018.

Table 2.21 details the performance of PACS and the physical infrastructure as of March 2017. During 2016–17, 46,586 PACS were making profits, while 38,036 were going into losses. This represents a slightly better performance than the previous year when 44,703 PACS were in profit. Interestingly, the proportion of profit-making PACS is not very different across regions regardless of their portfolio performance during the year.

In terms of outreach and physical infrastructure (Table 2.21), PACS covered 6,04,888 villages with a staff of 1,72,563, representing no significant change from the previous year. And 52,643 PACS or a significant majority had godowns.

Overall, while the performance of PACS was not satisfactory, they continued to be a last-mile point of contact with actual and potential customers of financial services. Over the years, PACS have received support from NABARD to develop them as multi-service centres as also to facilitate their upgrade to the CBS platform. In this manner, they continue to contribute to financial inclusion and could with appropriate support play a more diversified role either within the existing framework or as BCs and extended arms of a restructured cooperative sector in their respective states.

NABARD provides both financial as well as technical support to rural cooperative credit institutions. Financial support is provided through the Cooperative Development Fund (CDF), while technical, capacity building and knowledge-sharing support comes from the Centre for Professional Excellence in Cooperatives (C-PEC). Besides these, NABARD also provides assistance to PACS Development Cells (PDC). Support under CDF enables these institutions to achieve better governance and managerial efficiency, human resource capability, analytical capability, management information system (MIS), etc. Across all tiers of credit structures, the CDF support by way of grant, soft loan or grant-cum-soft loan assistance amounted to Rs 18.84 crore in 2017–18 (cumulative support stood at Rs 176.23 crore, as of 31 March 2018).[39]

C-PEC was instituted at Bankers' Institute of Rural Development (BIRD), Lucknow to coordinate training efforts of various cooperative training institutes (CTIs) and build professional and technical competence in cooperative credit institutions. As of 31 March 2018, C-PEC membership stood at 7,062, which included 43 accredited CTIs, 26 StCBs, 1 State Cooperative Agricultural and Rural Development Bank (SCARDB), 1 state cooperative union, 211 DCCBs, 5,421 PACS and 1,359 individuals.

PDCs are created in DCCBs and StCBs to undertake capacity building and strengthening of PACS through training, handholding, guiding, exposure visits and other suitable interventions so that these agencies can deliver financial and non-financial services in an efficient and viable manner to their members. As of 31 March 2018, 94 PDCs had been provided a total financial assistance of Rs 14.91 crore.[40]

State and district cooperative banks

The performance of StCBs during 2015–16 and 2016–17 is presented in Table 2.22. As the loan portfolio of StCBs is largely dependent on the loan portfolio of DCCBs, loans had shown a modest growth in spite of appreciable increase in deposits and borrowings.

Table 2.22: Performance of State Cooperative Banks

	As of 31 March 2016	As of 31 March 2017	Growth (%)
Total number of banks	33	33	0
Share capital (in Rs crore)	5,647	5,161	–9
Reserves (in Rs crore)	7,334	10,294	40
Deposits (in Rs crore)	1,09,257	1,22,039	12
Borrowings (in Rs crore)	68,775	80,892	18
StCBs in profit	28	31	-
Profit (in Rs crore)	714	970	-
StCBs in loss	5	2	-
Loss (in Rs crore)	115	18	-

Source: NABARD, NABARD Annual Report 2017–18 (Mumbai: NABARD, 2018).

Table 2.23: Performance Indicators of DCCBs

	DCCBs			% change FY16–17
	2014–15	2015–16	2016–17	
Number of banks	370	370	370	0
Share capital (in Rs billion)	130.45	160.08	186.74	17
Reserves (in Rs billion)	135.14	143.56	197.66	38
Deposits (in Rs billion)	2,621.14	2,915.99	3,309.04	13
Borrowings (in Rs billion)	811.54	818.91	914.38	12
Investments (in Rs billion)	1,360.34	1,534.89	1,846.34	20
Total loans outstanding (in Rs billion)	2,229.77	2,368.52	2,526.55	7
Number of banks in profit	308	318	315	-1
Amount of profit (in Rs billion)	17.48	16.85	16.67	-1
Number of banks in loss	62	52	55	6
Amount of losses (in Rs billion)	11.03	5.67	7.57	34
Gross NPA (in Rs billion)		223.74	264.15	
NPA % of loan outstanding as of 31 March		9.4	10.45	

Source: NABARD, *NABARD Annual Report 2017–18* (Mumbai: NABARD, 2018).

At the aggregate level, the percentage of NPAs to loans outstanding in respect of StCBs reduced to 4.08 per cent as of 31 March 2017 as against 4.50 per cent as of 31 March 2016. Region-wise analysis showed that NPA levels in percentage terms of the StCBs in the central, northeastern and western regions were higher than the all-India level.

The comparative performance of DCCBs during 2015–16 and 2016–17 is given in Table 2.23.

Notwithstanding a proportionately higher increase in borrowings and deposits (13 per cent), loan growth among DCCBs was only 7 per cent during 2016–17. DCCBs as a whole reported a net profit of Rs 910 crore during 2016–17. However, accumulated losses increased by 10 per cent from the previous year to Rs 5,242 crore.

The average gross NPAs for DCCBs across India increased from 9.4 per cent as of 31 March 2016 to 10.45 per cent as of 31 March 2017. This was a reversal in trend because NPA as a percentage of loans outstanding had been declining consistently from 2013 to 2016. The increase in NPAs could possibly be attributed to the effects of demonetisation as also the RBI imposition debarring DCCBs from accepting or exchanging scheduled bank notes (SBNs), that is, the old currency, with effect from 21 November 2016. As a result, despite several representations from NAFSCOB, Rs 147.53 crore of SBNs held by DCCBs still could not be deposited with the RBI as of the end of financial year 2017–18.[41]

Due to concerted efforts by NABARD, and with the support of state governments, 340 banks could achieve the mandated CRAR of 9 per cent. In comparison to 110 non-complying banks as of 31 March 2016, 30 banks did not comply with the 9 per cent CRAR norm as of 31 March 2017.[42]

Cooperative banks and financial inclusion: Also making a contribution

Apart from its role in short-term credit provision by way of working capital for agriculture, the cooperative credit structure is a little known contributor to microfinance and financial inclusion.

As in several other states such as Karnataka and West Bengal, PACS in Rajasthan too are lending to SHGs for economic activities (Box 2.2). The SHG loan limit ranges from Rs 50,000 to Rs 3 lakh. According to Rajeevika, the Rajasthan State Rural Livelihoods Mission, their SHGs are of good quality and will ensure 100 per cent recovery. PACS, acting as BCs, have also opened accounts under MNREGA and Bhamashah Yojna for those beneficiaries covered under the scheme. Apart from PACS, which have been working as BCs for a long time, E-mitras are also working as BCs on behalf of the Rajasthan State Cooperative Bank (RSCB).[43]

Box 2.2: Initiatives of DCCB Banks and PACS in Karnataka

In the state of Karnataka Rs 3,450 crore is outstanding through PACS at 4.5 per cent rate of interest. PACS are also lending to SHGs in almost all districts. They are entitled to lend to Mahila societies through amendment in by-laws, as pioneered by the Bidar Central Cooperative Bank. Around 70 per cent of DCCB loans are to societies and about 30 per cent to SHGs. Almost all DCCBs are on CBS. PACS in a few districts, for example Bagalkot, South Canara and Bidar are on CBS but face network problems. A few PACS are acting as BCs. SHG lending accounts for about 5 per cent of PACs operations. PACS are also assisting in enrolling members under the PMJDY, PMSBY and Pradahn Mantri Fasal Bima Yojana (PMFBY).

The performance of the DCCBs in SHG lending has been very good with very high savings mobilisation: as much as 40 per cent of loans disbursed and only 2 per cent NPAs. Around 2,62,000 SHGs have been formed, of which 39,000 are new and 78,000 are credit-linked. DCCBs are engaged in SHG formation, linkage and nurturing, and receive NABARD training for establishment of financial literacy centres (FLCs). Eight DCCBs have FLCs. Besides, National Rural Livelihoods Mission (NRLM) is funding NGOs for SHG formation with the support of Rs 3,000 per SHG, along with interest subvention. Loan waivers because of political interference are a source of problem. Sugar prices have been low for two years, only Rs 26 per quintal, resulting in 34 per cent NPAs in the sugar industry.

Source: B. Jinesh and Gayathri, Karnataka State Cooperative Bank (KSCB), Bengaluru, discussions with the author, June 2018.

NABARD is also working closely with the Department of Cooperation and the RSCB for the technological upgrading of PACS and to involve DCCBs and PACS in a big way to create financial literacy awareness among the rural masses. Their objective is to make cooperative credit structure an efficient medium for financial inclusion through the Bhamashah Card of the Government of Rajasthan and other social sector schemes. It is expected that with the proactive support of the state government, the maximum number of eligible PACS will be taken on board to act as deposit mobilisation agents in Rajasthan. This support will enable a total of 211 ATMs, 64 FLCs and 1,500 micro ATMs to be established, and 1 million Rupay KCCs to be issued.[44]

Thus, apart from mainstream banks, other financing agencies too are now contributing to the financial inclusion effort with support from central, state and apex financial institutions.

Delayering of the cooperative structure: Under way but with no clear direction

There have been no significant steps taken towards cooperative reform since the 2013 report of the Prakash Bakshi expert committee to examine the three-tier short-term cooperative credit structure (STCCS) in India, which recommended that all PACS be converted into BCs to their respective DCCBs.

In recent years, the rural cooperative structure too has had its share of activity in the matter of reorganisation and reform. However, these have not related to the reform of the PACS system but to the merging of the upper tiers in the three-tier system. The question of restructuring is a prerogative of the state government through the Cooperative Societies Act, and NABARD maintains that it has no opinion on the possibility of a merger between DCCBs and StCBs towards a two-tier structure. During the last couple of years several states have moved in this direction.

As reported in detail in last year's report, the Jharkhand State Cooperative Bank has amalgamated seven DCCBs with itself towards a two-tier structure following recapitalisation of Rs 50 crore by the Government of Jharkhand towards complying with the minimum CRAR of 9 per cent. After conditional approval by the RBI, the Government of Jharkhand notified the amalgamation towards the new entity w.e.f. 1 April 2017. Box 2.3 gives the early experience of the Jharkhand State Cooperative Bank, which became the first StCB to follow this route. It is understood that a procedural review of the merged entity will be undertaken after a couple years of functioning.

Box 2.3: Jharkhand StCB—Experience of Amalgamation of Seven DCCBs

The Government of Jharkhand took a decision to have a two-tier cooperative credit structure. Subsequently, the RBI approved the merger of the existing seven DCCBs (barring Dhanbad) into a single entity. A two-tier cooperative credit structure for the state with an apex bank was then created.

The rationale was, among others, the need for a responsive and efficient bank to provide credit through rationalisation and standardisation of processes and systems, to realise economies of scale, and to better leverage technology for financial inclusion.

According to Brajesh Nath, CEO of the Jharkand StCB, 2017–18 is the first financial year of the combined entity. It's a unique structure, a first in the country, which has started functioning with the existing network of 105 branches of the erstwhile DCCBs and 2,808 PACS/LAMPS (large-sized multi-purpose societies) and other types of societies, affiliated to it at the grassroots level.

Latest Initiatives: The bank provides a number of services which are at par with those offered by commercial banks, like CBS platform, locker facility, net banking (view option only), micro-payment system and E-Kuber. NABARD has sanctioned a mobile van for taking up promotional work.

The bank made effective use of technology for a seamless merger of the seven DCCBs branches into a unified structure even as it strove to provide all technology-enabled services. It is also conducting a 'Going Digital' programme and camps at its rural branches and FLCs. It has received MICR code for all of its 105 branches.

The bank offers RTGS, NEFT, ATM, RuPay debit card, RuPay KCC, etc. to corporate, institutional and retail customers, farmers, and small traders and businessmen. BCs make use of micro ATM devices, and an application has been sent to the RBI to start mobile banking to extend this facility to customers. The bank has engaged 180 IT-proficient personnel for its technology infrastructure; it needs another 550 personnel.

NPA Recovery: The bank was able to reduce total NPAs from 42.97 per cent at the beginning of 2017–18 to 35.26 per cent as of 30 November 2017.

Expansion Plans: The bank is planning to expand the use of the micro-payment system through Bank Mitras, and undertake computerisation of LAMPS and PACS. The bank has applied to the RBI for 138 new branches across the state. NABARD has sanctioned 15 ATMs and 6 FLCs.

Source: Banking Frontiers, 'Jharkhand SCB', 2018. https://www.pressreader.com/india/banking-frontiers/20180125/282338270304184. Accessed on 15 September 2018; NABARD, NABARD Annual Report 2016-17 (Mumbai: NABARD, 2017).

Another state that has been in the news is Kerala where the state government set up an expert committee under M.S. Sriram that in 2017 recommended the merger of higher level cooperative institutions to similarly move towards a two-tier structure.[45] However, a final decision is yet to be taken as the move has come under fire from the political opposition in the state which was reluctant to support the merger in view of the allegedly unsatisfactory outcome of the merger of SBI associates with the parent bank.[46]

Apart from Kerala, in the case of two other states, namely, Chhattisgarh and Uttar Pradesh, merger proposals towards delayering are being considered. Plans have to be submitted and whetted for post-merger parameters to merit licensing and to meet conditions under the Cooperatives Act and the Banking Regulation Act.

According to Sriram, for Kerala the decision was a 'business case' for the consolidation of the bank to offer value-added services to its network of clients by strengthening the already strong cooperative structure—which had a 30 per cent market share but in need of modernisation—to effectively compete with the mainstream banking system. Another factor was the merger of the State Bank of Travancore with the SBI on 1 April 2017. This could open up the space for the expansion of the Kerala Cooperative Bank Ltd. An added attraction was the ability of the new bank to accept non-resident Indian (NRI) deposits not possible under the old structure.

The state of Chhattisgarh, which announced its decision to merge district cooperative banks in July 2017, wanted to improve the availability of banking services to the agricultural sector and local businesses. This was to be undertaken through the merger of six district cooperative banks in the expectation that the consolidated entity would be easier to manage and governance would be strengthened.[47]

Other states too are understood to be under pressure from NABARD to reform the cooperative credit structure. The idea of a merger of DCCBs and state central cooperative banks is not feasible in several states as DCCBs are highly political and have independent fiefdoms that are resisting NABARD pressure to merge. Sporadic attempts by some states will not address the deeper malaise of political interference, accumulated losses, poor performance and inefficiencies that have been a feature of this sector for long.

CONCLUDING OBSERVATIONS

Despite the many initiatives undertaken, the current status of banking agencies, particularly in pursuing inclusion as a development intervention, leaves something to be desired. Commercial banks are hardly well placed to expand their lending to the poor and unbanked clientele given the high NPAs and operational losses, need for bailouts and restructuring and other restraints placed on their functioning by the Reserve Bank of India. Moreover, the diverse set of players now in the mainstream banking space is an emerging source of uncertainty. For example, IDBI bank, which specialised in project financing and was directed into universal banking, now finds itself being taken over by the Life Insurance Corporation of India, which too does not have banking experience.

RRBs have moved away over the years from their original mission towards becoming universal banks and are aiming for the same clientele as the commercial banks without taking into account what the essential character of the RRB was as promoted by the sponsor bank. It would appear that RRBs and their sponsor banks are not clear about what path they have to pursue, responding as they must to the dictates from above and now also subject to PCA plans where necessary.

As regards cooperative societies, these too are on the decline. The question also arises whether the bottom tier of potential clients is actually being reached through cooperatives. A large proportion of PACS are not functioning well. It is also suggested that the subvention scheme and loan waivers have killed cooperative societies. Solutions are being sought not in addressing the needs of grassroots-level societies but restructuring higher levels in the cooperative structure. Here again, the case of the merger of cooperative banks towards a single entity in Kerala is instructive. A uniform approach was applied in the process of the merger. A suggestion that profitable cooperatives should be compensated during the process has been rejected and a uniform criterion is to be applied. Overall, it appears that sporadic changes in the banking institutions are being initiated without a sound policy backing based on a clear picture of the desired banking architecture for inclusive finance.

ANNEXURE 2.1:
Profitability of Public Sector Banks

	Banks	Net profit (in Rs crore)		
I	NATIONALISED BANKS	Year ending March 2016	Year ending March 2017	Year ending 2018
1	Allahabad Bank	(743)	(314)	(4,674)
2	Andhra Bank	540	174	(3,413)
3	Bank of Baroda	(5,396)	1,383	(2,432)
4	Bank of India	(6,089)	(1,558)	(6,044)
5	Bank of Maharashtra	101	(1,373)	(1,146)
6	Canara Bank	(2,813)	1,122	(4,222)
7	Central Bank of India *	(1,418)	(2,439)	(5,105)
8	Corporation Bank	(506)	561	(4,054)
9	Dena Bank	(935)	(864)	(1,923)
10	Indian Bank	711	1,406	1,259
11	Indian Overseas Bank	(2,897)	(3,417)	(6,300)
12	Oriental Bank of Commerce	156	(1,094)	(5,872)
13	Punjab & Sindh Bank	336	201	(744)
14	Punjab National Bank	(3,974)	1,325	(12,283)
15	Syndicate Bank	(1,643)	359	(3,223)
16	UCO Bank	(2,799)	(1,851)	(4,436)
17	Union Bank of India	1,352	555	(5,247)
18	United Bank of India	(282)	220	(1,454)
19	Vijaya Bank	382	750	727
	TOTAL OF 19 NATIONALISED BANKS	(25,920)	(4,852)	(70,585)
II	State Bank of India (SBI)	9,951	10,484	(6,547)
III	ASSOCIATES OF SBI			
1	State Bank of Bikaner & Jaipur	851	(1,368)	
2	State Bank of Hyderabad	1,065	(2,760)	
3	State Bank of Mysore	358	(2,006)	
4	State Bank of Patiala	(972)	(3,579)	
5	State Bank of Travancore	338	(2,152)	
	TOTAL OF 5 ASSOCIATES (III)	1,639	(11,867)	
	TOTAL OF STATE BANK GROUP (II + III)	11,590	(1,383)	
IV	Other Public Sector Banks			
1	IDBI Ltd.	(3,665)	(5,158)	(8,238)
2	Bharatiya Mahila Bank	2	4	
	TOTAL OF PUBLIC SECTOR BANKS (I+II+III+IV)	(17,992)	(11,388)	(85,371)

Source: RBI (www.rbi.org.in)

ANNEXURE 2.2:
Region-wise Deployment of ATMs for Quarters Ending June 2017 and June 2018

		Metro centres	Urban centres	Semi-urban centres	Rural centres	Total
Scheduled commercial banks						
Public sector banks	2017	34,175	41,408	42,615	30,029	1,48,2,27
	2018	32,229	41,064	42,258	29,547	1,45,098
Private banks	2017	24,922	15,207	14,074	4,934	59,137
	2018	24,625	15,346	14,337	4,857	59,165
Foreign banks	2017	745	171	17	16	949
	2018	731	171	17	18	938
Payments banks	2017	0	0	0	0	0
	2018	0	3,406	0	1,441	4,847
Small finance banks	2017	0	0	0	0	0
	2018	312	374	394	127	1,207
Total (banks)	2017	59,842	56,786	56,706	34,979	2,08,313
	2018	57,898	60,361	57,006	35,990	2,11,255
White label ATMs	2017	2,156	1,807	4,468	6,018	14,449
	2018	1,939	1,978	4,872	6,408	15,197
GRAND TOTAL (ATMs)	2017	61,998	58,593	61,174	40,997	2,22,762
	2018	59,837	62,339	61,878	42,398	2,26,452

Source: Reserve Bank of India. https://rbi.org.in/Scripts/StateRegionATMView.aspx. Accessed on 22 September 2018.

ANNEXURE 2.3:
Commercial Bank Initiatives for Financial Inclusion

<table>
<tr><th></th><th>Bank</th><th>Products offered</th><th>Infrastructure support</th><th>Remarks</th></tr>
<tr><td>1</td><td>SBI</td><td>• Savings bank
• Recurring Deposits
• STDR
• Remittances and Overdrafts
• Direct Benefit Transfer
• PMJDY
• KCC
• Pradhan Mantri Jeevan Jyoti Bima Yojana (PMJJBY)
• PMSBY
• APY
• Asset-backed agricultural loan (ABAL)</td><td>• BC
• Bricks-and-mortar branches
• ATM/Recycler
• POS services
• Internet banking
• Mobile banking</td><td>• Bank has set up FLCs;
• has conducted 23,962 financial literacy camps during the year;
• has set up rural self employment training institute (RSETI)centres for livelihood.</td></tr>
<tr><td>2</td><td>Dena Bank</td><td>• BSBDA
• DBT
• PMJDY with overdraft facility
• Remittance facilities
• Dena Kisan credit card
• Dena general credit
• RuPay card and Aadhaar-enabled Payment System (AEPS) transactions through Micro ATMs</td><td>• CBS application
• ATM/debit card
• Internet banking
• Mobile banking
• Tab banking
• Micro ATMs
• POS services
• Ultra-small branches through VPN
• BC
• Bricks-and-mortar branches</td><td>• Bank has been adjudged winner of Best Financial Inclusion Initiatives amongst Small Banks in the IBA Banking Technology Awards 2018;
• has set up FLCs and credit counselling centres.</td></tr>
<tr><td>3</td><td>PNB</td><td>• BSBDA
• Credit card
• KCC
• APY
• PMSBY
• PMJJBY
• PNB MetLife product</td><td>• Bricks-and-mortar branches
• Ultra-small branches
• BC
• Kiosk banking
• ATM/Recycler
• POS services
• Internet banking
• Mobile banking</td><td>• Bank has provided training and certification to all Bank Mitras either through Indian Institute of Banking and Finance (IIBF) or in-house certification;
• has operationalised Aadhaar seeding facility at BC locations in addition to branches, ATM and internet banking;
• has made available OTP-based Aadhaar seeding and authentication of accounts through secure web page on the PNB website;
• has provided biometric-based Aadhaar seeding and authentication of existing customers at branches.</td></tr>
<tr><td>4</td><td>IDBI Bank</td><td>• BSBDA
• Credit card
• KCC
• APY
• PMSBY
• PMJJBY</td><td>• ATM/debit cards
• Internet banking
• Mobile banking
• Micro ATMs
• POS services
• Ultra-small branches through Virtual Private Network (VPN)
• BC
• Bricks-and-mortar branches</td><td>• Bank has set up desks known as Vittiya Sakhsharta Jankari Kendras in rural branches, which have been entrusted with the responsibility of spreading awareness on various banking products and government social security schemes, through outdoor literacy camps;
• has signed Memoranda of Understanding (MoUs) with 13 state-level rural livelihood missions (SRLMs), which are the implementation agencies for National Rural Livelihood Mission (NRLM) at the state level. (NRLM is the flagship programme of the Government of India for poverty eradication, administered through SHGs.)</td></tr>
</table>

	Bank	Products offered	Infrastructure support	Remarks
5	Central Bank of India	• Kisan credit card • Central artisan credit card • Swabhiman/Aadhaar card • PMSBY • PMJJBY • APY • BSBDA • DBT • Credit products under various categories	• ATM/debit cards • Internet banking • Mobile banking • Micro ATMs • POS services • Ultra-small branches through VPN • BC • Bricks-and-mortar branches	• Bank has set up 3 RRBs as on 31 March 2018 in 3 states covering 48 districts with a network of 1,629 branches; • has opened 177 urban financial inclusion centres; • has acquired the lead bank responsibility in 51 districts spread over seven states, viz. Madhya Pradesh (18), Bihar (10), Maharashtra (7), Uttar Pradesh (5), West Bengal (4), Rajasthan (3) and Chhattisgarh (4).
6	Allahabad Bank	• Kisan credit card • PMSBY • PMJJBY • APY • RuPay prepaid card • GCC • BSBDA • DBT • RD	• Micro ATMs • Kiosk banking with Bank Mitra • BC • Bricks-and-mortar branches • Internet banking • Mobile banking • POS services	• Bank has ensured that a total of 4,580 sub-service areas (SSAs) are fully covered through 4,355 Bank Mitras and the remaining 225 SSAs are covered through branches; • has provided financial literacy through FLCs located in all lead districts and Bank Mitras; • has opened 75.98 lakh accounts had been under PMJDY, as on 31 March 2018.
7	Corporation Bank	• RuPay Kisan credit cards (ATM-enabled) • PMSBY • PMJJBY • APY • GCC • BSBDA	• Micro ATMs • Fixed-point Bank Mitra • Bricks-and-mortar branches • Internet banking • Mobile banking • POS services	• Bank has engaged fixed-point Bank Mitras at all the 625 SSAs (covering 2,291 villages) where bank branches are not opened. 93 per cent of the Bank Mitras are active and carry out daily transactions; • has implemented financial inclusion through branchless banking in 4,393 locations; • has opened 40.75 lakh accounts under financial inclusion as on 31 March 2018.
8	Canara Bank	• Weavers' credit card • Kisan credit card • PMSBY • PMJJBY • APY • GCC • BSBDA • DBT	• Ultra-small branches • BC • Bricks-and-mortar branches • Internet banking • Mobile banking • POS services	• Bank has opened 893 financial inclusion branches under the branch model; • Has engaged 2,459 business correspondent agents (BCAs) under the BC model; • Has formed 39,705 SHGs and credit linked 44,439 SHGs to the extent of Rs 1,991 crore during the year. Outstanding SHG accounts were more than 1.30 lakh, with an outstanding amount of Rs 3,359 crore.
9	Bank of Baroda	• Kisan credit card • PMSBY • PMJJBY • APY • RuPay prepaid card • GCC • BSBDA • DBT	• Micro and table-top ATM • Kiosk banking with Bank Mitra • BC • Bricks-and-mortar branches • Internet banking • Mobile banking • POS services	• Bank has carried out massive expansion of the BC model; • has been driving SHG/joint liability group (JLG)-based lending; • has been expanding the scope of services of BCs like mobilising deposits, follow up and recovery in small-loan accounts, including NPA and post written off (PWO) accounts, and providing special incentives to enable them to remain financially viable.

	Bank	Products offered	Infrastructure support	Remarks
10	Union Bank	• Credit cards • IRCTC cards • Prepaid cards • KCC • APY • PMSBY • PMJJBY • PMJDY • DBT • PMMY	• BC by engaging Bank Mitras • Micro-credit through BC • Mobile banking • Internet banking • Bricks-and-mortar branches • POS services • Pass key and biometric-enabled ATM	• Bank has opened 30 FLCs in all 14 lead districts along with few a non-lead districts; • has organised a total of 5,328 village camps to provide digital literacy services to customers; • has achieved a milestone by bringing 54,833 persons into the banking fold by opening their accounts and facilitating credit services; • Has conducted a total of 1,044 digitised camps, within which 230 conducted at rural branch centres.
11	HDFC Bank	• BSBDA	• Brick-and-mortar branches • BCs • ATM facility • POS services	• Bank has made total impact in the area of financial literacy and inclusion; • 59, 12,272 participants covered under Financial Literacy Programmes (FLPs): 59,17,272 • 6,83, 319 participants covered under FLPs
12	AXIS BANK	• Kisan credit card, • PMSBY • PMJJBY • APY • RuPay prepaid card • Asha home loans for aspiring first time home owners • GCC • BSBDA • DBT • RD	• Branches • Speed banking kiosk • BCs with biometric authentication • Brick-and-mortar branches • ATM/Recycler • POS services	• Bank has covered 0.22 million rural people in 15,240 financial literacy camps under Pragatishala.
13	ICICI Bank	• BSBDA • Express loans • KCC • Mandi OD • PMJJBY • PMJSBY • APY • GCC	• BCs • Bricks-and-mortar branches • Internet banking • Mobile banking • POS services	• Bank has been working with 17 BCs who have a network of about 5,920 customer service points covering over 16,100 villages • ICICI Digital Villages Programme was launched in fiscal 2017, and by the end of fiscal 2018 the bank covered more than 600 villages across 21 states in India, as part of this initiative.
14	Syndicate Bank	• PMJDY • KCC • Credit card • APY • PMJJBY • PMSBY • Micro credit	• Banking outlet • BCs • Bricks-and-mortar branches • Internet banking • Mobile banking • POS services	• Bank has covered all allotted 3,229 SSAs comprising of 6,953 villages; • has appointed 2,630 Bank Mitras across the country to provide banking services to the villages; • has set up FLCs and financial inclusion resource centres (FIRC)
15	Yes Bank	• RuPay Kisan card • Micro-credit • Pradhan Mantri Fasal Bima Yojana • Micro-saving • Remittances	• YES SAHAJ Micro ATM • BCs • Bricks-and-mortar branches • Internet banking • Mobile banking	• Bank has launched, through its Digital and Financial Literacy Programme for Farmers, an initiative during 2017–18 to empower 10,850 farmers in 15 districts of Haryana and Rajasthan by providing training in Good Agricultural Practices (GAP), financial inclusion and digital literacy. The programme is aimed at market awareness on money management and debt financing needs of farmers.

Source: Annual Reports for 2017-18 of respective banks.

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12 https://timesofindia.indiatimes.com/business/india-business/apr-jun-data-shows-worst-may-be-over-for-psu-banks/articleshow/65416985.cms. Accessed on 15 September 2018.

13 Three acquisitions carried out in 2016 were: (i) BSS Microfinance by Kotak Mahindra Bank; (ii) Gram Vidiyal by IDFC Bank; and (iii) ASA International India operating in the North East (10 per cent stake acquired by IDFC Bank). Other recent and upcoming mergers are: (iv) BFIL by IndusInd Bank (RBI and SEBI approval for wholly-owned IndusInd subsidiary received); (v) Swadhaar FinServe Pvt. Ltd (not an NBFC-MFI; 100 per cent stake acquired by RBL Bank in June 2018); and (vi) Madura Finance by Federal Bank (still at discussion stage).

14 Beena Parmar, 'RBI Allows Banks to Co-originate Loans with NBFCs to Boost Priority Sector Lending', *Money Control,* 2 August 2018.

15 Ila Patnaik, 'How Parliament Can Reform Its Ailing Public Sector Banks', Bloomberg, 23 July 23 2018. //economictimes.indiatimes.com/articleshow/65098199.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst. Accessed on 15 September 2018.

16 For all SCBs operating in India, 40 per cent of adjusted net bank credit (ANBC) is required to be directed to the 'priority' sector. The target for agriculture is 18 per cent of ANBC with a sub-target of 8 per cent for small and marginal farmers. ANBC earmarked for microenterprises is 7.5 per cent and 10 per cent for the weaker sections of society.

17 PSLCs are a mechanism to enable banks to achieve the priority sector lending targets and sub-targets by purchase of these instruments in the event of shortfall. This also incentivises surplus banks as it allows them to sell their excess achievement over targets thereby enhancing lending to the categories under the priority sector. Under the PSLC mechanism, the seller sells the fulfillment of priority sector obligation and the buyer buys the obligation with no transfer of risk or loan assets.

18 19 July 2018 it was reported that the union government had decided to withdraw the controversial FRDI Bill 2017 which was introduced in the Lok Sabha in August 2017.

19 For detailed data as of 31 March 2016 refer to Table 2.6 in M.S. Sriram, *Inclusive Finance India Report 2017* (New Delhi: Sage, 2018), p. 19.

20 The increase in bank deposits as an effect of demonetisation was also highlighted by Reserve Bank of India, Macroeconomic Impact of Demonetization: A Preliminary Assessment (Mumbai: RBI, 2017).

21 The RBI report mentioned in Note 20 noted that deposits under PMJDY accounts increased significantly post-demonetisation. The total balance in PMJDY deposit accounts peaked at Rs 746 billion as of 7 December 2016 from Rs 456 billion as of 9 November 2016—an increase of 63.6 per cent—but declined to Rs 643 billion by 1 March 2017.

22 Press Information Bureau note, dated 30 August 2017, also indicated that scrutiny of 18 lakh accounts, prima facie, did not appear to be in line with their tax profile. http://pib.nic.in/newsite/PrintRelease.aspx?relid=170378. Accessed on 15 September 2018.

[23] For a fuller description of the revised RBI guidelines on rationalisation of branch authorisation policy dated 18 May 2017, see https://rbidocs.rbi.org.in/rdocs/notification/PDFs/NOTI3062319C9C94C33494794C2B5271CF92878.PDF

[24] The classification for March 2017 and March 2018 is based on the 2011 Census of India, while the data for earlier years is based on the 2001 Census of India. Because of the change in the census base, several rural areas have been reclassified as semi urban. Hence, the 2017 and 2018 numbers are not strictly comparable to earlier numbers.

[25] Data from Reserve Bank of India, *RBI Annual Report 2017–18* (Mumbai: RBI, 2018)., on the progress of financial inclusion plans (Table 2.8 in this chapter) reports a figure of 50,805 for bank branches in villages.

[26] Data for March 2017 suggests that about 35 per cent of all savings bank accounts were BSBDAs, of which around 56 per cent were PMJDY accounts as designated post-2014. tps://www.moneylife.in/article/banks-harass-no-frills-account-holders-by-freezing-or-converting-their-account-to-regular-ones-iit-study/54171.html.
The phenomenon of conversion of BSBDA accounts to regular ones is discussed in Chapter 3.

[27] According to NABARD, nearly 30 million digitalised RuPay cards had been issued to KCC holders of cooperative banks and RRBs by March 2018.

[28] NABARD, NABARD All India Rural Financial Inclusion Survey *(NAFIS) 2016–17,* (Mumbai: NABARD, 2018).

[29] NABARD, Regional Rural Banks: Key Statistics as on 31 March 2018 (Mumbai: NABARD, 2018).

[30] Based upon preliminary data for 2017–18 received from NABARD.

[31] Ajay Tankha, 'Regional Rural Banks and Financial Inclusion: Policy Imperatives', policy paper under the aegis of the Poorest States Inclusive Growth (PSIG) Programme, SIDBI-Access Assist-UKAid, 2015. https://sidbi.in/files/psig/j%20(iv).pdf. Accessed on 15 September 2018.

[32] NABARD, *NABARD Annual Report 2017–18* (Mumbai: NABARD, 2018).

[33] 'Cabinet Nod for Extension of RRB Recapitalisation Scheme', Indian Express, 4 July 2018. http://www.newindianexpress.com/business/2018/jul/04/government-approves-extension-of-regional-rural-banks-recapitalisation-scheme-nabard-to-decide-amo-1838141.html. Accessed on 15 September 2018.

[34] N.S.Vageesh, 'Centre Plans Amalgamation of RRBs at the State Level', *Business Line,* 12 June 2018. https://www.thehindubusinessline.com/money-and-banking/centre-plans-amalgamation-of-rrbs-at-the-state-level/article24146190.ece. Accessed on 15 September 2018.

[35] https://www.thehindubusinessline.com/economy/move-to-merge-rrbs-will-affect-rural-customers-bankers-union/article24305663.ece. Accessed on 22 September 2018.

[36] Under the present arrangement, the Government of India (GoI), the respective states and sponsor banks share RRB capital ownership in the ratio 50:15:35.

[37] For example, at a meeting with NABARD and Indian Banks Association (IBA) held on 25 May 2017, All-India Regional Rural Banks' Officers Federation (AIRRBOF) reiterated its stand that it should be privy to all discussions at the IBA level regarding RRBs and a meeting should take place with all the chairpersons of RRBs to list out issues in order to take them up at the appropriate level. https://www.airrbof.org/circular/pdf/2017/circular41.pdf

[38] M.S. Sriram, 'The Amalgamation of Regional Rural Banks Is Poorly Planned', *Livemint,* 27 June 2018.
https://www.livemint.com/Opinion/JPjso6IINtEkjGrc1XWWSI/The-amalgamation-of-regional-rural-banks-is-poorly-planned.html. Accessed on 15 September 2018.

[39] NABARD, *NABARD Annual Report 2017–18* (Mumbai: NABARD, 2018).

[40] NABARD, *NABARD Annual Report 2017–18* (Mumbai: NABARD, 2018).

[41] NAFSCOB. *Annual Report 2017-18.* http://nafscob.org/publications_f.htm. Accessed on 15 September 2018.

[42] NABARD, NABARD *Annual Report 2017–18* (Mumbai: NABARD, 2018).

[43] Centre for Microfinance, *Rajasthan Microfinance Report, 2017,* (Jaipur: Centre for Microfinance, 2017).

[44] NABARD, NABARD Annual Report 2016-17 (Mumbai: NABARD, 2017).

[45] The report of the Sriram Committee is available at https://kerala.gov.in/documents/10180/9a3e118f-791c-46c7-9451-f51913681e00. Accessed on 15 September 2018.

[46] https://timesofindia.indiatimes.com/city/kochi/kerala-co-op-bank-to-strengthen-cooperative-sector-minister/articleshow/62871015.cms. Accessed on 15 September 2018.

[47] https://www.bloombergquint.com/opinion/2017/07/22/consolidation-coming-this-time-in-district-co-operative-banks#gs.rbaSvdw. Accessed on 15 September 2018.

Financial Inclusion: Agents, Programmes and Institutional Support

3

This chapter covers three critical aspects of the financial inclusion strategy that has been pursued with increasing vigour over the past decade or so. A review of banks in financial inclusion is supplemented by examining a key element of the strategy, namely the use of business correspondents (BCs) and the deepening of technology-led financial service models. The BC model is a critical component of the enabling banking architecture and the digitisation of financial services that have been a cornerstone of the strategy. The evolution of the BC model and relationships has followed a somewhat uneven development path that is now showing signs of stability and maturity. It has involved the participation of multiple and varied stakeholders towards a common purpose. The compulsions of compatible technological systems for this project have resulted in an elaborate and complex financial architecture that has yet to realise its full potential. This has also resulted in a major role for technical service providers (TSPs), who along with bankers and a large army of banking agents have thus far been crucial to the spread of the BC model. As in past reports, an attempt is made to assess the viability of the model and the dynamics of the relationships between the various stakeholders. This is done with the help of recent studies and impressions from field visits.

Simultaneously, with the development of the service delivery channel have been efforts of successive governments and the RBI to implement a largely target-driven programme in mission mode. This is being done first to extend the geographical outreach of the banking system and subsequently to create universal access through the opening of bank accounts for all families and for the provision of certain basic banking and insurance services. This was largely accomplished in a remarkably short period of time. At the same time, the challenge of better utilisation of financial services on offer by the relatively unbanked remains as indeed the need for an expansion of the scope of the services. Over the past four years the Prime Minister's Jan Dhan Yojana (PMJDY) has captured the imagination of all by virtue of its ambitious and wide reach, and time-bound progress such as to extend to over 320 million accounts as of 15 August 2018. Along with the PMJJY, PMSBY and the Atal Pension Yojana, it has a provided a basic model and package of both financial services and social security which is now being extended through the Ayushman Bharat Health Scheme. The progress and possible hiccups in the implementation of these major programmes necessarily merit attention.

Finally, underlying the expansion of financial services is the institutional support provided by the RBI, the National Bank for Agriculture and Rural Development (NABARD) and other development agencies in creating the physical infrastructure and enabling environment for smooth functioning. These apex institutions have played an important role in supporting a vast network of training and extension efforts, of which the campaign for financial literacy is a notable one. In addition, they have contributed to enhancing the capabilities of financing agencies in managing systems of data gathering and MIS, strengthening credit bureaus, and with the provision of operations and communications hardware, facilitating innovation in products and technology-driven processes, particularly to RRBs and cooperative banks. The scope of recent activities and support by these agencies is reviewed as also the challenges that remain.

BUSINESS CORRESPONDENTS

BACKGROUND AND ROLE IN FINANCIAL INCLUSION

There are two major planks of the commercial banks' involvement in the larger financial inclusion: (i) outsourcing through different types of agent structures; and (ii) introduction of IT-based devices and innovation for low-cost operations and for accounting and MIS. The idea of introducing business facilitators (BFs) and BCs was based on the need to lower transaction costs of banks by outsourcing certain financial and non-financial functions. In the initial stages PSBs were not seen to be seeking out individual BC intermediaries for undertaking a range of financial functions. However, private banks with their limited branch network had been expected to use BC–MFIs as part of their business strategy for micro-lending, as had been pioneered by ICICI Bank. While pilot projects were also launched for the delivery of liability products—micro savings, micro insurance and micro pensions—the cost of raising small deposits through BCs-MFIs was seen as a deterrent.

Subsequently when the BC model took root, the prime movers acting as BCs on behalf of the banks were TSPs who were expected to provide hardware and software solutions using ICT applications for efficient and economically viable operations. It also necessitated their involvement in field operations, either directly or indirectly—through their own financial services affiliates or through experienced support organisations in managing BC networks to deliver services to the clients. What emerged as a result was not merely a BC or a BF linked to a rural bank branch to assist in last-mile service delivery, but a whole superstructure of stakeholders with specific tasks and roles along with fee structure and implications for the cost of service delivery. The opening of no-frills accounts—subsequently the basic savings deposit accounts (BSBDAs) and still later the PMJDY accounts—was the starting point of the thrust towards financial inclusion. The process involved an essentially non-financial role for the designated BCA (BCA) or customer service point (CSP). It was only when accounts became operative and transactions took place in them that the CSP would perform the BC role involving financial functions and cash handling.

In addition to the branchless banking function of the BCAs was their intended role in facilitating direct benefit transfers (DBTs). In fact, a massive Aadhaar-enabled DBT programme was seen as providing a platform and anchoring product to ensure access of poor households to high quality banking and driving account usage and financial inclusion. As a result the role of the BC initially became restricted to opening accounts and facilitating transactions and government payments with a limited function for savings mobilisation. The progress of the BC channel was monitored in terms of account openings and BC-facilitated transactions with a reluctance on the part of banks to provide loans through BCs. It is only relatively recently that there has been a major revival of the original model of bank lending operations in partnership with MFIs. The two types of BC partnerships—on the liabilities and credit side—thus merit separate discussion and analysis even as there are some instances of integrated or composite models.

VIABILITY OF THE BC MODEL: RECENT FINDINGS

The growth of the banking infrastructure through the financial inclusion plans of banks under the Swabhimann programme also resulted in a massive deployment of BCs. However, notwithstanding the progress made in financial inclusion, questions remained about the extent of use of financial services by the poor, the utility of the products and services sought to be provided, the margins available and the profitability of their operations for the proposed partners, agents and intermediaries as represented in the BC network. It is only now that the BC channel shows signs of stability and maturity and providing a valuable service to the hitherto unbanked population and the new generation of bank account holders.

The findings of several studies of BC operations of banks, as implemented through network managers and agents, undertaken during the period 2010 to 2015 pointed to the limited efficacy of the model as (i) there was a mismatch between the costs and revenues of BC operations which resulted in a high rate of attrition of BCs; (ii) BC operations were restricted to opening accounts and a limited degree of payments and savings collections; and (iii) it did not address the people's demand for bank loans.

Adding to this, a wide range of policy and implementation issues and operational constraints were identified. These included an unsuccessful attempt to introduce common corporate BCs (CBCs) for all PSBs in 20 clusters delineated across the country; the limited enthusiasm of bankers; a lack of trust in BCs on the part of the population; the slow pace of adoption of technology and the many glitches towards interoperability and connectivity; the risks of cash management; and the low levels of financial literacy, all of which affecting viability at all stages of the delivery chain resulting from limited products and low transaction levels.

MicroSave has conducted extensive research on various aspects of BC operations over 10 years. Numerous studies have served to project the weak performance as well as the potential of the BC model as implemented in India that generally shows an inability to reach anywhere close to the kind of transaction volumes and incomes realised, for example, by agents and CBCs under M-Pesa in Kenya. A Business Correspondent Federation of India (BCFI) presentation[1] that reviewed several earlier MicroSave studies, while noting several discrepancies in the various findings, showed that revenues of BCAs were lower than the minimum wage expectation of Rs 3,000 per month if they focused on only one activity—branchless banking or DBT payments—but increased to over Rs 5,000 per month if they combined both. In view of the suboptimal commissions for G2P payments at the current fee pool ratio of 1.3 per cent, 0.6 per cent and 0.2 per cent respectively among BCAs, CBCs and banks, DBT revenues were not viable for BCAs. In fact, even a 25 per cent increase in DBT commissions would not achieve the minimum wage requirements. The large agent base thus represented a fragmented market with poor economics for all. The viability of agents could be ensured only if the two activities of branchless banking and DBT operations were combined and/or the agents were to simultaneously engage in other related economic activities.

However, MicroSave's most recent study shows the great progress that has been made in the removal of operational constraints as also, importantly, in agent incomes and profits. The finding of the latest Second Wave of the ANA Survey 2017 highlights the fact that in India there has been a shift from account opening to account usage with much-improved support systems as well as the emergence of new players. Crucially, the viability issue seemed to be taking a favourable turn with the survey pointing to a near doubling of transactions, income and profits of rural and non-metro agents between 2015 and 2017 (Box 3.1).

Box 3.1: MicroSave Helix's The State of the Agent Network, India 2017 Report—Major Findings

The study was part of MicroSave's four-year Agent Network Accelerator (ANA) research project—the second wave of Micro Save's ANA Survey that built upon the first wave conducted in 2015.

The study was based upon a nationally representative sample of 3048 agents, of which 55% were in rural areas, 25% in non-metro urban areas and 20% in metros. Of the sampled agents, 31% had a direct relationship with banks while 69% were sub-agents of BC network managers. 92% of the agents were male and 8% female.

State Bank of India accounted for 38% of agents in 2017 as against 35% in 2015. The other major share was that of other public sector banks that accounted for 35% in 2017 (down from 43% in 2015) and private banks with 15% (down from 21% in 2015). Payments banks accounted for 7% predominantly in metro and urban areas and regional rural banks for 6% predominantly in rural areas. 45% of agents were dedicated BCs operators in 2017 whereas 55% were also dependent on other sources of income. The proportion of the latter went up significantly from 33% in 2015.

The study report notes that in two years, India's story of financial inclusion had shifted from account opening to account usage. Supported by enabling technology and focused policy moves, India presented a clear example of how policy imperatives can drive the agenda of financial inclusion. 2017 was a positive shift from 2015. During this time, new models like payments banks emerged, support systems become better, use-cases increased, while agent networks strengthened to position themselves as delivery channels for various financial and non-financial services.

Some of the major findings of the study were:

1. New players (Payments Banks, Common Service Centres) had emerged and existing banks had consolidated on agent management with a focus on refresher training.

2. Banking services and government-to-people (G2P) payments had offered use-cases, which had led to increased transactions and subsequently, revenues and profits.
3. Agent recruitment seems to have slowed, suggesting that providers increasingly look to maintain or develop existing operations in preference to further expanding footprints.
4. High operating costs clubbed with dedication had an impact on profitability and requires solutions.
5. Increased instances of fraud were an area of concern.
6. Recent policy moves of interoperability and payments banks have started to reshape the market. A lot of dynamism is expected in the next few years.

Other highlights of the study were as under:

- *The proportion of experienced agents had increased.* A little over half the agents in rural areas had been in business for over three years This indicated the presence of a widespread delivery channel that providers have managed to create and nurture.
- *Agents were offering a higher range of products and services than before.* Apart from account opening, cash in and cash out and remittances, they included insurance, pension and scholarship registration, utility bill payment, Aadhaar linkage of accounts, airtime top-up and loan processing. Some agents were facilitating fixed and recurring deposit account transactions as well.
- G2P facilitation was a major driver of transactions in rural and non-metro urban areas with nearly 80% of agents in these areas offering a G2P service.
- *On the question of viability, median daily transactions by BC agents had more than doubled in 2017 as compared to the earlier study conducted in 2015.* Those in business over three years were now conducting over 40 plus median daily transactions.
- *Rural and non-metro agents saw a more than doubling of their income between 2015 and 2017* with cash in-cash out (CICO) and G2P remittances mainly contributing to the increase. Their profits too had nearly doubled. However, high operating costs such as rent, utility payments, staff salaries, etc. were a cause for concern. 29% of agents were incurring losses.
- *Women agents did a higher median number of transactions than men but had lower income.*
- 77% of agents had received induction training sessions in 2017—up from 59% in 2015.
- *76% of agents offered interoperable transactions. However, 41% of those who did attributed it to bank policy.*
- Agents primarily undertook the rebalancing of cash flows at the bank branch. The mean distance to the rebalancing point was 5.2 km.
- There was a need to improve agent monitoring and marketing with *service downtime reported by 58% of agents.* The quality of support from payments banks to their agents was better than the country level.
- Finally, *incidence of fraud* was high with an average of 22% of agents experiencing fraud and 29% of the high performing ones.
- Banks managed 31% of their agents while Business Correspondent Network Managers (BCNMs) managed 69%. *Agents managed by banks had higher profits and received greater refresher training support than agents of BCNMs.*

Source: State of the Agent Network, India 2017, ANA Report, India Country Report (MicroSave-Helix Institute of Digital Finance, 2018). http://www.helix-institute.com/sites/default/files/Publications/Agent%20Network%20Accelerator%20Research%20Country%20Report%20India.pdf. Accessed on 22 September 2018.

The findings are largely positive and point to a changing scenario during the period 2015 to 2017. Overall, the picture represents a vast improvement in performance and viability as compared to earlier rounds of similar studies, though with some lingering questions about the cost of service delivery. As discussed below, these findings are generally validated by feedback from a range of stakeholders and field visits by the authors. A disquieting feature, however, is the high incidence of fraud reported, which does not appear to have been taken up by the banks and the CBCs as an area of great concern.

BCs: CURRENT STATUS AND OUTSTANDING ISSUES

3.1 BCAs: Numbers and Outreach

The coverage of villages by BCs and the volume of BC-initiated ICT transactions under the FIPs have been discussed in chapter 2. However, as in the case of other financial inclusion data, there is a lack of clarity about the number of active BCs. Table 3.1 presents RBI data regarding the number of rural banking outlets, rural and urban BC locations and BC transactions. The information on BC numbers contained therein is not uniformly captured over the years.

The increasing number of number rural banking outlets and villages covered by BCs over the years is supplemented by a comparatively smaller, but increasing in proportion, number of urban BC locations. BC-facilitated ICT transactions have virtually experienced exponential growth during the last four years.

RBI data generally relate to the number of villages covered by BCs or number of rural banking outlets through BCs and not the number of BCs. The count of the number of BCs is not maintained, but informally it is placed at around 3,00,000 as of March 2018. This does not include touchpoints of payments banks (PBs) like FINO and Paytm. Indeed, the BCs of SFBs and agents/banking points of PBs (25,000 of FINO on day one of launch) should have inflated the numbers during the last year. A BCFI presentation to the Department of Financial Services (DFS) on 6 September 2018 reports a total of 6.4 lakh Bank Mitras or BCAs.[2]

As part of universal access to financial facilities, all 6 lakh villages, mapped into 1.59 lakh sub-service areas, are to have at least one fixed-point banking outlet to cater to 1,000 to 1,500 households. According to a DFS presentation dated 4 January 2018, 1.26 lakh unbanked SSAs had been covered by interoperable BCs.[3] The figure of 1.26 lakh BCs, clearly an underreporting of the total number of BCs countrywide, has also entered into the BC discourse being associated in some accounts with the PMJDY drive for account opening. Thus, an April 2017 article[4] notes that 'currently, 126,000 of the total 285,000 BCs[5] are engaged only for activities under the Pradhan Mantri Jan Dhan Yojana (PMJDY) programme'.

Regulatory Issues: BC Training, Registration and Employment Status

According to RBI's annual report of 2015–16, a study on the efficacy of the BC model brought out the

Table 3.1: BC Banking Outlets and Transactions, 2012 to 2018

As on end-March	Rural banking outlets through BCs/ villages covered by BCs (1)	Total rural banking outlets—branchless mode@ (2)	Banking outlets in villages—bank branches (3)	Banking outlets in villages—Total (4) (2+3)	Urban locations covered through BCs (5)	ICT accounts BC transaction during the year (in million) (6)	ICT accounts BC transaction during the year (in Rs billion) (7)
2012	1,41,136	1,44,282	37,471	1,81,753	5,891		
2013	2,21,341	2,27,617	40,837	2,68,454	27,143		
2014*	>3,33,000	3,37,678	46,126	3,83,804	60,730	329	524
2015	3,57,856#	5,04,142	49,571	5,53,713	96,847	477	860
2016	4,15,207#	5,34,477	51,830	5,86,307	1,02,552	827	1,687
2017	5,43,472	5,47,233	50,860	5,98,093	1,02,865	1,159	2,652
2018^	5,15,317	5,18,742	50,805	5,69,547	1,42,959	1,489	4,292

Notes:
@ Includes other modes such as ATMs and mobile vans
* 2,48,000 BCs were deployed as reported by banks through their financial inclusion plans
# No. of villages covered by BCs as reported by State Level Bankers' Committees (SLBCs)
^ Provisional
Source: Reserve Bank of India, RBI Annual Reports for 2012–13, 2013–14, 2004–15, 2015–16, 2016–17, 2017–18 (Mumbai: RBI, 2013, 2014, 2015, 2016, 2017, 2018).

need for certification-training programmes for BCs along with providing them other support in terms of timely and adequate remuneration, effective ways of cash management and improving the acceptance infrastructure and technology. The need for creating a BC registry and effective monitoring and supervision involving banks were also highlighted.

The first phase of a BC certification course and exam has now been conducted by the IBA. In the second phase, training is to be carried out on complex products such as pensions and mutual funds. The course has been developed by the Indian Institute for Banking and Finance (IIBF). Any new BC is required to be certified through a two-day course conducted in-house by banks. BCFI has a target of 17,000 ABCs trained, certified and placed on the BC registry by June 2020. Under the BC registry, the details and working location of BCs are provided on an e-portal. However, access is not open to the public, only to members.

According to IBA sources, the BC model is viable at all levels and now BCs are operating like Life Insurance Corporation (LIC) agents. During the past year the IBA was involved in developing an agreement to be entered into by banks with BCs.[6] Interestingly, the language and terms of the agreement seem to be directed towards denial of potential employment rights on behalf of BCs vis-à-vis banks. In fact, the nature of the relationship between banks and BCs is a contested one with the EPFO, India's retirement fund manager asking banks to treat BCs as their employees and extend all benefits due to them.[7] This would also attract minimum wage provisions and retirement benefits that could make the BC unviable. Accordingly, the entire range of stakeholders from the IBA and BCFI to the RBI have written to the labour ministry to exempt BCs from provident fund coverage. The IBA has alerted banks to the need for a 'principal to principal' agreement between the bank and the BC to minimise risks and liabilities in the agreement.

In an interesting subsequent development, there have been reports about 6,000 BCs joining the All India Bank Employees Association (AIBEA) soon. This is according to the association's general secretary, who is quoted as saying that BCs are not being provided the right remuneration and perks despite putting in the same level of work as banking employees.[8] This could become an issue that may need to be dealt with in the coming months.

Another outstanding matter for BC operations relates to the chargeability of the goods and services tax (GST) on BCs, the double taxation in the inclusive value chain and major compliance burdens related to inter-state operations, reverse charge mechanisms, etc. A host of representations by the BCFI to the DFS appears to have gone unheeded.[9]

STAKEHOLDER EXPERIENCES OF THE BC MODEL

Perspective of Banks

The BC relationship with banks is the cornerstone of an important part of the new financial architecture. However, the viability of the BC channel at various levels had continued to defy solutions for over a decade. PSBs had been slow to implement the model and uncertainties prevailed about viability at all levels. Using BCs to open millions of bank accounts and provide doorstep services as part of last-mile service delivery undertaken more under compulsion than commitment. For example, even RBI Governor Raghuram Rajan had in 2014 questioned banks being saddled with the cost of opening and maintaining new accounts under the PMJDY. Early experiences with BC partnerships—both corporate and individual—were mixed, with banks such as the State Bank of India having a negative fallout. Over the years the BC programme has been stabilising, though solutions have not been found to all the challenges posed by the model. In the case of PSBs the compliance load is higher, and cost recovery under the model continues to be a major issue. However, the financial inclusion experience of two leading banks[10] appears to confirm the impact of improved technology and greater diversification. It also asserts the increased viability of BC operations, while at the same time corroborating the programme- and target-driven nature of the financial inclusion drive.

Andhra Bank

Andhra Bank works with several CBCs—Bartronics, Coromandel and Stree Nidhi. In the case of Stree Nidhi, SHG women act as CSPs. Forty per cent of BCs are women. There are 2,000 BCs operating, out of which about 5 to 10 per cent experience problems of poor connectivity. This will ease with the introduction of fibre-optic connections. Under financial inclusion, the focus is on the expansion of BCs in sub-service areas, with all villages required to have a BC available within a radius of 5 km. The target is to eventually have one BC per village. Andhra Bank relies on both kiosk-based BCs and BCs operating with ATMs in the ratio of 60:40. BCAs of the bank earn an average of Rs 10,000 per month, receiving 0.44 per cent of the value of transactions. The bank pays 0.55 per cent, with 80 per cent going to the CSP. BCs are engaged in SHG recoveries, recoveries of NPAs and loan application sourcing. However, it is difficult to have viable BCs in tribal areas and areas of scattered populations. The DFS requires banks to introduce more BCs towards 100 per cent saturation. At present, interoperability has become possible across banks, with 90 per cent of BCs being able to conduct such operations. Interchange fees is paid to the BC and switching fee to the NPCI. Banks are happy with the use of BCs to serve small accounts. In Andhra Pradesh and Telangana, 99 per cent of accounts are fully KYC compliant, with RuPay debit cards being issued for flexibility in the withdrawal of cash by farmers and other clients.

Canara Bank

The bank has 3,000 rural branches, 3,962 sub-service areas and 2,459 BCAs. CBCs are Integra and FINO and there are 873 dedicated financial inclusion branches. The bank's BCs are viable and are paid Rs 5,000 per month basic fees subject to 100 transactions being carried out. Beyond that, further incentives are given. VSATs are being provided through the financial inclusion fund of NABARD in difficult areas. The RBI has recognised banking outlets that function for four hours a day, five days a week as bank branches. Mobile BCs have been constituted as banking outlets under this facility and are able to generate up to Rs 10 lakh per month by way of transactions.

Role of and Innovation by BCNMs

The BC model involves a partnership between the bank and the individual or CBC. It relies upon the following for its operations:

1. *Technical Service Providers:* TSPs are organisations that provide the technology for performing BC operations. Some of these companies also expand their scope vertically to offer BCNM or FBC services (see below), thus becoming end-to-end (E2E) service providers.
2. Business Correspondent Network Managers (BCNMs) or Field Business Correspondents (FBCs): Several NGOs leverage their existing field presence to offer FBC services through tie-ups with a TSP. These organisations establish a service-level agreement (SLA) with the TSP for the provision of technology services and to operate their own BCAs.

Some of the leading BC partners have been operating the E2E model where the TSP is also the BCNM. On the other hand, as banks have developed their own software, they have dispensed with the TSP and work directly with the BCNM. Several BCNMs are operating thousands of agents and facilitating transactions of billions of rupees. Details of outreach, finances and products of four BCNMs that have provided data to Access Assist for this report are given in Annexure 3.1. As technical and financial service providers they have been vital to the introduction of technology in banking operations for financial inclusion. Selected features of their operations are given below.

Sub-K

Sub-K offers multiple products and services by leveraging last-mile technology solutions and formidable distribution channels. Sub-K is perhaps the only CBCNM that offers a wide variety of financial and payment services—savings, credit, remittance, insurance, business to consumer (B2C) and government to citizen (G2C)—for a multitude of financial service providers in multiple geographies pan-India. Sub-K has built an in-house payment platform ViTranSP, a state-of-the-art solution that is operable on a basic phone. It is completely secure, multifunctional, biometric-enabled, real-time and fully compliant with all regulatory requirements. Sub-K has also been able to raise equity capital from institutional investors, most recently in March 2018.

Integra

Integra has been a pioneer in the space of financial inclusion E2E service, where the blend of operation and technology skills has resulted in innovational tools and services. Integra is continually working on multiple technology innovation for servicing the customer, from the era of Total Branch Automation (TBA) to CBS, offline-to-online, smart card-to-Aadhaar, voice and quick response (QR) code-supported AI/ML (artificial intelligence/machine learning) services. Mobile-based monitoring system has been introduced for both agent performance and Integra's operational team with innovative features like geotagging and status update.

NICT

NICT has hired local, resident, unemployed youth for sustainability and stability at the financial inclusion kiosks. It has proved its 2E (empowerment and employment) model by having the lowest number of inactive kiosks and has been one of the top three performers under financial inclusion projects with various banks. Another important feature is its employment of women social banking entrepreneurs. In the last three years, 2,617 women entrepreneurs have been trained and are successfully running bank kiosks.

SAVE

SAVE designed and advocated a dedicated banking kiosk model, which has now become an approved standard across the country in terms of a banking kiosk structure. It is one of the most tech-oriented BCNMs in India with integrated ERP, Android app-based field monitoring system with highly efficient and transparent MIS and a compliance tracker. All this adds to the viability and sustainability of the entire kiosk model. SAVE has pioneered the use of technology in terms of the operational process. It has also designed a cloud-based online reporting and settlement system. This system streamlines the settlement process and transactional settlements can be done as per the requirements of CSPs.

SELECTED BC MODELS AND AGENT RELATIONSHIPS

A Business Model in the Expansion Phase: The BC Model in Bihar[11]

The BC Model consisting of the channel bank—BCNM—BCAs/CSPs continues to be operational as introduced several years ago. CDOT was one of the early participants first as a field BC and subsequently as a CBC. It is also engaged in MFI lending, micro insurance and other financial and development activities. It is working in 3,000 villages in eight states and has appointed nearly 4,000 BCAs who have opened nearly three million bank accounts, apart from providing other banking facilities. According to the CDOT and other stakeholders, the model is proving to be a genuine business proposition for banks and BCs. Earlier, with mainly zero-balance accounts it was unattractive. However, with inter-bank operability, more types of transactions are possible. e-KYC has enabled transactions through thumb impressions. The BC business has moved towards greater financial discipline after the early cases of malpractice. The Madhya Bihar Grameen Bank (MBGB) has obtained Rs 280 crore of deposits through BCs and the Allahabad Bank Rs 3,000 crore. BCs are branching out into other services, including insurance, pensions and mutual funds. They are handling up to 2,000–3,000 accounts of persons who trust them to provide different kinds of services. CSPs are earning up to Rs 60,000–70,000 per month by engaging additional staff as well.

B2B platforms such as railway tickets and hotel bookings too have emerged because of the development of trust in BCs. However, in some areas, people are inclined to deposit their money in the bank branch even though they withdraw money from the BC.

The gender balance requires improving since about 90 per cent of BCAs are men. However, under BRLPS, 300 women Bank Sakhis have been trained by the CDOT to act as BCs. The MBGB has appointed 100 Bank Sakhis and Jeevika is spending on training them. BCs mostly operate from fixed locations by renting a room or from their own residences in villages/small towns. They may, however, move to other nearby villages for a few hours a day.

Overall, the CDOT reports that about 40 per cent BCs are good and working well, 40 per cent are not working full time or in a fully committed way and about 20 per cent are sluggish. Once established as BCs, they add other services like photocopy and Aadhaar and start working as common service centres (CSCs). Network issues continue to be present. Nowadays all data is uploaded online. Often BCs use SIM cards of as many as three networks for efficient functioning. Problems with the bank server or an overloaded Aadhaar server may require them to stagger their transactions throughout the day. Typically a BC carries a micro-ATM, a laptop, a printer and a power back-up. Along with the float amount necessary to facilitate payments, this may require an investment of Rs 1 to 1.2 lakh. Besides this, cashless disbursement is being undertaken in MFIs and liabilities BCs have become credit BCs. CSPs are competing with other BCs in the same geographical area.

Box 3.2: The Crorepati BC Club

Monthly transactions by individual BCAs in Bihar go up to Rs 18–20 lakh with Rs 5 lakh even for those who are not very busy. A float amount of Rs 1 lakh is required by the BC. There is 0.46–0.50 per cent commission per transaction and 1 per cent commission on fixed deposits and rural deposits, 20 per cent of which is to be shared with the CBC. BCAs are selling mutual funds as well through tie-ups with the Unit Trust of India. The Allahabad Bank has a 'Crorepati Club' of BCAs who transact more than Rs 1 crore per month. This would translate into a gross income from BC operations of about Rs 50,000 per month.

Source: Based upon discussions with CDOT staff, Patna, June 2018.

As regards software, banks are now using own technology and dispensing with TSPs such that former field BCs, like the CDOT, now have a direct relationship with banks instead of through TSPs, as in the case of Punjab National Bank and Bank of India. At the software level, though interoperability is now possible, transactions of other banks often do not go through. This creates major refund issues with BCs having to suffer losses in the event of their account not being credited towards withdrawal by the client. Where possible BCs are advised to check the credit to their accounts before making disbursements.

Allahabad Bank offers 0.40 per cent per transaction to BCs under a variable cost model, Rs 20 per new account enrolment, and Rs 5 per recurring deposit or fixed deposit account. With 250 accounts and 300 transactions, Rs 5,000 extra is provided; 20 per cent of that and all the earnings of the BC are earmarked for the CBC. PNB and MBGB pay Rs 3,000 and Rs 4,000 per BC, respectively, plus variable costs. Fund transfer—cash-in/cash-out (CICO)—has a cap of Rs 25 to 50 per transaction. Withdrawal limit through BCs is Rs 10,000.

A new phenomenon is that of recovery agents or 'star centres' appointed by the Bank of India, also called 'special BCs'. These are trained in operations over and above the BC function and offer extra products of Bank of India, including personal loans. They are assessed on the basis of their collection of repayment of bank loans. These special BCs receive training of six days in-house in the banks in a course developed by the IIBF.

Box 3.3 Three BCs from Bihar

1. *Suraj Kumar Patel, BC of Syndicate Bank*

He is a CSP of the CDOT with Atyati as the TSP. Though based at a kiosk on the roadside in Muzaffarpur district, he covers two to three villages spending two to three hours in each every day. He has invested in a tablet computer costing Rs 43,000. He uses the tablet as a mini-ATM with a PIN pad for Aadhaar recognition. As BC he gets Rs 11,000 as income (subject to a minimum of 100 transactions per month) plus Rs 2.50 per transaction from the Syndicate Bank and carries out 150–200 transactions per day. He also provides enrolment facility for insurance services, PMJJY and PMJSY.

2. *Chandra Kishore Sharma, CSP of Allahabad Bank*

He operates from his residence in a village in Muzaffarpur district with the bank branch 2 km away and the nearest ATM 5 km away. He has a laptop computer provided by the CDOT. He does up to 50 transactions per day. The commission received is 0.32 per cent (i.e. 80 per cent of 0.4 per cent received by the CDOT) and Rs 4,000 fixed remuneration per month, subject to a minimum of 300 transactions per month or 250 accounts opened, or other combinations of the two. He has also facilitated Rs 5 to 6 lakh worth of fixed deposits for clients. The major issues faced by him are of a technical nature—there is only one telecom operator that is functional in the village and inter-bank operability is a problem. He finds that people come to him mainly for withdrawals while depositing their savings directly in the bank branch as they still do not fully trust the BC system.

3. *Ram Kumar: BC of Punjab National Bank and MBGB*

Based at a stall in the market of a small town in Nalanda district, he has a monthly income of Rs 15,000, of which Rs 4,000 is paid as rent. In addition he carries out other businesses of selling stationery and photocopying with the help of an assistant. He conducts 80 to 90 transactions worth Rs 1.5 lakh daily. He is compensated in two ways: a fixed remuneration of Rs 5,000 per month from the bank with incentive payments for transactions over the stipulated minimum. He is able to provide Aadhaar-based cash withdrawal services for all banks but no deposits.

Source: Suraj Kumar Patel, interview by author, Muzaffarpur district, Bihar, June 2018.
Chandra Kishore Sharma, interview by author, Muzaffarpur district, Bihar, June 2018.
Ram Kumar, interview by author, Nalanda district, Bihar, June 2018

SHG Women as BCAs: An Emerging Force of Bank Sakhis

While SHGs themselves cannot act as BCs, SHG members and SHG associations, such as federations, are able to. It is estimated that only about 10–12 per cent of BCAs are women. Banks were encouraged by the RBI to appoint women SHG members working as Bank Mitras under the Deendayal Antyodaya Yojana-National Rural Livelihoods Mission (DAY-NRLM) as BCAs so that they could formally transact banking business for SHG members as well as for other customers of banks in a specific area. This constituted a rare attempt at integration or convergence of SHGs with the financial inclusion model.

The German technical support agency GIZ, along with NABARD, had engaged in two pilot projects to test the potential of women SHG members functioning as bank agents to offer banking services to villagers, particularly women and poor households, at their doorstep. The projects were implemented with the Gramin Bank of Aryavart (GBA) in Unnao district of Uttar Pradesh and in Indore district of Madhya Pradesh with the Narmada Jhabua Gramin Bank (NJGB). The objective was to test the model in a different part of the country with different partners, business model and technology. In both projects the banks partnered with a local federation, CBC and GIZ as the technology service provider.[12] SHG members of the federation appointed as BCAs became the first Bank Mitras or Bank Sakhis.

Following its lead, a pilot initiative supported by the National Rural Livelihoods Project (NRLP) is now exploring different pathways of improving formal financial access of rural women-headed households in partnership with various financial institutions and NBFCs like M-Pesa and Oxigen. Under the National Rural Livelihoods Mission (NRLM), various states are identifying and training eligible SHG members as BCAs in association with partner banks. Apart from investments in hardware and training, BCAs are also trained to service transactions of SHGs and their members. Since June 2017, under this initiative around 2,000 SHG members have started operating as BCAs of partner banks across six low-income states, including Bihar, Jharkhand, Madhya Pradesh, Odisha, Rajasthan and Chhattisgarh. In February 2018 alone these BCAs collectively did over 2,60,000 transactions worth over Rs 640 million. The agents are equipped with micro-ATMs and kiosks. Private banks are also involved in four or five states. Technological feasibility of partnership with payments banks such as Airtel and Paytm is also being explored. Such initiatives are not only improving usage of bank accounts by women but are also helping in improving loan repayment rates due to improved access to banks. Bankers are happy as this is migrating low-value transactions to a low-cost ICT-enabled channel and reducing attrition amongst BCAs.[13] The Bank Sakhi as BC model is poised for take-off as this World Bank-supported initiative is executed throughout the country by the NRLM. During 2018–19 the NRLM has a target of appointing an additional 5,000 SHG members as BCAs.

The above project is not to be confused with an NRLM initiative in which all 13,000 bank branches involved with it have a trained Bank Sakhi of a different kind with a more limited role. This cadre of Bank Sakhis (essentially BFs rather than BCs) is an extension of the bank but works exclusively for SHG women. It plays a major role in loan repayments. Bank managers hand out a list of potential NPAs to the Bank Sakhis, who then inform the concerned cluster-level federations (CLFs) of SHGs (where formed) to follow-up with their respective groups. By 2019, the NRLM aims to reach 20,000 more branches with Bank Sakhis.[14]

BANKS, MFIs AND BCs: DIVERSE AND NEW RELATIONSHIPS

BC Portfolio of MFIs: An Increasing Trend Likely to Sustain

The microfinance institutional network was not allowed by the RBI until 2014 to become BCs of banks in view of 'conflict of interest' as they served the same clientele. MFIs had used the securitisation model to overcome capital constraints by selling part of their portfolio to banks—which the MFIs continue to manage on their behalf for a fee. Banks in turn meet their PSL targets through these loans on their books. With NBFC-MFIs also allowed by the RBI to increasingly act as BCs, MFIs are coming forward to be BCs of banks to increase their outreach through off-balance-sheet lending. According to data provided by Sa-dhan, the Association of Community Development Finance Institutions,[15] Indian MFIs have collectively managed a portfolio worth nearly Rs 21,080 crore as of March 2018, as against Rs 13,898 crore as of March 2017. The managed portfolio as of March 2018 also included a BC portfolio of Rs 14,524 crore which was 21 per cent of the total loan portfolio and 69 per cent of the managed portfolio of the reporting MFIs. The BC portfolio was up 43 per cent from the previous year's figure of Rs 10,131 crore. Thus over one-fifth of the total MFI lending portfolio is accounted for by the BC component.

The distribution of the BC portfolio as of March 2018 among different categories of MFIs is shown in Table 3.2. A few of the large MFIs—in the category of NBFCs and others—dominate, with the share of

Table 3.2: BC Loan Portfolio and Category-wise Break-up for 2017–18

MFIs by type of legal form	NBFC/NBFC-MFI	Section 8 company	Others*	Total
Total BC portfolio (in Rs crore)	4,758	1,201	8,565	14,524
MFIs by size of total portfolio (in Rs crore)	<100	100–500	>500	Total
Total BC portfolio (in Rs crore)	508	1,592	12,423	14,524

Note: The leading MFI, Shri Kshethra Dharmasthala Rural Development Project (SKDRDP), registered as a charitable trust, would be the major contributor to this category.
Source: Sa-dhan, The Bharat Microfinance Report 2018 (New Delhi: Sa-dhan, 2018).

Section 8 not-for-profit companies only about 8 per cent. Similarly, a major share of the reported BC portfolio, that is, nearly 86 per cent, is accounted for by large MFIs in the category of total portfolio greater than Rs 500 crore.

In the case of credit BCs, the managed portfolio of MFIs acting as BCs of banks has become nearly one-third of total lending as of March 2018. Private banks, with their compulsions of increasing outreach with a limited branch network, have utilised the BC model. Even SFBs are entering into BC relationships in states where they do not have a presence. While PSBs have still to be involved in BC relationships with MFIs in a big way, it is understood that the State Bank of India is interested in selecting some MFIs as BC partners for micro-lending.

YES Bank's YES LEAP Partnership: Strategy and Future Directions[16]

Under Yes Bank's Livelihood Enhancement Action Program (YES LEAP), Yes Bank provides comprehensive financial services (credit, saving and insurance) to SHGs/JLGs (joint liability groups) through partner organisations acting as BCs and has touched over 2.1 million households across 19 states and 260 districts. While being committed to financial inclusion, the recent focus has been on enhancing technology solutions to efficiently scale Yes Bank's outreach to cater to more unbanked and underbanked populations of India. Innovative methods like virtual training, voice call training and WhatsApp training for BC and ISB staff in remote areas have been adopted, and financial literacy modules have been disseminated to ISB clients.

The BC-MFI staff, who are the BCAs for the bank, form SHGs or JLGs and provide them financial literacy training. Each member's credit eligibility is checked with credit bureaus before the sanctioning of loans. All eligible members are disbursed loans at BC branches and collection of repayment is done by BCAs in group meetings at pre-decided frequencies through the Yes Sahej Micro-ATM.

Through the YES LEAP, over two lakh households have been financed. Over 40 BC partners have worked for Yes Bank to disburse about Rs 6,000 crore with about Rs 15,000 crore outstanding. The bank provides these services in over 260 districts of 19 states in India. Thus, without opening any bank branches in such areas, the BC branches in those regions can act as proxies of Yes Bank to provide last-mile financial services in the form of collateral-free loans to poor women organised in SHGs and JLGs.

The BC gets a margin of 8–10 per cent of interest as income and the borrowing SHG/ JLG pays 22–24 per cent (this is lower in the case of some partners). A 5 per cent first loss default guarantee (FLDG) is taken to offset default. This is invoked from time to time. The bank has a TSP, a processing centre and a risk monitoring team. The cost of credit bureau checks is billed to the bank.

The bank has recently moved to financing JLGs rather than SHGs and to big MFIs from a credit-risk perspective. Partnerships with self-help promoting institution (SHPIs) are not favoured in view of the potential to create ghost borrowers by front-end staff and the SHG leadership. A strategic balance is maintained between different channels. Where rural branches exist, the retail model is used. Rural branches of Yes Bank have a financial inclusion nodal officer and lend to NRLM SHGs at 10–12 per cent per annum like public sector banks under the SHG Bank Linkage Programme. The Bank also has Yes Money, a digital remittance product but not fixed-point BCs as in the case of public sector banks. The move is towards front-end digitisation to improve turn around time (TAT) through e-KYC credit bureau checks, etc. and to introduce cashless recovery in addition to cashless disbursement. Group loan is becoming a liability for a woman who has repaid on time but the group has not, so she cannot get another loan.

Yes Bank still works with smaller MFIs with the complete package, including technology upgrade and financial literacy initiatives. The focus on technology is not only to enable scale but also towards efficiency. Yes Bank also works with Accion on financial literacy.

ICICI Bank-CMRC BF Model

In this model the Community Managed Resource Centres (CMRCs), which are federations of SHGs in Maharashtra, act as BFs. The rate of interest charged to SHGs is 14 per cent per annum, of which 2 per cent goes back to the CMRC, 1 per cent on disbursement and 1 per cent on repayment. SHG prepares their microcredit plans, which are consolidated by the CMRCs, and based upon which district- and state-credit plans are prepared and loans provided by the bank accordingly. Repayment is fixed on the fifth of each month and field teams of ICICI, MAVIM[17] and CMRC arrange disbursement and recovery. The average service charge received by a CMRC is Rs 3 lakh per year, and the average loan size for SHGs is Rs 2.5 lakh. Around 82 per cent SHGs have active loans. For checking NPAs and recoveries, daily delinquency report from ICICI Bank is received, which provides the number of 'buckets', that is, instalments, of default. The CMRC receives 2 per cent of the loan amount at no risk. For SHGs, the savings requirement is 1:6, with loans up to a maximum of Rs 7 lakh. SHGs used to on-lend at 24 per cent per annum to their members. This rate is now down to 18 per cent through MAVIM's persuasion. While in the Yes Bank model the sanction of loans is done by the BC, under this arrangement the district team of the ICICI Bank is involved in disbursement.

NABFINS: Lending by NBFC using Business and Development Correspondents[18]

NABARD Financial Services Ltd (NABFINS) is a subsidiary of NABARD with equity participation from the latter, the Government of Karnataka, Canara Bank, Union Bank of India, Bank of Baroda, Dhanalakshmi Bank and Federal Bank. It is a non-deposit taking NBFC registered with the RBI to operate throughout India. As of March 2018, the company has operations in 125 districts across 13 states with a portfolio of Rs 1,118 crore. NABFINS's unique model of operation enables it to lend money at the least interest rate in the sector, that is, 16.90 per cent per annum to SHGs. During FY 2017–18 it achieved a growth of 41 per cent year-on-year despite the effects of demonetisation that prevailed in the initial months of the financial year.

1. *B&DC and B&DF model:* Under this vertical NABFINS empanels NGOs, trusts, societies, etc. with a proven track record to act as a business and development correspondent (B&DC) for disbursal of credit and recovery of loans from clients with 2 per cent of the loan amount as commission. On the other hand a business and development facilitator (B&DF) involved only in sponsoring groups gets just 1 per cent commission. At present, the model has Rs 900 crore outstanding, which is 75 per cent of the total portfolio. During the FY 2017–18, the company made a record disbursement of Rs 1,221 crore through this model alone.

2. *Direct Lending (DL) model:* The direct lending model of the company has been implemented since the beginning of 2017 to finance SHGs and JLGs without any intermediaries. The staff of the company identifies potential groups for lending and disburse loans according to credit requirements. NABFINS also provides traders' loans by forming a JLG of traders. As of now DL operations reach 12 locations comprising of 18 branches with a portfolio close to Rs 100 crore. The company aims to open more DL branches by the end of FY 2018–19.

3. *Second-level Institutions (SLIs):* The main objective under this vertical is to provide timely and adequate credit to those institutions that are engaged in aggregation, value addition and support services related to rural producers/products. To reduce the burden of members of a group arising out of death of a group member, loan-linked credit insurance is provided to all clients at a nominal rate. The insurance covers the amount of loan disbursed.

NABARD refinance is available to NABFINS at around 9 per cent—up from 8.2 per cent earlier. BCs get 0.5 per cent of loan amount at the time of disbursement, 1.5 per cent of loan amount recovered and 0.5 per cent for timely recovery. Along with a 0.25 per cent incentive for digital repayment, BCs can earn up to 2.75 per cent commission. Since some BCs have up to Rs 25 crores outstanding of the two-year loans, this can be substantial amount.

NABFINS being a purely lending agency cannot have savings accounts and mobilise savings from SHG and JLG borrowers. Similarly it cannot have the FLDG or margin money to cover repayment losses and NPAs. It provides larger loans than available through normal savings-linked SHG lending of banks and MFI lending to JLGs. For example, in Tamil Nadu, up to Rs 10 lakh of loans are being provided to a 12-member group. NABFINS faces several problems in its attempts to disburse money to SHGs through cashless transactions. Though receiving sums up to Rs 10 lakh into their accounts at rural branches, SHGs are unable to withdraw the sum easily because of full KYC compliance being necessary for transactions over Rs 1 lakh in the account. Besides, bank branches give the excuse of limited 'cash retention capacity' at branches, which does not allow such large disbursement.

Some of the issues and challenges faced by NABFINS include:

1. Quality of SHPI partners working as B&DCs. Indeed, several partners have cheated NABFINS.
2. Problems associated with the nature of the business and the rapid expansion by the company. These include: business and credit risk, localised clientele risk and model risk.
3. No partners available in certain areas—for example, the northeast region.

As a result of these issues, NABFINS is moving away from lending to SHGs through the sponsoring NGOs, and SHPIs acting as B&DOs have started direct lending operations instead to better control the business risk.

Other Emerging BC Channels and Stakeholder Relationships

The new categories of banks have found their place in the network of BC relationships and channels. Among SFBs, to grow beyond core geographies, Utkarsh is also adopting the BC model. It is working with another newborn, Kolkata-based Janakalyan Consultancy & Services, to grow business in the east and plans a similar strategy for southern India. Likewise, Kerala's ESAF may expand in the west through partners. This is helping smaller MFIs grow off-balance-sheet business without equity expansion while the small banks can focus on diversifying beyond microfinance.[19] AU SFB has announced the signing of a Memorandum of Understanding (MoU) with Sahaj e-Village for extending its banking service in remote areas through the BC model. Sahaj has been working through 70,000 touchpoints in multiple gram panchayats since the past 10 years.[20]

PBs too figure in BC relationships as BC partners of universal banks. Several of them maintain thousands of BC touchpoints, while at the same time opening accounts of their own subject to the limits pertaining to size of transactions and account balances for PBs. For some of them, the constraints imposed on their functioning as PBs have led to problems with the regulatory authorities and their being temporarily debarred from enrolling new customers.

NBFC-MFIs too have got into the business of subcontracting BC operations. The rationale and compulsion of this is also to extend to new geographies and diverse portfolio risk both NBFC-MFI and the partner bank. For the bank, pooling the portfolio of an existing partner MFI working in a localised area with that of a larger NBFC-MFI having a wider outreach is expected to contribute to reducing concentration risk. In this manner Disha Microcredit, Saharanpur, Uttar Pradesh, a Section 8 company, is operating as a BC of Arohan Financial Services, a leading NBFC-MFI. Arohan is providing Rs 25 crore to Disha to lend to JLG borrowers at 24 per cent per annum with a 5 per cent FLDG. Thus, Disha is secured by being able to operate in its core area in Saharanpur as well as diversify its funding sources.

From the ranks of the CBCNMs, Sub-K was one of the first to have tested the idea of facilitating microcredit through the BC model in collaboration with RBL Bank in 2012. Today Sub-K serves more than 3,50,000 low-income women entrepreneurs across six states and has assets under management (AUM) of Rs 750 crore through this model. The BC-led microcredit model has helped resolve viability challenges of the BC business and brought banks to the centre of financial inclusion. In 2016 Sub-K became the first BCNM to adapt the BC model to individualised microenterprise lending. The company has tied up with the United Bank of India to promote and deepen Mudra Loans in Rajasthan through the BC model. Around Rs 60 crore have been disbursed through this approach to around 4,000 micro-entrepreneurs in four states with impeccable portfolio quality. This model is now being adopted across the banking sector. Sub-K has currently partnered with five financial service providers to promote MSME loans in 10 states.[21]

At the same time field BCs, such as Margdarshak in Uttar Pradesh and the CDOT in Bihar operating in support of BCNMs and TSPs, graduated to credit-MFI relationships with banks. CDOT is the BC in 11 districts for RRBs, having about 100 clients per BCA who are given bank loans. The credit rating of groups through Highmark and provision of insurance facilities under this model is provided by the CDOT. MFIs can operate on about a 6 per cent margin under this model.

Thus the BC space is being populated by a wide range of players and stakeholders with shifting relationships performing different and overlapping functions both in the delivery of liability products and micro-lending. Basic financial functions are supplemented by related insurance products of the PMJDY as well as other linked activities such as promotion and marketing of solar devices, cookers, water purifiers, etc. as also performing recoveries of overdue loans on an incentive basis. This serves to contribute to the viability of BC operations.

Summary Observations on BC Model

Notwithstanding the initial difficulties in the implementation of the BC model, a large number of innovations have been undertaken in service delivery at the last mile. There appears also to be a retreat from the promotion of a universal model of a mobile BC delivering doorstep financial services to a more limited objective of providing services through kiosks. CSCs are increasingly playing a more diversified role in financial services delivery along with G2C services. Accordingly, new areas of service delivery through cross-selling are also being found to ensure continued viability of BCs.

The use of MFIs as BCs by banks is helping to crack the challenge of diversified product delivery, particularly credit. Some of these innovations, which involve a role for MFIs, SHGs and their federations and cooperative institutions, otherwise excluded from the scope of financial inclusion, are potentially replicable as well. In that sense, there is a greater source of viability of credit BCs than BCs for savings and liability products. With increasing loan sizes and loan volumes and even the risk appetite, in most cases there does not appear to be any downward impact on the rates of interest under the BC model, which continue to be as high as 20–26 per cent in most cases. Thus it is possible for a large profitable spread of as much as 12 per cent or so to be shared between the bank and the BC.

With a thrust towards opening of bank accounts and the coverage of the entire country, a major role of the BCA has been completed. However, with the expansion of the BC model, fresh challenges have emerged. For example, bank branches do not have the ability to hold cash and the authorisation limit for handling potentially large government payments enabled by channelling DBTs through BCs. Over the years, affordability and technical feasibility have become possible but investment will have to be made in the delivery structure.

PMJDY AND RELATED SCHEMES

The PMJDY has undoubtedly been a remarkable campaign and achievement in terms of its sweep and coverage. Comprehensive financial inclusion under the mission was based on six pillars:

1. Phase 1 (15 August 2014 to 14 August 2015)
   - (a) Universal access to banking facilities
   - (b) Providing basic banking accounts for saving and remittance and RuPay debit card with in-built accident insurance of Rs 1,00,000
   - (c) Financial literacy programme
2. Phase 2 (15 August 2015 to 15 August 2018)
   - (d). Overdraft facility of up to Rs 5,000 after six months of satisfactory performance of savings/credit history
   - (e). Micro insurance
   - (f). Unorganised sector pension schemes like Swavalamban

In establishing the above pillars, along with Jan Dhan accounts were also launched two highly subsidised insurance schemes—the PMSBY and the PMJJBY—with the Atal Pension Yojana and the provision of Rs 5,000 overdraft per account.

Under the promotion of the Jan Dhan-Aadhaar-Mobile (JAM) trinity that followed, over a billion mobile phones and Aadhaar identities have been created, over 300 million Jan Dhan accounts opened and various measures undertaken such as BHIM, UPI and AEPS to enable over one billion digital transactions a month towards a less cash economy. Through NPCI and AEPS, DBTs are to be routed directly to Jan Dhan accounts. DBT is possible even through PACS and in 393 DCCBs.

The recent completion of the two phases, however, was not marked by notifications of successful achievements of targets or the announcement of fresh goals and products. Notwithstanding continued efforts of the government to push for greater financial inclusion through digital technology and the institutionalisation of the BC channel through training, certification and registration, the mobilisation for lagging insurance products, as well as financial literacy campaigns, there was a sense that with the near-universal opening of bank accounts the mission had largely achieved its purpose.

However, in a belated announcement on 5 September 2018 the finance minister stated that the PMJDY had been 'a runaway success'. It has been renewed to make it an open-ended scheme with an enhanced overdraft facility of Rs 10,000 instead of Rs 5,000.[22] The free accident insurance cover for those opening a Jan Dhan account after 28 August too has been doubled to Rs 2 lakh. There will be no conditions attached for overdraft of up to Rs 2,000. Also, the upper age limit for availing the facility has been hiked to 65 from the earlier 60 years. The minister further announced that 53 per cent of account holders under the scheme were women and that 83 per cent of accounts had been seeded with Aadhaar.

According to the FII,[23] PMJDY has played a crucial role in expanding bank account ownership to previously unbanked adults but with high levels of account dormancy and inactivity. Driven by demonetisation, financial inclusion increased by 15 per cent in the adult population from 2016 to 2017, reaching 78 per cent of adults older than 15 years (approximately 759 million people). New registered bank users, many of whom opened PMJDY accounts, were the main source of growth in financial inclusion. PMJDY account holders grew from 13 per cent to 22 per cent of adults from 2016 to 2017. Registered inactive users were nearly one-quarter of the population (24 per cent) in 2017. Mobile money access increased significantly from less than 1 per cent of adults in 2016 to 3 per cent in 2017.

Even though enrolments for the Aadhaar identity were made mandatory under threat of denial of a range of banking, insurance and investment services, apart from government pensions and other entitlements, the articulation of the JAM strategy does not appear to carry with it a sense of universal acceptance, given the limited use of mobile for banking (still only about 3 per cent of adults) and in view of the lack of institutional preparedness, public support and several downsides of the digital engagement.[24] The almost evangelical drive of DFS, Niti Aayog and certain sections of banking and insurance, especially fintech and mobile companies, has thus still to yield the desired results. In this context, the RBI governor (Box 3.4) too appears to clarify that the RBI has only a limited role to play in overseeing the future development of the PMJDY. Indeed there is no mention of the PMJDY in the RBI's annual report for 2017–18.

Box 3.4: RBI and PMJDY

RBI Governor Urjit Patel notes that with the PMJDY a very large portion of the excluded households has access to the formal banking system. Going forward the market will take over the financial inclusion agenda through technology and innovation and there is not much that the RBI needs to do in terms of a policy push or regulatory initiative. With the onslaught of innovation by players in the market and with technology evolving there will be disruptive new ideas delivering suitable financial products to the poor using this platform. The role of the central bank would be largely limited to ensuring that consumers are protected and that there is no scope for systemic risk.

Source: M.S. Sriram, ed., Talking Financial Inclusion in Liberalized India (New Delhi: Routledge, 2018).

PMJDY: A RUNAWAY SUCCESS?

Under the programme, all 6,00,000 villages across the country were to be mapped according to the service area of each bank such as to have at least one fixed-point banking outlet catering to 1,000–1,500 households. Around 1.59 lakh such sub-service areas (SSAs) were identified.

The state-wise household report suggests that all SSAs throughout the country had been surveyed with the exception of 59 in Chhattisgarh and 4 in Maharashtra. Household coverage was 100 per cent in all states except in 9 states where the coverage was fractionally short at well over 99 per cent. It can be inferred that the programme has indeed been a major success in reaching a saturation level in coverage.

At the same time, while the PMJDY enabled outreach of the banking system through BSDAs open for virtually all families and creating a means for cash cash-in in/cash cash-out services, savings and basic insurance facilities—apart from electronic benefit transfers (EBTs)—it did not make a serious effort or impact in the provision of loan facilities. Indeed, the small overdraft facility available under the programme has remained largely unimplemented. Similarly, the much heralded PMMY (discussed in Chapter 4) -which has partly occupied the same space and under which total lending of over Rs 6,00,000 crore to this segment is understood to have been claimed since the launch of the scheme in 2015[25]—has in fact taken into account the pre-existing lending programmes of banks to this segment with very limited augmentation of resources and channels. Thus, the refinance available through Mudra to banks and other agencies for small- and medium-sized loan amounts was, in contrast, only about Rs 7,000 crore by mid-2018.

Table 3.3 shows the performance of the PMJDY up to 15 August 2018. According to it, 324.1 million accounts have been opened since the launch of the programme, of which 81 per cent were by PSBs, 16 per cent by RRBs and 3 per cent by private banks. Also, 191.2 million accounts were opened in rural areas and 132.9 million in urban areas, the share of rural and urban accounts thus being 59 per cent and 41 per cent, respectively. Women comprised 57 per cent of the account holders. About 75 per cent of the account holders were issued RuPay cards. The balance in the accounts was Rs 812.25 billion or an average balance per account of Rs 2,506.

The above data compares with the performance of total accounts opened as on September 2017 of 301.5 million with an average balance of Rs 2,196.

Table 3.3: PMJDY performance up to 15th August 2018

Bank Category	Rural (in million)	Urban (in million)	Total accounts opened (in million)	No of RuPay cards (in million)	Balance (in Rs billion)	Average balance per active accounts (in Rs)
PSBs	140.9	120.7	261.7	197.9	648.97	2,480
Percentage share	74%	91%	81%	81%	80%	
RRBs	44.3	8.2	52.4	37	141.28	2,696
Percentage share	23%	6%	16%	15%	17%	
Private banks	6	4	10	9.3	22.00	2,200
Percentage share	3%	3%	3%	4%	3%	
Grand Total	191.2	132.9	324.1	244.2	812.25	2,506

Source: PMJDY as on 15 August 2018. https://pmjdy.gov.in/account. Accessed on 25 August 2018.

While this data suggests that all accounts were active, in effect one of the major issues in respect of PMJDY accounts has been the number of zero-balance, bogus and duplicate accounts. Besides, there have been reports that under pressure to achieve targets under the PMJDY, either bank employees opened fake accounts or converted existing accounts into PMJDY accounts. These could number around 10 per cent of all new accounts.[26]

Data on zero-balance and inoperative accounts is not available on the PMJDY site. Besides, the World Bank Global FINDEX database report, 2017 stated that 48 per cent of new bank accounts in India were inactive in the last 12 months as compared to a figure of 20 per cent globally. Part of the explanation has been the launch of the PMJDY in a mission mode. Even the accounts that were active were scarcely used. Reports have also suggested that bankers made small deposits into dormant accounts in order to restore their active status.

The numbers of such zero-balance accounts are not available on the PMJDY site. MicroSave[27] had reported 28 per cent of dormant accounts—mostly attributed to factors such as lack of information on operational procedures, product features and account duplication (one person having multiple accounts). Validation of the phenomenon of inoperative or dormant PMJDY accounts was provided by the minister of state for finance in the Rajya Sabha in March 2018,[28] when he stated that 25.18 crore accounts out of an estimated 31.2 crore PMJDY accounts at the time were operative, implying thereby that over 6 crore accounts were lying dormant.[29] Financial Inclusion Insights' India Wave 4 Report[30] found that only 40 per cent of Indian bank account users had used the account in the last 90 days.

Meanwhile, an academic study by Ashish Das has found that banks are quietly converting the no-fee BSBDAs to fee-based accounts, or charging fees when customers carry out a fifth digital payment transaction in a month. More than half the BSBDAs that have been opened through branches and BCs have been opened under the PMJDY. This has created irrational impediments in the financial inclusion drive.[31]

A study by Bloomberg notes that though over 320 million people have been brought into the formal banking system in just four years, many of India's villages still lack bank branches or ATMs to help service these new customers, since the pace of building the new financial infrastructure has actually slowed. Thus, though India gained about 25,000 bank branches and 45,000 ATMs in the four years up to March 2018, growth has not kept up with the surge of customers.[32] In this context the role of BCs acquires greater significance.

As noted in a paper by Sinha and Azad,[33] the PMJDY is a recent scheme and not much independent data is available to assess its impact on financial inclusion. However, the scheme in its current form is inadequate to address the problems of financial exclusion, as it must also make available affordable credit to the poor. While the PMJDY has mobilised over Rs 800 billion for banks, there has been no impact on access to credit for the poor. According to a Right to Information (RTI) response as of 27 December 2017, overdraft facilities were availed by only 31.39 lakh beneficiaries, that is, about 1 per cent of the account holders. Notwithstanding the announcement of an increase in the overdraft limit, this has been one component of the scheme that has clearly not taken off, largely because of the reluctance of banks to provide this unsecured facility to such accounts.

Finally, the picture emerging from data received in response to a recent RTI query by the finance and business journal *Moneylife* has provided some evidence of the use of PMJDY accounts for money laundering during the demonetisation drive.[34] United Bank of India reported over 1.18 million accounts having in excess of the maximum limit of Rs 1 lakh during a year and a maximum balance of Rs 50,000 at any one time. In addition, a single PMJDY account had deposits of Rs 93.82 crore after demonetisation. Similarly, 16 PSBs that responded to the query reported significant deposits in individual PMJDY accounts well above the limit and running into crores of rupees. The RTI application revealed that as many as 2.08 million Jan Dhan accounts in just 18 banks (which provided data) ought to be classified as 'highly suspicious'. In the absence of lack of clarity about provisions, process and progress in dealing with this phenomenon there is no clear indication how many of these accounts have been frozen and from how many have depositors been able to withdraw the suspect amounts.

Related to this, documents reviewed by Business Standard showed that cash totalling Rs 422 billion was deposited in 37.4 million PMJDY accounts between 8 November 2016 and 30 December 2016. Deposits in PMJDY accounts stood at over Rs 700 billion by 4 January 2017, implying that about 60 per cent of the money was part of suspicious transactions.[35] The finance secretary had informed the paper that deposit amounts were being matched with the profile of depositors to ascertain illicit deposits but it was a time-consuming process.

OTHER PMJDY PRODUCTS: MICRO INSURANCE AND PENSION

Pradhan Mantri Jeevan Jyoti Bima Yojana (PMJJBY) and Pradhan Mantri Suraksha Bima Yojana (PMSBY)

The PMJDY package included two simple and highly welcomed insurance schemes which represented a start towards providing a form of minimum affordable social security. While these schemes have been slow to take off, with greater awareness and through a greater push on the part of banks, BCs, and even the NRLM and NGOs through their SHGs, enrolment rates have increased substantially. So the focus under the PMJDY has recently shifted from opening bank accounts to enrolment in these insurance schemes.

PMJJBY offers renewable annual life cover of Rs 2 lakh to all subscribing bank account holders in the age group of 18 to 50 years, covering death due to any reason for a premium of Rs 33 per annum per subscriber. The scheme is administered through the LIC and 10 other life insurance companies offering the product on similar terms on the choice of the bank, RRB or the cooperative bank concerned. The initial cover period from 1 June 2015 to 31 May 2016 now stands renewed every year from 1 June to 31 May the next year.

PMSBY offers a renewable one-year accidental death-cum-disability cover of Rs 2 lakh to all subscribing bank account holders in the age group of 18 to 70 years for a premium of Rs 12 per annum per subscriber. The scheme is offered/administered through public sector general insurance companies (PSGICs) and eight other general insurance companies offering the product on similar terms. The initial cover period from 1 June 2015 to 31 May 2016 now stands renewed every year from 1 June to 31 May.

Table 3.4 gives the performance of the two schemes in the three years since their launch. As on 30 April 2018, enrolment in the PMJJBY was 5.34 crore, while that in the PMSBY was 13.51 crore. The corresponding figures for 31 March 2017 were 3.10 crore and 9.95 crore, respectively. There has thus been a major spurt in enrolments during the past year.

Gram Swaraj Abhiyan, a special campaign, was organised from 14 April 2018 to 5 May 2018 and extended from 1 June 2018 to 15 August 2018 targeting poor households for providing universal coverage under the PMSBY, wherein PSGICs and

Table 3.4: Performance of PMJJBY and PMSBY

Scheme	Enrolments (in crore)	No. of claims paid	Amount disbursed (in Rs crore)
PMJJBY	5.34	92,089	1,841.78
PMSBY	13.51	16,644	332.88
TOTAL (PMJJBY + PMSBY)	18.85	1,08,733	2,174.66

Note: Data as on 23 April 2018.
Source: http://jansuraksha.gov.in/Performance.aspx. Accessed on 26th August 2018.

banks put up stalls to enrol people in such schemes. With this campaign, 44,15,817 people have been enrolled under the PMSBY.

The government regularly monitors progress in settlement of claims under the PMSBY. While the low premiums under these schemes are undoubtedly attractive, it is understood that under the PMJJBY, the claims ratio for companies during 2017–18 was 120 per cent, while for the PMSBY it was around 180 per cent in the same period. Despite requests from insurance companies the finance ministry is not in favour of increasing the premium under these schemes. State-owned insurance companies, which form around 75 per cent of the market share in both the schemes, have been facing losses of around 90 per cent, especially in the PMSBY.[36]

Atal Pension Yojana

Atal Pension Yojana (APY), a guaranteed pension scheme for citizens of India announced by the Government of India, is focused on unorganised sector workers who constitute more than 85 per cent of the workforce. Under the APY, the guaranteed minimum pension of Rs 1,000 or 2,000 or 3,000 or 4,000 or 5,000 per month is to be given at the age of 60 years depending on the contributions by the subscriber. The spouse of the subscriber is also eligible for pension and the nominee receives the accumulated pension wealth.

The APY is offered by all banks and post offices. The subscriber base of the APY grew manifold to reach 1.10 crore as of 15 May 2018 over the three-year period since its inception, and Rs 3,950 crore as contribution had been collected under the scheme. The scheme has generated around 9.10 per cent compound annual growth rate (CAGR) since its inception till March 2018.[37] Table 3.5 gives the top states in the APY mobilisation.

During 2017–18, 49 lakh subscribers were added. Of the total APY accounts opened thus far, only around 75 per cent are regular accounts (where a holder is making regular monthly contributions). While some banks have been able to meet their targets, others have faced challenges in attracting subscribers. Given that APY is a guaranteed pension scheme, any shortfall in funding will have to be made up by the government. The PFRDA is looking into the amount of this gap funding that may be required.[38] It is further planned to modify the scheme to increase the benefit to Rs 10,000 per month.

According to some experts there are many challenges and complexities of managing a pension over time for persons of low levels of financial literacy and variable incomes who are required to make sustained contributions in anticipation of what could both be a drain on government funds and a limited discounted value of payout for the subscribers.

Table 3.5: Number of Subscribers to APY (15 May 2018)

	State	No. of APY subscribers
1	Uttar Pradesh	1,401,631
2	Bihar	1,061,660
3	Tamil Nadu	8,14,917
4	Maharashtra	7,58,695
5	Karnataka	6,86,504
6	Andhra Pradesh	6,53,404
7	West Bengal	5,51,471
8	Madhya Pradesh	4,98,111
9	Rajasthan	4,97,962
10	Gujarat	4,86,465

Source: Ministry of Finance, Government of India, 'Atal Pension Yojana Subscribers Base Crosses 1 Crore Mark on Completion of 3 Years of Launch of the Scheme,' (2018). http://pib.nic.in/newsite/PrintRelease.aspx?relid=179289. Accessed on 22 September 2018.

APEX FINANCIAL INSTITUTIONS AND INCLUSIVE FINANCE

FINANCIAL LITERACY

An integral part of the financial inclusion strategy, as also one of the six pillars of the PMJDY, has been to improve the capability for financial decision-making, particularly by weaker sections of the population with limited or no exposure to banking, through a financial literacy programme. Given the poor socio-economic condition and low literacy levels of a significant proportion of the population this has proved to be a challenging task. The challenge has been even greater to the extent that new technology and modalities of financial transactions in the digital age can prove to be demanding even for those experienced in the use of banking channels and products and indeed also for bankers themselves. The 'digital divide' adds another dimension to the gulf between the haves and have-nots. There are, in any event, limitations to how far banking practices can be simplified in the interests of reaching the excluded sections. Intermediaries in the form of BCs have performed a useful function providing access to banking services.

While many initiatives have taken place during the last decade or so, it is instructive to learn from the findings of the NAFIS study (Box 3.4) that only 11 per cent of study respondents had good financial literacy such that they were capable of making sound financial decisions. It thus remains the responsibility of state apex financial institutions to enhance literacy levels and access to the banking system.

Box 3.4 Findings of NAFIS study on Financial Literacy

The National Financial Inclusion Survey (NAFIS) carried out in 2016-17 by NABARD constituted a comprehensive overview of the rural population in terms of their status of livelihoods and level of financial inclusion. It covered 40,327 households in 29 states and 245 districts. One of the themes for analysis under NAFIS was the overall status of financial literacy in India.

NAFIS adapted the OECD/ INFE framework for measuring the level of financial literacy in the target households. Financial literacy in context of this study was taken to connote a combination of awareness, knowledge, skill, attitude and behaviour necessary to make sound financial decisions and ultimately achieve individual financial wellbeing.

In respect of *financial knowledge,* the overall trends suggest that *over 70% of respondents were reasonably knowledgeable about the potential risk and returns associated with money and were aware of the meaning of inflation.* When analysed for different categories, no significant differences were observed. The male respondents and those belonging to semi-urban areas were found to be relatively better informed than their respective counterparts.

As regards *financial attitude,* overall trends reflected *a polarization towards spending money and having short-term orientation in financial planning.*

NAFIS focused on a wide range of financial behaviours with an emphasis on those that can enhance or reduce *financial wellbeing.* Overall findings suggested that a sizeable proportion of respondents reported responsible financial behaviour in various situations.

However, the overall assessment of respondents on financial literacy indicated that only about *11% of the total respondents could fall in the category of having 'good financial literacy'.* Individuals living in semi-urban areas and those belonging to non- agricultural households were faring somewhat better when compared to their counterparts. On the whole, the current status of financial literacy left much to be desired in towards making individuals capable of making sound financial decisions for themselves as well as their households.

Source: NABARD, *NABARD All India Rural Financial Inclusion Survey (NAFIS) 2016-17* (Mumbai: NABARD, 2018).

Innovative Approaches to Financial Literacy

The RBI undertook a number of new initiatives on financial literacy during 2017–18. By end-March 2018, 1,395 financial literacy centres (FLCs) were operational in the country, up from 1,376 a year earlier. During the year ending March 2018, 1,29,280 financial literacy-related activities were conducted by FLCs as against 96,315 activities during the preceding year.

In order to explore innovative and participatory approaches to financial literacy, a block-level CFL project was initiated in 2017 by the RBI across 80 blocks in 9 states. The project is currently being implemented by 6 NGOs in collaboration with 10 sponsor banks. Some of the best practices and innovative methods adopted by the NGOs in the execution of the project are highlighted in Box 3.5. In order to improve the effectiveness of financial literacy camps, FLCs and rural branches of banks were advised to use handheld projectors to show audiovisuals and posters on financial awareness messages. Reimbursement for handheld projectors and speakers is provided from the Financial Inclusion Fund (FIF) to the extent of 50 per cent of the cost incurred, subject to a maximum of Rs 5,000 per rural branch/FLC.

Box 3.5 Pilot Project on Centres of Financial Literacy (CFL)

A hub-and-spoke approach to strengthen the financial capabilities of communities has been adopted wherein CFL function as a hub for training and learning, creating trained human resources from communities within the block. Subsequently, these trained human resources drive outreach in their respective communities as spokes.

NGOs work with low-income communities to build their financial capabilities. The trainers and community financial health workers engage with the community and deliver financial education. *Anganwadi* teachers, *Asha* workers and self-help group leaders who demonstrate good communication skills are recruited from amongst the community. Peer learning and participatory learning methods are among the key components of the pedagogy.

A mass awareness campaign is initially conducted targeting 100 people in a village. Subsequently, interested participants are divided into batches of 25 and focused three-day training programmes are conducted for these participants for about 3-4 hours per day. This reinforcement helps the participants build knowledge and skill to choose appropriate financial products and services.

As a first step, influencers, *viz.*, members of SHGs, farmers' federations, *panchayati raj* institutions and health workers are identified and named as "Change Agents - CAs". They are then nurtured and equipped with knowledge, and ways of behaviour change, through a series of multiple and repeated literacy sessions.

A suitably designed digitally equipped vehicle is being utilised to reach out to ensure that both illiterate people and people in far-flung areas are targeted. This Digital Financial Literacy Vehicle contains financial literacy material, audio/ video (power point, demo equipment, etc.) and is managed by a block counselor.

Source: Reserve Bank of India, RBI *Annual Report 2017–18* (Mumbai: RBI, 2018).

The RBI has developed tailored financial literacy content for five target groups (namely farmers, small entrepreneurs, school children, SHGs and senior citizens) that can be used by trainers in financial literacy programmes. The content in the form of five booklets can also be downloaded from the financial education webpage of the RBI. FLCs of banks have been advised to structure the pedagogy for the mandated target-specific financial literacy camps with the help of the booklets.

Financial Literacy Initiatives by NABARD

NABARD provided grants for the establishment of 384 FLCs and 1,086 in RCBs. To increase rural demand for institutional financial services, NABARD supports FLCs, conducts financial literacy awareness camps and prints financial literacy material. In order to give a fillip to digital transactions, NABARD supported 19,186 digital financial literacy awareness programmes (dFLAPs) from December 2016 to March 2017.

Rural branches and FLCs of banks were advised to conduct special camps every month on 'going digital' to promote financial literacy and digital banking. Furthermore, banks and state-level bankers' committees (SLBCs) were advised to cover Unbanked Rural Centres (URCs) under their jurisdiction in mission mode. As of 31 March 2018, NABARD sanctioned Rs 105.32 crore for 'going digital' camps pan-India to various banks and an amount of Rs 77.75 crore had been sanctioned for 1,62,852 camps.

Box 3.6: Setting Up of Digital Village in Gwalior District, Madhya Pradesh

NABARD supported Central Bank of India (CBI) to transform Barai village into a digital village by setting up a Hi-tech Banking Kiosk Centre with two CBI-appointed facilitators, micro-ATM, and PoS machines for awareness creation as well as digital transactions.

As on 31 March 2018, the kiosk had facilitated P2P (peer-to-peer) digital transactions worth Rs. 86 lakhs through micro-ATM and BHIM app. 77 villagers have been taught to use BHIM app, AEPS and Ru-pay Cards. Rupay cards were provided to all 376 households, which have been activated through ATMs.

NABARD provided grant support of Rs. 19.90 lakhs towards conduct of Digital Finance Literacy programmes and capacity building of Branch Managers/Facilitators. CBI has provided the infrastructure for running the kiosk. Due to the success of the kiosk, CBI has decided to set up another Centre in Chinour village of the same district, which has been adopted under the Saansad Adarsh Gram Yojana.

Source: Based upon information provided by the Department of Financial Inclusion and Banking Technology, NABARD, August 2018.

OTHER FINANCIAL INCLUSION MEASURES UNDERTAKEN BY THE RBI

The RBI continued its efforts towards fulfilling the financial inclusion agenda during the year. In this direction, several new initiatives were undertaken in 2017–18.[39]

Committee on Medium-Term Path on Financial Inclusion

In 2015, the RBI Committee on Medium-Term Path on Financial Inclusion, under the chairmanship of Deepak Mohanty, sought to propel the economy to a medium-term sustainable inclusion path. Drawing upon the recommendations of the committee, the RBI focused on strengthening the mechanism for effective credit delivery to productive sectors of the economy. Some of the major recommendations that were implemented during 2017–18 include:

1. BC registry portal has been launched to enable domestic SCBs, excluding RRBs, to upload data pertaining to BCs deployed by them. Subsequently, on stabilisation of the database, the facility of using BC tracker for public shall be made available.
2. A basic certification course for BCs has commenced. The translation of the syllabus into different languages is also under way.
3. The CCC scheme for MSMEs which could help bridge the information gap, and thereby help banks to make better credit decisions was launched during 2017–18.

National Strategy for Financial Inclusion

In order to systematically accelerate the level of financial inclusion in the country in a sustainable manner, the 'National Strategy for Financial Inclusion' document is being finalised under the aegis of the FIAC to take forward the momentum generated by the RBI's financial inclusion policies, the government's Jan Dhan programme and the emerging advancements in the field of digital technology.

Apart from an overview of the progress made so far in bringing financial inclusion to the hitherto unserved and underserved sections of the population, the document would also provide a critique on key issues and challenges that hamper financial inclusion in the country. Based on a cross-country analysis, the document would provide a vision and mission for ensuring sustainable financial inclusion in the country through provision of easy to use, affordable and appropriate financial services to the entire population.

With an increased understanding of interlinkages among financial inclusion, financial literacy and the consumer protection framework, the following strategy pillars have been identified in the document:

1. Developing adequate physical and digital infrastructure in the country through providing necessary access points and connectivity
2. Designing suitable regulatory framework that balances innovation and risks in the financial sector to enable financial service providers to come up with innovative ways to ensure universal access to financial services
3. Focus on increasing financial awareness among various target groups to enable prospective customers and new customers to make suitable choices
4. Putting in place structures for a robust grievance redressal mechanism to protect customers' rights and for timely redressal of their grievances
5. Designing of appropriate scientific assessment tools to granularly measure the extent and issues in financial inclusion
6. Fostering an effective coordination mechanism among all relevant stakeholders

Agenda for 2018–19

Going forward, in order to ascertain efficacies, the RBI would undertake the following steps on credit delivery and financial inclusion: (i) preparation of a framework for credit delivery to tenant farmers; (ii) integration of FIP data with ADEPT to enable automated and timely extraction from the CBS of banks; (iii) impact assessment of pilot the CFL project by an independent agency; and (iv) strengthening of the BC model by capacity building of BCs through the 'Train the Trainers' programme.

FINANCIAL INCLUSION AND BANKING TECHNOLOGY: ROLE OF NABARD[40]

With the setting up of the FIF and the Financial Inclusion Technology Fund (FITF) in 2008, the role of NABARD in bridging the supply–demand gap in the rural financial infrastructure increased manifold.

On the supply side, the CBS was implemented to strengthen RRBs and RCBs; all 56 RRBs are functioning on the CBS platform since 2011. Other technology upgrades include electronic fund transfers and real-time settlement.

NABARD also supported the grounding of post-CBS ICT solutions in RRBs and RCBs. With NABARD's facilitation, the number of RCBs onboarded for the RuPay Kisan Card increased from 47 (1 January 2017) to 350 (31 March 2018).

Sanctions and Disbursements under FIF

The FIF and the FTIF set up in 2008 were merged in July 2015 and renamed the FIF. The fund was augmented with interest differentials of Rural Infrastructure Development Fund (RIDF) deposits as per the policy of the RBI. As of 31 March 2018, cumulative sanctions and disbursements under the FIF stood at Rs 3,400.08 crore and Rs 1,568.74 crore, respectively. Amounts of Rs 712.8 crore and Rs 294.8 crore were sanctioned and disbursed respectively during the year 2017–18. Sanctions and disbursements under the FIF during the last four years are given in Table 3.6.

Table 3.6: Sanctions and Disbursements under NABARD's Financial Inclusion Fund* (in Rs crore)

Year	Sanctions	Disbursements
2014–15	304.89	131.50
2015–16	464.31	157.23
2016–17	1,131.46	628.33
2017–18	712.80	294.77

Note: *FIF and FITF were merged into a single fund FIF in 2015.

During 2017–18, 3,473 training programmes were conducted covering 1.41 lakh participants from various banks/stakeholders under the FIF.

On 31 December 2016, the prime minister announced that RuPay debit cards would be issued to three crore Kisan Credit Card (KCC) account holders. To fulfil this mandate, NABARD facilitated the issue of 113.18 lakh RuPay Kisan Cards through RRBs and 175.99 lakh cards through RCBs.

Pilot Project for Comprehensive Financial Inclusion

A pilot project on comprehensive financial inclusion was launched by NABARD in six SSAs of RRBs in Assam, Bihar, Rajasthan, Tamil Nadu, Uttar Pradesh and Uttarakhand. The objective is to ensure delivery of all financial inclusion products in SSAs through technology and awareness creation in households. Anchored by NGOs, the pilot will run for 18–24 months under the supervision of regional officers and district development managers of NABARD and RRBs.

PACS Computerisation

The union budget of 2017–18 announced support for the computerisation and integration of 63,000 functional PACS with DCCBs to ensure smooth credit flow to farmers in rural areas. NABARD will anchor the scheme, which will be implemented over the next three years at an estimated cost of Rs 1,985 crore with financial participation from state governments and the cooperative credit structure. Consultations with state governments have been completed and the roll out of the scheme is expected to begin during 2018–19.

Micro-ATMs for RRBs

NABARD continued to extend grant support under the FIF to RRBs and RCBs for setting up micro-ATMs, all-in-one integrated devices or mobiles/PCs/tablets with accessories that are to be deployed in branches/PACS of RRBs and BCs/agri-vendors attached to RRBs. During the year, a scheme for funding one micro-ATM per RRB branch was launched in addition to the support that was extended earlier.

Operationalisation of Central KYC Records Registry

The Central KYC Records Registry (CKYCR) was set up, as per the Prevention of Money Laundering (Maintenance of Records) Rules, 2005. All regulated entities (other than scheduled commercial banks) have to upload KYC data of new individual accounts opened from 1 April 2017 onwards with CKYCR, that is, CERSAL. This will eventually lead to a unified KYC regime across the BFSI sector. NABARD is extending support to RCBs and RRBs in order to encourage them to onboard to the CKYCR system.

NABARD supports a range of other initiatives. In dark areas without connectivity VSAT technology is provided, and in grey areas mobile boosters are made available for access in interior regions. In the northeast, the salary of BCs to the extent of Rs 4,000 per month is provided for two years. In tier 5 and tier 6 towns of population up to Rs 10,000 POS machine is provided even for commercial banks. Rs 5,000 per month is provided for 'going digital' camps for all types of digital banks.

CONCLUDING OBSERVATIONS

The status and prospects of the three main strands of the inclusive finance thrust were examined. Recent studies and field reports suggest that the BC model that is the mainstay for last-mile delivery of financial services by banks may now be becoming viable as the transaction volumes increase substantially and interoperability is achieved. An increasing size of BC loan portfolios of banks managed by NBFCs and other MFIs has emerged as an important channel for lending to JLGs, SHGs and individuals. The landmark PMJDY has achieved almost universal coverage and its associated schemes the PMSBY, the PMJJY and the APY are being promoted with vigour. However, concerns remain about the extent of the phenomenon of duplicate and inoperative PMJDY accounts, and the misuse of the facility in view of a large number of such accounts found to be holding balances in excess of the prescribed limit. Finally, many support measures for building the infrastructure for inclusive finance have been undertaken by the RBI, NABARD, banks, fintech companies and government missions such as the NRLM. A focus on financial literacy appears to be a major policy imperative for the coming years especially given the findings of the recent National Financial Access (NAFIS) Survey,[41] reported earlier, which revealed that only 11 per cent of respondents had good financial literacy. With sights set on greater digitisation and use of mobile technology, a larger effort would be required both in creating the physical infrastructure and in tackling the substantial demand-side limitations to greater financial inclusion.

ANNEXURE 3.1:
Outreach, Products and Operational Performance of Selected Leading Business Correspondent Network Managers

	INSTITUTIONAL DETAILS				
1	Name of BCNM	BASIX Sub-K I Transactions Ltd	Integra Micro Systems Pvt. Ltd	NICT Technologies Pvt. Ltd	SAVE Solutions Pvt. Ltd
2	Legal entity (type)	Private sector company	Private limited company	Company	Private limited
3	Commencement of operations	2010	1982	2013	2010
4	Leading state 1	Karnataka	Karnataka	Madhya Pradesh	Bihar
5	Leading state 2	Telangana	Tamil Nadu	Uttar Pradesh	Jharkhand
6	Number of states covered (more than 25% coverage) (FY 2017–18)	21	18	25	21
	FINANCIAL & OPERATIONAL DETAILS				
7	Active customer base (FY 2017–18) (in million)	2.13	7.40	4.06	13.23
8	Number of customers who have done no transaction (FY 2017–18) (in million)	0.36	NA	1.35	3.70
9	Number of customers who have done at least one transaction in (FY 2017–18) (in million)	1.65	7.4	n.a.	9.52
10	Number of partner public banks (FY 2017–18)	4	13	3	3
11	Number of partner private banks (FY 2017–18)	11	3	0	1
12	Number of partner RRBs (FY 2017–18)	-	3	0	2
12	Number of active agents (FY 2017–18)	7,640	9,456	9,836	8,514
13	Total number of women agents (FY 2017–18)	641	3,860	1,163	794
14	Number of SSAs covered (active CSP/Bank Mitra presence) (FY 2017–18)	2,721	650	3,231	6,238
15	Number of gram panchayats covered (FY 2017–18)	2,634	8,656	4,216	6,158
16	Number of urban towns covered (FY 2017–18)	1,230	340	1,034	54

17	Number of basic savings bank accounts (FY 2017–18) (in million)	1.14	7.4	5.45	13.23
18	Number of customers who have done at least one transaction during January to March 2018)-Basic Savings Bank A/c - (in million)	0.35	5.3	NA	7.93
19	Average number of transactions per month over the year (FY 2017–18) (in million)	0.55	4.3	3.56	55.92
20	Average value of transactions per month over the year (FY 2017–18) (in Rs million)	1.39	15. 77	13.54	154.6
	PRODUCT-WISE CUSTOMER STATISTICS				
21	Number of remittance customers (FY 2017–18)	2,49,310	3.70	6.79	4.68
22	Average value of remittance per month per customer (FY 2017–18) (in Rs)	5,506	498	12,077	4,156
23	Number of EBT/DBT customers (those being serviced for LPG, MGNREGA, pensions, scholarships, etc. through CSPs/Bank Mitras/agents (FY 2017–18) (in million)	1.8	1.0	NA	2.91
24	Number of loan accounts (customers) at the end of the financial year (FY 2017–18)	3,54,198	5,10,000	NA	6,856
25	Total value of loans disbursed (FY 2017–2018) (in Rs billion)	7.23	18.00	NA	0.32
26	Total number of customers with outstanding loans at the end of the financial year (FY 2017–18)	3,54,198	2,50,000	NA	5,214

Source: Based upon returns submitted by the respective organisations to Access-Assist in connection with this report, August 2018.

ANNEXURE 3.2:
State-wise Performance of PMJDY

State	Beneficiaries at rural/semi-urban centre bank branches (in '000s)	Beneficiaries at urban/metro centre bank branches (in '000s)	Total Beneficiaries (in '000s)	Balance in beneficiary accounts (in Rs billion)	No. of RuPay cards issued to beneficiaries (in '000s)	Average balance per account (in Rs)
Andaman & Nicobar islands	38	16	54	0.233	42	4,300
Andhra Pradesh	4,510	4,574	9,084	15.52	7,618	1,708
Arunachal Pradesh	153	101	254	0.8305	197	3,269
Assam	10,086	3,121	13,208	30.09	10,202	2,278
Bihar	22,459	13,174	35,634	78.81	25,246	2,212
Chandigarh	39	211	250	0.9786	196	3,908
Chhattisgarh	8,584	4,731	13,315	24.38	8,913	1,831
Dadra & Nagar Haveli	85	16	101	0.3961	59	3,919
Daman & Diu	21	25	46	0.1667	31	3,658
Delhi	487	3,642	4,129	16.25	3,350	3,936
Goa	105	47	152	0.8519	123	5,615
Gujarat	6,504	5,854	12,358	34.41	10,138	2,784
Haryana	3,425	3,190	6,616	26.74	5,739	4,042
Himachal Pradesh	880	139	1,018	4.7764	832	4,692
Jammu & Kashmir	1,701	307	2,008	7.9202	1,517	3,945
Jharkhand	8,325	3,233	11,557	26.92	8,401	2,330
Karnataka	6,710	5,130	11,840	27.23	9,412	2,300
Kerala	1,605	1,976	3,582	9.7865	2,440	2,732
Lakshadweep	5	0.795	5	0.0746	5	14,060
Madhya Pradesh	13,725	14,670	28,395	41.56	20,035	1,464
Maharashtra	10,942	11,612	22,553	46.88	16,030	2,079
Manipur	377	447	824	1.8343	654	2,227
Meghalaya	367	71	438	2.0245	252	4,627
Mizoram	107	177	284	0.6442	78	2,269
Nagaland	103	118	221	0.4336	177	1,960
Odisha	9,273	3,506	12,779	36.17	9,810	2,831
Puducherry	62	88	149	0.3304	111	2,211
Punjab	3,460	2,706	6,166	22.68	5,167	3,679
Rajasthan	14,993	10,041	25,034	59.11	17,508	2,361
Sikkim	69	23	92	0.3136	75	3,423
Tamil Nadu	4,182	4,900	9,082	15.21	7,529	1,675
Telangana	4,624	4,408	9,032	13.46	7,515	1,491
Tripura	605	239	844	6.4733	649	7,673
Uttar Pradesh	29,865	19,813	49,678	140.97	39,134	2,838
Uttarakhand	1,415	846	2,260	9.7725	1,876	4,324
West Bengal	21,356	9,714	31,070	107.99	23,169	3,476
Total	1,91,244	1,32,867	3,24,112	812.25	2,44,231	2,506

Source: State-wise PMJDY as of 15 August 2018. https://pmjdy.gov.in/statewise-statistics. Accessed on 25 August 2018.

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The 'Lost Middle': Engine of Inclusive Growth

4

THE ROLE OF MICRO AND SMALL ENTERPRISES IN INCLUSIVE GROWTH

The Scale; Vast Numbers

The current focus on financial inclusion revolves mainly around small-scale payments, savings and loans, especially microfinance loans. Although microfinance loans are also used for financing livelihoods, the small size of these loans constrains its scope to either tiny household enterprises or meeting a small part of financing needs. Based on this limitation, the core theme of microfinance is to first bring financially excluded people into the ambit of formal finance, and then gradually move them towards larger sized loans from banks. The ultimate aim is to create M&S enterprises, some of which may go on to become large enterprises. The ubiquity of household-level and tiny or microenterprises is evident not only from the fact that we see them all around, but also that it is difficult to put a precise number to such enterprises. Various types of classifications—such as formal and informal, occupational, micro/small/medium that are based on the MSMED Act, 2006, and different legal specifications, further compound the problem. The Sixth Economic Census (2016)[1] survey findings show there are 58.50 million establishments in the country, out of which, 34.80 million establishments (59.48 per cent) are in rural areas and 23.70 million (40.52 per cent) are in urban areas. These establishments employ around 131 million people. The MSME ministry places the figure of non-agricultural MSMEs in the country at 63.38 million, employing 110 million, based on the definition under the MSMED Act, 2016, and the 73rd round of the National Sample Survey.[2] These MSMEs are typically proprietorship, partnership or household enterprises, not having any legal entity, and hence referred to by the survey as unincorporated—broadly meaning not incorporated under tighter and more formal laws like the Companies Act, 2013, or the Factories Act, 1948. Agriculture has been kept out of this count on the lines of the sixth economic census as at a small scale it is mostly for the purpose of self-consumption. It is noteworthy that of the 63.38 million unincorporated and non-agriculture enterprises, 99 per cent are microenterprises. The current definition of microenterprises stipulates that in manufacturing, investment in plant and machinery should be under Rs 25 lakh, and for service sector enterprises investment in equipment should be under Rs 10 lakh—this is the typical customer segment a graduated microfinance client belongs to and can also be called a BoP enterprise.

Generally the focus is on more organised or large companies referred to as the 'corporate sector', and microenterprises are clubbed together as part of the informal sector. Professor R. Vaidyanathan, in his book *India Uninc.,* rightly observes that:

> Referring to them as 'un-organised' is inappropriate, since they are well organised from the economic and organisational point of view. They are not residual segments of the economy. They are very much part of the 'formal' system of laws/rules/regulations. Hence, we would use the term 'Uninc.' [unincorporated] or sometimes, the non-corporate sector.[3]

It is heartening that now the NSS and the Ministry of MSME also classify these enterprises as unincorporated.

These numbers show the importance of M&S enterprises to the Indian economy in terms of their contribution to national income and GDP, as well as employment. During the last few years the country has been debating the spectre of jobless growth, and as to how a surge in the number of youth seeking employment sits uneasily with shrinking jobs in the corporate or government sectors. Modern technology is only going to exacerbate the situation, and it is vital for policy to focus on this unincorporated segment. To be fair, the policy has always accorded priority to it, starting from the 1960s, when the National Credit Council identified SSIs as a priority sector along with agriculture. The creation of SIDBI in 1990, under an Act of Indian Parliament, as the principal financial institution for promotion, financing and development of the MSME sector, as well as for the coordination of functions of institutions engaged in similar activities; the notification of the MSMED Act in 2006; the formation of the Ministry of MSMEs by merging the erstwhile Ministry of Small-Scale Industries and Ministry of Agro and Rural Industries in 2007; and more recently as well as significantly, the formation of MUDRA in 2014, are some of the key milestones. Further, the traditional sectors of khadi and coir have received policy attention since the 1950s, as evident from the formation of the KVIC and the Coir Board, which now function under the Ministry of MSME.

Before analysing the contribution of MSMEs to the Indian economy and the recent policy initiatives in relation to them, it is useful to see the global picture on contribution of MSMEs, why they are called the 'lost middle' or 'missing middle', and what the critical constraints faced by them are.

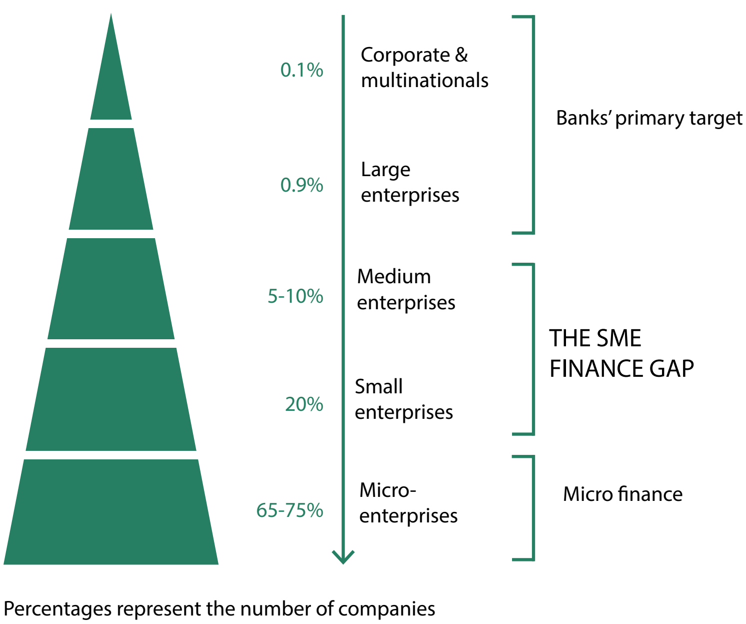


Figure 4.1: Business Landscape in Emerging Economies

Note: Percentages represent the number of companies
Source: IFC, 'The SME Banking Knowledge Guide' (Washington, D.C.: IFC, 2010).

The Global Picture of MSMEs

Globally SME is the term commonly used and each country has different ways of defining as what it constitutes. The World Bank defines MSMEs based on number of employees, assets, annual sales as well as loan size—as a proxy. Microenterprises, which are more pertinent to this report, fall under the category of enterprises that have less than 10 staff or loans below $10,000. Even with this definition, there has to be a country-specific classification because what is medium in a small economy can be tiny for developed economies. As such, it is better to understand the MSME space as a vast spectrum starting from household enterprises and stretching till the very end of economic activity, barring large corporates, while the classification of micro, small and medium can depend on country context.

SMEs serve as a link for the economy, often transacting with large corporations, and providing connections to the formal sector for micro-entrepreneurs. They are active at almost all points in the value chain as producers, suppliers, distributors, retailers and service providers, often in symbiotic relationships with larger businesses. The presence of MSMEs in an economy varies depending on the type of economy. If informal or unincorporated enterprises are included, in almost all economies MSMEs play a vital role. Developed economies have more formal SMEs as compared to developing countries, with better linkages to the financial sector. In developing countries, the Uninc. part is larger, as also severely constrained in access to formal finance.

IFC's report on SME across the globe shows that emerging economies typically have 65 to 75 per cent of enterprises as microenterprises (Figure 4.1). While the report indicates a resource gap at the level of small and medium, assuming that microenterprises can be reached by microfinance, it is not always the case. For example, in India which would typically represent this segmentation, microfinance lending at an average loan size of Rs 25,000 does not meet the credit demand fully, and the coverage remains partial. The entire spectrum, starting from micro to small and parts of medium, has severe access to finance constraint, as its requirements are beyond microfinance but too little for banks, and hence it is referred to as the 'lost middle'. Microfinance's few attempts to up the loan size have been seen as 'mission drift', that is, moving away from the poverty focus. The issue is debatable, but the fact is that despite the need this segment remains out of microfinance's reach.

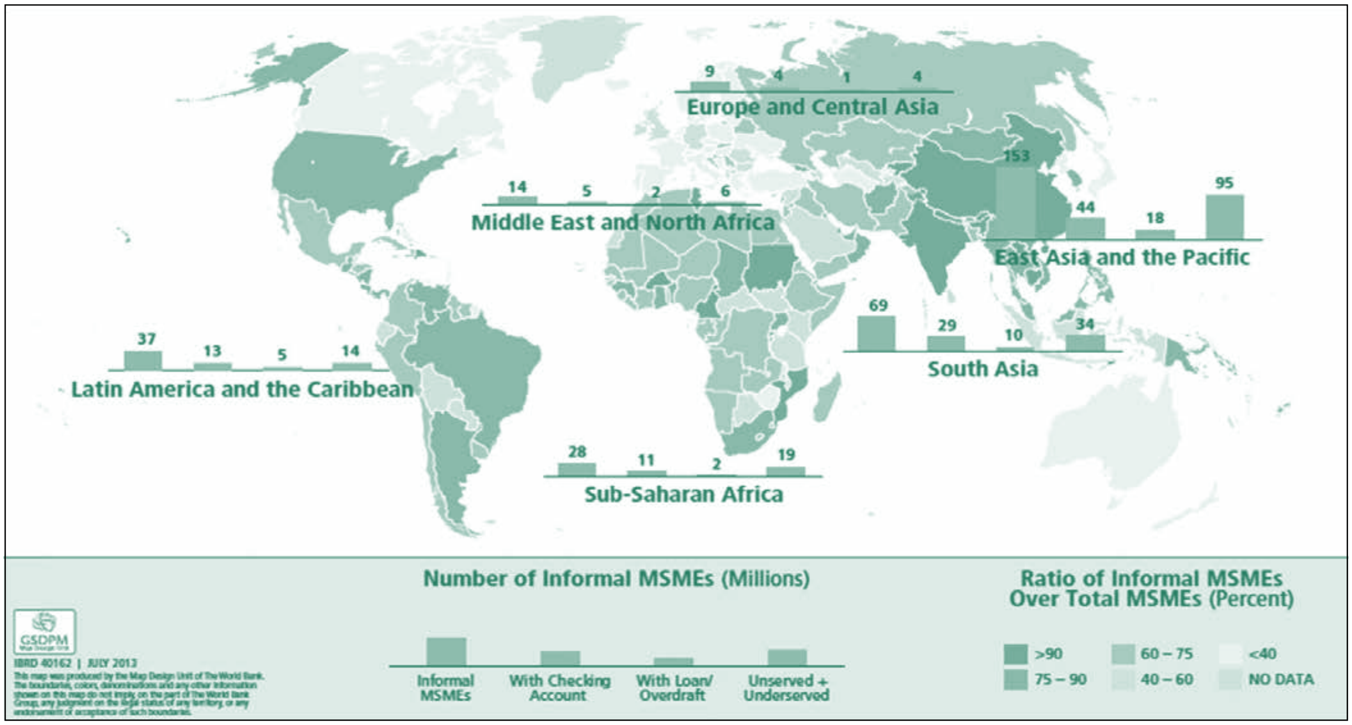


Figure 4.2: Informal MSMEs—Location and Access to Credit

Source: Peer Stein, Oya Pinar Ardic and Martin Hommes, 'Closing the Credit Gap for Formal and Informal Micro, Small and Medium Enterprises (Washington, D.C.: IFC, 2013).

This 'lost middle' is of importance as it creates numerous jobs and contributes significantly to the national economy. IFC's 2010[4] report states that Uninc. and the formal SME sector together contribute to about 65 to 70 per cent of the country's GDP across all income levels. Further, by stating that formal SMEs account for a higher share in developed economies, it also establishes a link between SMEs and economic growth. Globally, informal enterprises contribute 47 per cent to the GDP of low-income countries, 30 per cent to middle-income countries and 13 per cent to high-income countries. The informal sector in developing economies also absorbs around 60 per cent of the labour force. The logical policy objective has to be to move the informal microenterprises up the value chain.

Despite the contribution, as a report of the IFC on the financing gap faced by MSMEs notes,[5] WBES across developing economies show that access to finance is one of the leading operational challenges cited by informal firms that impede their growth and sustainability. Other operational challenges include theft, access to technology and markets, access to land, and corruption. Interestingly, there are no robust national estimates of credit gap for micro- and small enterprises in India. As such, for the financing gap, one has to rely on international agencies like the World Bank and IFC. IFC's report indicates that more than 90 per cent MSMEs in India are informal, which corresponds to the Ministry of MSME figures. However, the report, while not indicating the credit gap at the national level, points out that 34 per cent of informal MSMEs in South Asia are either unserved or underserved, and places the total unmet need for credit, by all formal and informal MSMEs in developing economies, at $2.1 trillion to $2.6 trillion (Figure 4.2).

While talking about the financing gap faced by MSMEs, the report also observes that there is a gender dimension to it, with the financing gap being more pronounced for women-owned enterprises. The gap is also more severe in less-developed countries on account of weaknesses in the financial markets, larger presence of informal enterprises and the consequent information asymmetry, as well as unfavourable legal and regulatory requirements. Increasing access to finance leads to job creation through: (i) starting new businesses; (ii) expansion of existing businesses; (iii) higher liquidity with enterprises; and (iv) indirect job creation through supply and distribution chains.

IFC has recently brought out a new report[6] on the MSME financing gap in developing economies, reiterating that access to finance remains the major constraint for the growth of MSMEs. This report, termed as IFC (2017) here, mentions the problem of finance-gap estimation in the absence of reliable data and adopts a different methodology as compared to earlier assessments. The methodology assesses potential demand for a situation wherein credit markets function with minimal imperfections. Benchmarking with developed economies is a key step in this method, which implies determining how much MSMEs of a certain size and maturity borrow under ideal conditions. IFC (2017) reports that there are 162 million formal MSMEs in developing countries, and 141 million of these are microenterprises. The finance gap in respect of formal enterprises is estimated at $5.2 trillion. For informal enterprises, the report does not provide gap figures but estimates the potential demand at $2.9 trillion. Even if 50 per cent of this is assumed to be finance gap, the total unmet need (formal plus informal) in respect of MSMEs went up to $6.7 trillion in 2017. For India, in the case of formal MSMEs, the gap has been estimated at 11 per cent of GDP.

Three key things emerge from the above discussion on global reports. Firstly, microenterprises in both the formal and informal sectors constitute the bulk of the MSME space. Secondly, access to finance gap is growing over the years, and thirdly, this gap is more accentuated in the case of micro- and women-headed enterprises.

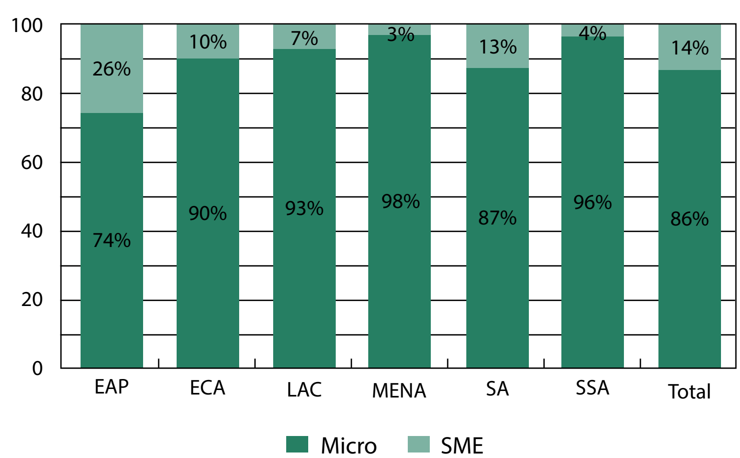


Figure 4.3: Credit Constrained MSMEs in Developing Countries (in per cent)

Source: IFC, 'MSME Finance Gap: Assessment of the Shortfalls and Opportunities in Financing Micro, Small and Medium Enterprises in Emerging Markets' (Washington, D.C.: IFC, 2017).

The importance of MSMEs, and the gamut of problems faced by them, have received global attention. The G20 action plan on SME financing, endorsed by the G20 leaders in November 2015 in Antalya, has also been adopted by the GPFI as a joint action plan. The action plan revolves around two broad areas, that is, financial market infrastructure reform and knowledge agenda. Financial market reform incorporates aspects such as reforms to allow banks and non-banks to increase their lending against movable collateral, insolvency laws and improvements in credit reporting infrastructure. Knowledge agenda focuses on efficient use of ICT, to improve approaches of SME finance, particularly in new areas such as crowdfunding/marketplace lending, addressing issues in data gap, and studies on understanding the role of different types of financial instruments in meeting long-term capital requirements of MSMEs. Thus, MSMEs and their financing constraints do occupy the global agenda, and it is heartening that these are making their way to the financial inclusion discourse, backed by the realisation that microenterprises are the engine of job creation and economic development.

MSMEs in India: Their Nature and Contribution to Economic Growth[7]

The 'micro' in the MSME space is integral to India's inclusive growth, based on its contribution to jobs and the national output, and also by the sheer dominance of economic activity. The classification of MSMEs in India as of now continues to be based on investment in plant and the amount of machinery (Table 4.1). Although the union cabinet passed a proposal in 2018 to change it, basing it on turnover, it has yet to come into effect, which will require an amendment to Section 7 of the MSMED Act, 2006. The proposal defines a microenterprise as a unit where the annual turnover does not exceed Rs 5 crore, a small enterprise as one where the annual turnover is between Rs 5 crore and Rs 75 crore, and a medium enterprise as one where the turnover is more than Rs 75 crore but does not exceed Rs 250 crore.

The Indian MSME space, comprising 63.39 million enterprises, which includes both formal and unincorporated entities, is dominated by the 'micro' segment. Microenterprises in India account for 99 per cent of the 63.39 million enterprises, as against the global average of 65 to 70 per cent for emerging economies. Higher number

Table 4.1: Current Classification/Definition of MSMEs in India

	Manufacture or production, processing or preservation of goods	Providing or rendering of services
Micro	Investment in plant and machinery does not exceed Rs 25 lakh	Investment in equipment does not exceed Rs 10 lakh
Small	Investment in plant and machinery is more than Rs 25 lakh but does not exceed Rs 5 crore	Investment in equipment is more than Rs 10 lakh but does not exceed Rs 2 crore
Medium	Investment in plant and machinery is more than Rs 5 crore but does not exceed Rs 10 crore	Investment in equipment is more than Rs 2 crore but does not exceed Rs 5 crore

Source: https://msme.gov.in/faq. Accessed on 24 July 2018.

of microenterprises exhibit the potential for growth and graduation of these enterprises with a facilitative environment. The MSME space has been rapidly growing, as the number of MSMEs in 2006–7 was 36.17 million, which has doubled in 2016–17. However, despite the increase in numbers, the share of microenterprises continues to be at 99 per cent, which should be an area of concern, as these enterprises are usually not able to scale up. It also reflects that new enterprises mainly belong to the micro category; experts have also attributed this to fewer jobs in the formal sector, forcing people to rely on self-employment.

There are two other distinct takeaways from the profile of MSMEs in India. Firstly, the rural–urban share in MSMEs is almost equal, with rural areas accounting for 51 per cent of MSMEs. Secondly, there is no activity concentration, with manufacturing, trade and service accounting for 31, 36 and 35 per cent share, respectively.

Considering the share of microenterprises, it is no surprise that 96 per cent of MSMEs in India are proprietorship entities. The positive side of this is that women's ownership is much higher in the case of microenterprises at 20 per cent as compared to 5.26 and 3.27 per cent in small and medium categories, respectively.

Table 4.3: Share of MSMEs in India's GDP over the Years

Year	Share in GDP (in %)
2012–13	29.94
2013–14	29.76
2014–15	29.39
2015–16	28.77

Source: CSO, Ministry of Statistics & Prog. Implementation www.mospi.gov.in. Accessed on 26 October 2018.

MSMEs contribution to jobs is enormous standing at 111 million, with microenterprises accounting for the bulk of it at 107.6 million, or 97 per cent. The broad activity-based job creation is almost equally shared by manufacturing, trade and services, as also the rural–urban split. A logical corollary of the predominant share of microenterprises is that jobs created per enterprise remain low. For the sector as a whole, the ratio of enterprises to jobs comes to 1:1.75. The ratio, excluding small and medium, falls even lower. However, as the average investment done by microenterprises is not available, it is not possible to deduce the minimum investment required to create one full-time job. This issue is pertinent in the current debate, where it is

Table 4.2: MSMEs Distribution by Geography and Type

Sector	Micro	Small	Medium	Total	Share (in %)
Rural	324.09	0.78	0.01	324.88	51
Urban	306.43	2.53	0.04	309.00	49
All	630.52	3.31	0.05	633.88	100

Source: Ministry of MSME, *Annual Report 2017–18*. https://msme.gov.in/relatedlinks/annual-report-ministry-micro-small-and-medium-enterprises. Accessed on 26 October 2018.

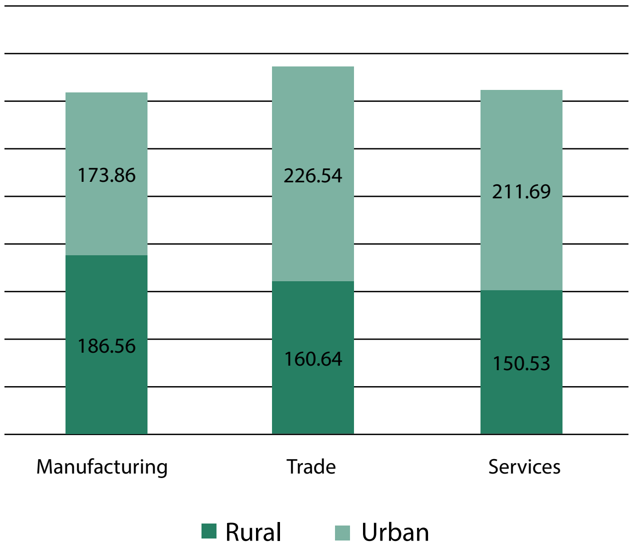


Figure 4.4: Employment in MSME Sector (in lakh)

Source: Ministry of MSME, *Annual Report*. https://msme.gov.in/relatedlinks/annual-report-ministry-micro-small-and-medium-enterprises. Accessed on 26 October 2018.

argued that loan amount under the Shishu category of MUDRA loans may not be sufficient for creation of full-time employment for even one person.

Besides providing employment, the MSME sector on an average contributes around 30 per cent to India's GDP. This brings out the current contribution of MSMEs to jobs and national income based on official statistics, but there are other estimates also. A report by the Aditya Birla Group says, 'SMEs contribute more than 45 per cent of India's industrial output, 40 per cent of the country's total exports and create 1.3 million jobs every year.'[8]

A survey of the global literature above shows that access to finance is the main constraint for MSMEs. The Indian scenario also exhibits a similar storyline. The Chamber of Indian MSMEs cites access to adequate and timely finance from the banking sector as the topmost need; a research paper on MSMEs in India also places access to finance at the top and says:

> The scarcity of finance and credit is the main obstacle in the development of MSMEs. The position of cottage and village industries in this regard is even worse. The capital base of the small industrial units is usually very weak, since they generally have partnership or single ownership. The artisans or craftsmen running cottage industries, either run their business with whatever little capital they possess, or take credit from the mahajans, or the traders who supply raw material to them. In many cases, such credit is obtained on a very high rate of interest, and is thus exploitative in character.[9]

A working paper[10] on the subject by the ADBI also puts access to finance as a key constraint for MSMEs. It points out that the barriers to accessing finance in India from formal institutions include the requirement for a collateral or a guarantee, inflexible policies, high rates of lending, a complicated procedure and entrepreneurs' lack of financial knowledge of applicable schemes. Interestingly, the study delves into access to finance issues across various stages of an enterprise, namely start up, survival, growth and sustenance, and finds that financial challenges and sources of finance differ widely across these phases.

However, when it comes to the estimation of the financing gap, there are not enough robust studies. What one comes across are occasional statements from various quarters, like around 90 per cent of Indian MSMEs being dependent on self-funding.[11] As such, though it is difficult to put a precise number to the gap, there is consensus on the huge unmet demand in the MSME space. The government, being aware of the problem, has accorded priority to MSME financing, and in recent years several steps have been taken to boost financing for the sector. The following section briefly enumerates key initiatives of the government, RBI and SIDBI to boost credit flow to MSMEs.

POLICY INITIATIVES IN RECENT YEARS TO ACCELERATE CREDIT FLOW TO MSMEs

Among the host of measures undertaken in recent years on credit to the MSME sector, the formation of MUDRA stands out. MUDRA's importance also stems from the fact that it focuses on the micro-sector. Accordingly, MUDRA's role, performance and what it can do to help the sector have been discussed as a separate section in the chapter.

RBI's guidelines on priority sector lending specify lending to MSMEs as an eligible activity under the definition of priority sector. Further, to focus on microenterprises, the RBI has specified a sub-limit of 7.5 per cent for microenterprises under the priority sector. The RBI definition of MSMEs follows the MSMED Act, 2006. During the current year, the RBI made two relaxations in counting eligible loans to MSMEs as priority sector. In February 2018 the RBI mandated that there will be no credit cap in lending to manufacturing MSMEs and, later in the year, extended it to service sector MSMEs also. Earlier, to be in the reckoning as priority sector, there were caps based on category of MSMEs. For example, loans of up to Rs 25 lakh for microenterprises in the manufacturing sector and of Rs 10 lakh for microenterprises in the service sector could only be considered as being for priority sector. Though this relaxation is not aimed at microenterprises, it will benefit the sector as a whole.

The demonetisation announced in November 2016 led to hiccups for the MSMEs, especially those relying on cash as the primary medium of operation, though the overall business environment was also impacted. The RBI, recognising that this would lead to loan defaults, relaxed the criteria for the NPA classification of MSME loans by banks and NBFCs. During its monetary policy announcement in February 2018, the RBI announced that GST-registered MSMEs, with aggregate standard exposure of up to Rs 25 crore, will now get 180 days to make loan repayments. Earlier the limit was 90 days and 120 days for banks and NBFCs, respectively. While providing relaxation, the RBI has also ushered in a nudge towards greater formalisation of the sector, as the facility is available only to GST-registered MSMEs.

Government and SIDBI Initiatives

Credit flow to MSMEs has always been a focus area of the government, and there have been numerous committees and task forces in the past to suggest measures—such as the Working Group on Flow of Credit to the SSI Sector, Ganguly Committee in 2004; the high-level committee on credit to SSI headed by SL Kapur; and the committee to examine the adequacy of institutional credit to SSI, Nayak Committee in 1991. In 2010 the Prime Minister's Task Force on Micro, Small and Medium Enterprises gave its report and stipulated targets for MSME lending to be achieved by banks. It said: 'All the scheduled commercial banks should achieve a 20% growth in credit year-on-year to micro and small enterprises, and strictly adhere to the allocation of 60% thereof to microenterprises, to ensure enhanced credit flow'.[12]

The prime minister announced the ambitious Stand-Up India scheme in 2015 to promote entrepreneurship at the grassroots level for economic development and job creation. The scheme envisages bank loans between Rs 10 lakh and Rs 1 crore to at least one SC or ST borrower and at least one woman borrower per bank branch for setting up a greenfield enterprise. The scheme portal was managed by SIDBI (standupmitra.in) and provides information on contact points of lead district managers/help centres and subsidy schemes. For the very first time, the scheme provides an opportunity for applicants to also apply online and track their application status. The scheme supports only greenfield ventures, implying a first-time undertaking of the client. The performance of the scheme till date, despite significant efforts by the government and SIDBI, are nowhere near the goal. There are nearly 1,40,000 bank branches in India, and as per the scheme, two loans per branch would have meant nearly three lakh new loan accounts. However, in the last three years, total sanctions have reached only 61,887 new entrepreneurs. Further, these are sanctions and it is suspected that disbursements would be even lower.

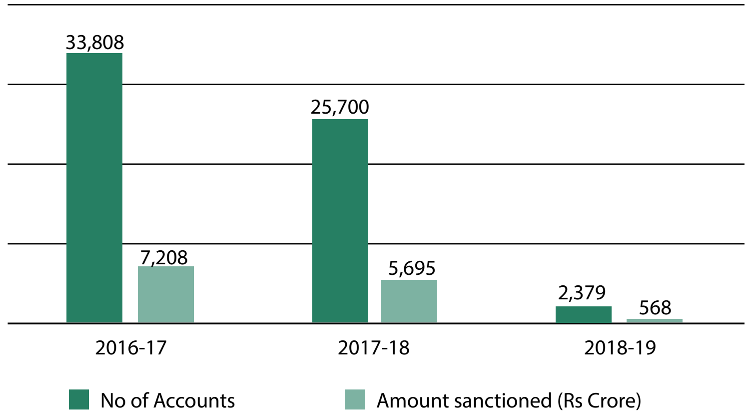


Figure 4.5: Progress under Stand-Up India

Source: SIDBI, email to author, 19 July 2018.

Still, assuming that according to its objectives the scheme has covered new entrepreneurs, it is a welcome development in promoting grassroots entrepreneurship, and the fact that the average sanction amount hovers around Rs 20 lakh is evidence of its impact at the microenterprise level. Three thousand and seven entrepreneurs also secured online sanctions, which can provide useful insights into the building of future fintech platforms for MSME lending by showing what works and what does not.

As part of using digital initiatives for MSME lending, in 2016 SIDBI launched a new portal (www.udyamimitra.in), building on the IT platform of Stand-Up India. The Udyamimitra portal was revamped in 2017 with enhanced features, both from the demand and supply side. The portal acts as a platform for Stand-Up, MUDRA and other MSME loans of up to Rs 2 crore. After 2018–19 the Stand-Up portal will get subsumed under the Udyamimitra portal. The demand-side features include enhancing loan limit from Rs 10 million to Rs 100 million, e-KYC facility, credit information report and a chatbot for assisting entrepreneurs. On the supply side, a new feature is the enlargement of the pool of lenders to include NBFCs and fintechs—earlier only banks were included. The Udyamimitra portal is a comprehensive digital platform (Box 4.1), and a one-of-its-kind, with the entire banking network of the nation in one place. As of now, it has 103 banks, including SFBs with their 1.25 lakh branches, and 41 NBFCs/fintechs on its platform.

Box 4.1: Key Features of the Udyamimitra Portal

- Facility to make both online and offline MSME loan applications
- Standardised loan application forms
- Guidance on handholding support
- Bankability kit showing key features of a successful application
- Information on various subsidy schemes
- Eligibility check
- e-KYC and credit bureau check
- Borrower can indicate preferred lender
- Online tracking of application

Source: www.udyamimitra.in

The portal is a unique step in creating a marketplace, wherein potential borrowers are provided information on making a successful application and the facility to submit it online, and lenders get free business leads. If a lender wants any additional information, the same can be sought and also submitted by the borrower through the portal. The other significant demand-building step integrated into the platform relates to information on handholding support and the bankability kit. After registration with a phone number and email address, the applicant can take a self-assessment exercise which categorises the potential borrower as a 'trainee' or 'ready', and accordingly guides them. More than 17,000 handholding support agencies have been mapped location-/district-wise on the portal. Handholding agencies have been mapped by their area of expertise, like loan application filling, project report preparation and skill training. SIDBI, under the guidance of the RBI, has also integrated the CCC programme into the portal. It has created a pool of trusted counsellors CCC4CCC, which cater to MSEs while operating under a governance framework (prescribed dos and don'ts, fee and benchmarking). The CCCs complete the prescribed course through a designated institution (certification agency), which at present is the IIBF. After completing the course, they can then apply to the implementing and registering authority, i.e. SIDBI, for being considered as a CCC. Presently there are 525 CCCs/CCIs in 436 districts, and more than 7,760 applications have been serviced by CCCs. SIDBI's target is to have CCCs in all 712 districts of the country.

The bankability kit available on the site covers topics such as: what it takes to be an entrepreneur; basics like KYC and credit score; the process of applying for loans on the portal; aspects banks look into while appraising their applications; and basics of MSME banking. In addition, the portal also has sample project profiles to help potential entrepreneurs. One can choose the industry, the category of enterprise (micro, small, medium) and the loan amount as filters to get the relevant project profile.

The process flow on the portal in the case of a potential entrepreneur is outlined in Figure 4.6.

SIDBI's aspiration is to reach a stage where the borrower can choose from bids by lenders, but at present, despite commendable efforts, that goal seems far off. As of June 2018, total loans sanctioned were 4,256, involving an amount of Rs 910 crore. The online and digital initiative is laudable, but it seems more suited for SMEs. Field realities show that micro-entrepreneurs requiring Rs 1 to 5 lakh will either not be literate to go through the portal or may not have internet access to do so. It will require a lot of field-level awareness, and financial and digital training to build traction from micro-entrepreneurs on the portal.

SIDBI, during the last year (2017), transformed its vision into SIDBI.2, wherein it aims to be an all-India financial institution that can create an integrated credit and development support ecosystem for Indian MSEs, thus promoting their inclusive growth. The major change seems to be its stress on micro and small in the MSME space, and its equal focus on non-credit or developmental support for micro- and small enterprises. It proposes to achieve its objective through a six-pillared strategy with support from its partners and associates (Figure 4.7). It specifically includes focus on digital means, process re-imagination and impact indicator.

As it has been recently launched, the full dimensions of how it pans out will be interesting to watch—whether it remains true to the new vision or the new vision will turn out to be just an addition of a few things to its existing repertoire. Of

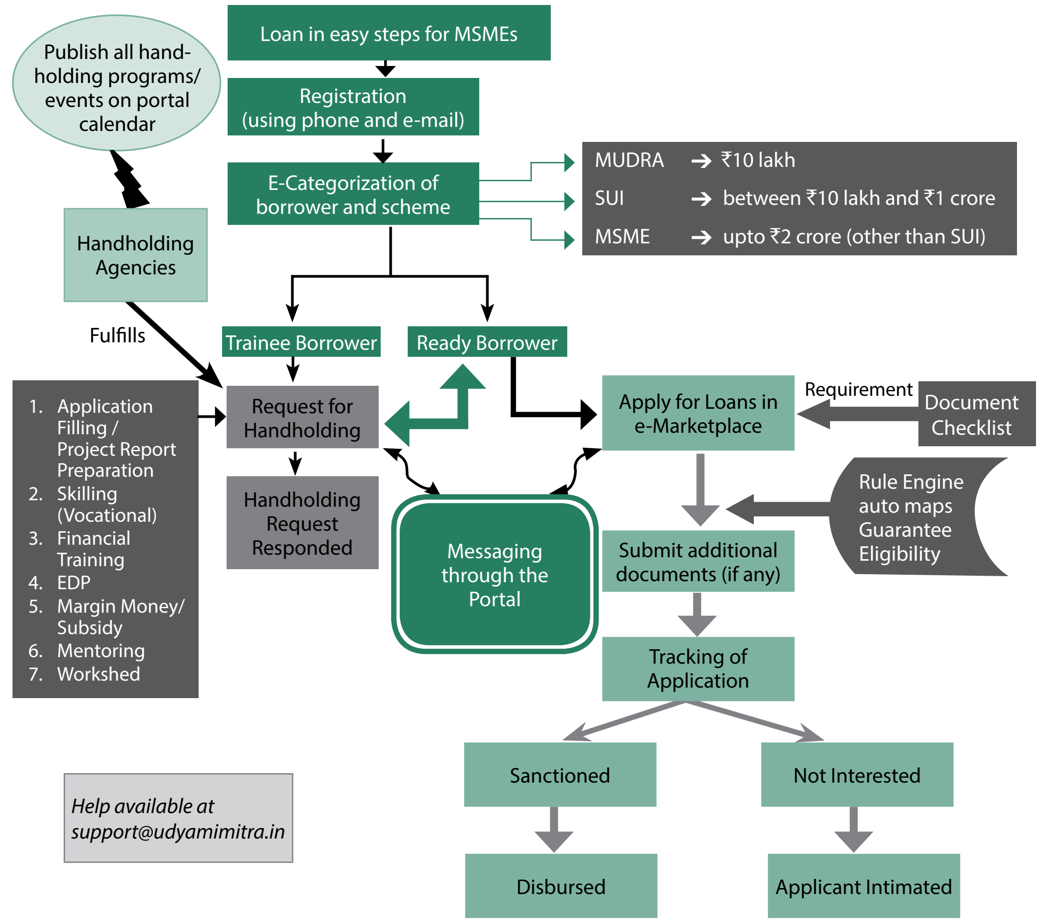


Figure 4.6: Process Flow under the Udyamimitra Portal

Source: www.udyamimitra.in

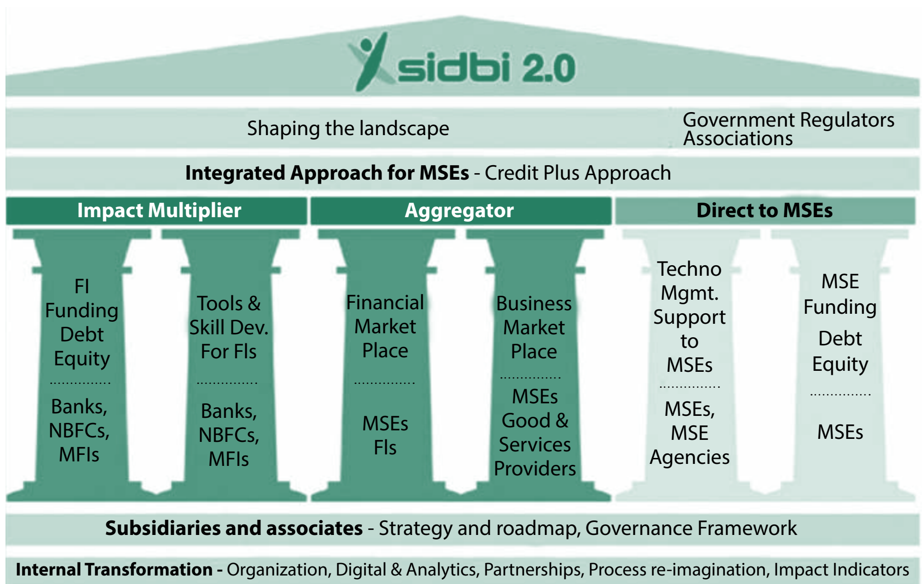


Figure 4.7: SIDBI's New Vision—V.2

Source: www.sidbi.in

particular interest is its focus on micro and small, as against its conventional focus in lending on small and medium, as well as the use of digital mode. The thrust on measuring impact and supplementing with developmental support is a welcome move, as typically public institutions have shied away from measuring impact.

A note of caution is needed here, as the section does not attempt to describe all of the existing schemes for even credit support, let alone the myriad schemes for subsidy, technology upgradation and cluster development. There are numerous such schemes at both the central and state levels like the PMEGP or ASPIRE Fund with SIDBI. The focus here is on recent changes in the national-level ecosystem of financing for micro- and small enterprises. In line with this focus, the setting up of three exchanges,[13] dealing with receivables of MSMEs, is not covered, as the process, commonly known as 'bills discounting', is not that pertinent to micro- and small enterprises.

CGTMSE

However, the operation of CGTMSE does need a mention, as credit guarantee has been prescribed as a mechanism for providing comfort to lenders in financing micro- and small enterprises. The Ministry of MSME launched CGS, and to operationalise the scheme the Government of India and SIDBI set up CGTMSE. Any collateral/third-party guarantee-free credit facility (both fund as well as non-fund based) extended by eligible institutions (banks including regional rural banks, and financial institutions including state finance corporations) to new as well as existing micro- and small enterprises, including service enterprises, with a maximum credit cap of Rs 200 lakh (20 million), is eligible to be covered. Incidentally, the guarantee cover amount is equal to eligible loans under the Udyamimitra portal. The guarantee cover available under the scheme is to the extent of 50 per cent, 75 per cent, 80 per cent or 85 per cent of the sanctioned amount of the credit facility based on the category of enterprise as well as the loan amount.

A few important changes to the scheme have taken place recently. In January 2017,[14] the list of eligible institutions was extended to cover select NBFCs and SFBs, and the limit of the credit facility cover was also raised from Rs 10 million to Rs 20 million. While this was a welcome move, capping coverage to loans not exceeding an interest rate of 14 per cent, including guarantee fee, may not be suitable for SFBs and NBFCs, whose lending rates are higher on account of high cost of funds. It also signals the policy duopoly of interest rate regulation in some sectors and free interest rates in others, and a reversion to the belief that interest rates are critical for micro-borrowers. In 2017 the government also increased the corpus of the trust from Rs 2,500 crore to Rs 7,500 crore, and announced that it will be fully funded by the Government of India. As of 31 December 2017, CGTMSE has covered more than 2.9 million micro-entrepreneurs, comprising a loan sanction amount of Rs 1,41,878 crore.

Among the host of initiatives taken in recent years, MUDRA being the most talked about, the following section examines the functioning of MUDRA and its significance for the microenterprise sector.

MUDRA—THE POLICY FOCUS ON MICROENTERPRISES

Evolution through the Years

MUDRA was registered as an NBFC with the RBI in 2015 under the aegis of SIDBI, in pursuance of the announcement made by the finance minister during his budget speech for the financial year 2015–16. The charter of MUDRA has seen evolution ever since its launch. The finance minister labelled it as 'funding the unfunded' in his budget speech and said:

> MUDRA Bank will refinance Micro-Finance Institutions through a Pradhan Mantri MUDRA Yojana. In lending, priority will be given to SC/ST enterprises. These measures will greatly increase the confidence of young, educated or skilled workers, who would now be able to aspire to become first generation entrepreneurs; the existing small businesses, too, will be able to expand their activities. Just as we are banking the un-banked, we are also funding the un-funded.[15]

Subsequently, the charter got drastically enhanced in the press release issued by the PIB on 1 April 2015, which listed the scope of MUDRA's work as follows:

> The MUDRA Bank would primarily be responsible for—
> 1. Laying down policy guidelines for micro/small enterprise financing business
> 2. Registration of MFI entities
> 3. Regulation of MFI entities
> 4. Accreditation/rating of MFI entities
> 5. Laying down responsible financing practices to ward off indebtedness and ensure proper client protection principles and methods of recovery

6. Development of standardised set of covenants governing last mile lending to micro/small enterprises
7. Promoting right technology solutions for the last mile
8. Formulating and running a Credit Guarantee scheme for providing guarantees to the loans which are being extended to microenterprises
9. Creating a good architecture of Last Mile Credit Delivery to micro businesses under the scheme of Pradhan Mantri Mudra Yojana[16]

The press release added key things like policy guidelines for small enterprise financing, regulation of MFIs, operation of PMMY as well as promoting good practices in the microenterprise lending segment. It seemed more of a new development bank on the lines of NABARD or SIDBI, also vested with some regulatory powers. It inspired confidence in many, including the author, that it would lead to the integration of the microfinance industry by bringing together NGO-MFIs and NBFC-MFIs under its umbrella, devising suitable regulation for the microfinance sector sans legal form-based regulation, and promote best practices and technology for micro- and small enterprises lending.[17] It was expected that it will play a wider developmental role, and though its starting focus would be microfinance, it would gradually cover the entire space, including banks and NBFCs. It was the developmental role which was considered more significant, such as technology solutions, strengthening the ecosystem with things like credit guarantee, and sensitisation and training of financial institutions. This was primarily because availability of funds, including with microfinance institutions, was/is not something which has a dominant role in non-lending to micro- and small enterprises.

The organisational charter, depicted on the MUDRA website in 2015 and 2016, also captured these broader objectives. However, the scope of work in the revised scheme of things is narrower (Fig 4.8).

In a write-up at a different place on MUDRA's website, the objectives have narrowed down to: 'MUDRA will provide refinance support, monitor the PMMY data by managing the web portal, facilitate offering guarantees for loans granted under PMMY and take up other activities assigned to it from time to time.'[18] Based on an analysis of its performance and interaction with stakeholders, this seems more in line with the functioning; the technology enabler and developmental role have not received priority as of now.

The scope of activities of MUDRA have narrowed down primarily to offering refinance support to the PMMY and operating a credit guarantee scheme. The PMMY, launched in parallel with MUDRA,

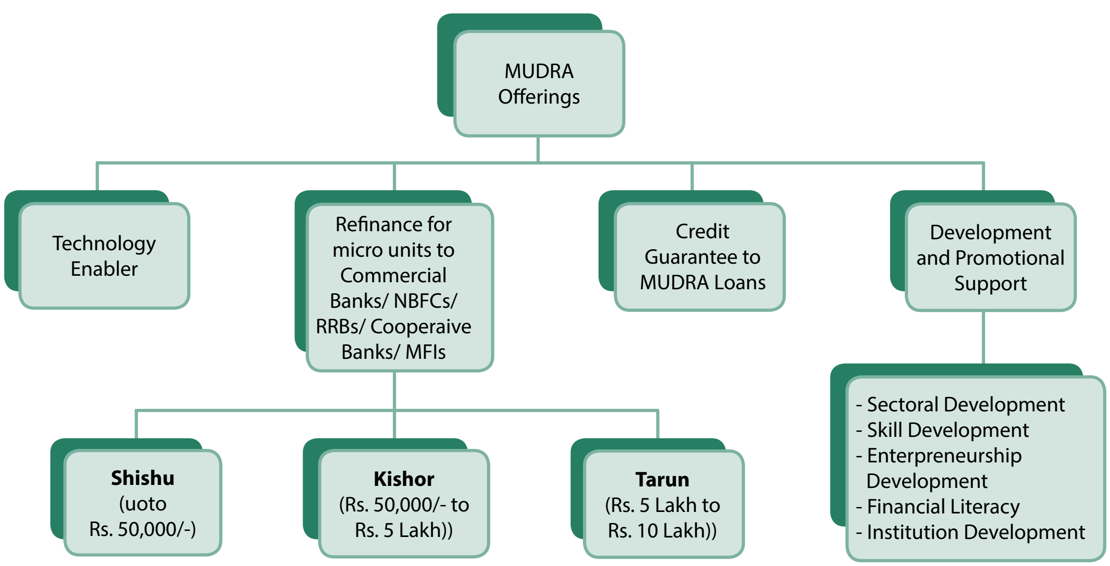


Figure 4.8: MUDRA Offerings

Source: https://www.mudra.org.in/Offerings. Accessed on 19 July 2018.

has three categories of loans for microenterprises. Loans below Rs 50,000 are called Shishu (infant), loans upwards of Rs 50,000 and below Rs 5 lakh are called Kishor (adolescent) and loans from Rs 5 lakh to Rs 10 lakh are called Tarun (young). Any financial entity, be it a bank, a small finance bank, a regional rural bank, cooperatives, an NBFC or an NBFC-MFI, disbursing of these loans is covered under the PMMY. The notable feature of the PMMY being publicised that sets it apart is that loans under it are collateral free. Though this relaxation was introduced by the RBI in its guidelines for MSME lending in 2014, it is often taken as a feature of MUDRA/PMMY loans. The RBI guideline is also mentioned in the PMMY brochure (Annexure 4.1). The other point relates to it moving up from the original vision of microfinance to microenterprise lending, as loans beyond Rs 1 lakh do not typically belong to microfinance in the Indian context. This is a welcome feature, as microenterprises, by their contribution, are integral to India's inclusive growth story, yet have faced severe credit constraints.

The funding base of MUDRA is derived from its paid-up capital and contributions from banks based on their shortfall in priority sector lending. As of 31 March 2018, MUDRA had paid-up capital of Rs 1,675 crore.

Performance under the PMMY: 40 Per Cent Jump In Disbursements during 2017–18

One of MUDRA's significant achievements is building up of a database of PMMY loans. Extensive data is available, which can be analysed institution-wise, state-wise, purpose-wise and client-wise. Earlier this data was available as an aggregate figure for banks in the RBI's Banking & Statistical Returns, and in MFIN data publications for NBFC-MFIs, but even aggregate data was not available for cooperative banks and NBFCs.

The performance of the PMMY is of critical importance, as the loans covered under it are for the 'lost middle' plus microfinance loans, which are typically below Rs 50,000. During the financial year 2017–18 all agencies together are reported to have disbursed Rs 2,46,347crore or Rs 2,463 billion under the PMMY, covering around 48 million loan accounts. That constitutes a healthy jump of 40 per cent in one year. Without factoring in double counting, this implies that 48 million borrowers were funded under the PMMY during 2017–18—an impressive achievement. MUDRA reports three figures in respect of financing under the PMMY: amount sanctioned, amount disbursed and amount outstanding. However, for the sake of analysis in this chapter, only loans disbursed have been taken into account, as sanctions may not result in disbursement, and outstanding amount does not give a true picture of financial assistance by reducing loan repayments during the year. The detailed performance—state-wise, loan category-wise and agency-wise—is given in Annexures 4.2 and 4.3, and the analysis here touches on the key highlights.

Agency-wise and loan category type share in PMMY disbursements during 2017–18: Shishu loans dominate with low average disbursement

The SBI and PSBs put together account for one-third of PMMY disbursements (35.56 per cent), which is expected, considering their share in the financial sector as well as their reach (Figure 4.9). Private sector banks have the second largest share of 20 per cent, followed by MFIs. However, clubbing SFBs with MFIs based on their recent transformation from MFIs provides a clear picture, and if the data is seen so, MFIs plus SFBs account for 27.54 per cent of PMMY disbursements. Foreign banks have been excluded from the analysis, as they account for a negligible share.

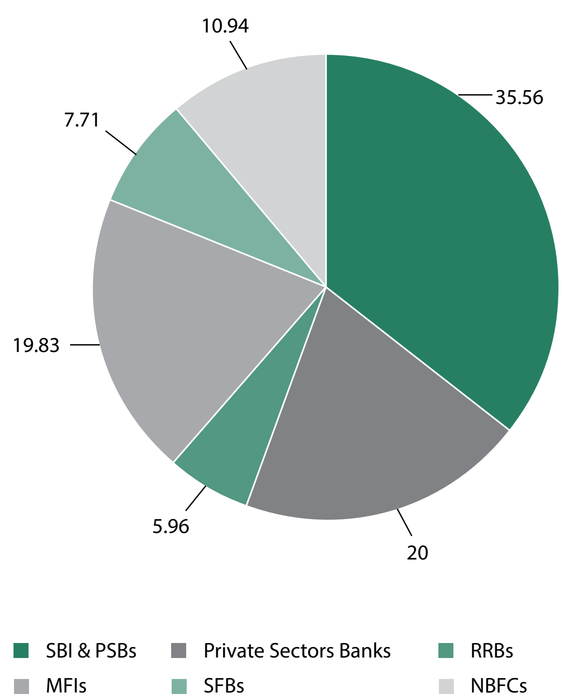


Figure 4.9: Agency-wise Share in PMMY Disbursements during 2017–18 (in per cent)

Source: Data given to author by MUDRA.

Table 4.4: Agency-wise Share in Loans Disbursed (in per cent)

	Shishu	Kishore	Tarun
SBI & PSB	6.55	51.12	64.85
Private sector banks	26.54	15.62	14.61
RRBs	2.68	11.80	3.52
MFIs	46.24	0.76	0.06
SFBs	12.96	3.73	4.04
NBFCs	5.03	16.96	12.89

Source: Data given to author by MUDRA.

The fact that MFIs plus SFBs have 27.54 per cent share that almost reaches the share of the SBI and PSBs put together is a telling commentary on the loan sizes under MUDRA. This is so because most MFI loans are below Rs 50,000.

While the above is the share of various agencies in aggregate disbursements under PMMY loans, including all three types of loans, the overall split between Shishu, Kishor and Tarun (Figure 4.10) shows that Shishu took the lion's share of 42 per cent in MUDRA disbursements, while Tarun (Rs 5 lakh to 10 lakh) took 24 per cent. Overall, three-fourth of loans disbursed under the PMMY during 2017–18 were below Rs 5 lakh.

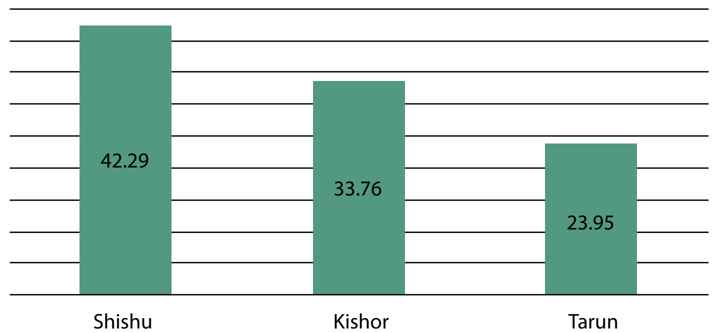


Figure 4.10: Share of Shishu, Kishor and Tarun during 2017–18 in PMMY Disbursements (in per cent)

Source: Data give to author by MUDRA.

The average disbursement under Shishu loans is Rs 24,426, under Kishor Rs 1,78,770 and under Tarun Rs 7,31,324. Not only do the smallest size loans account for 42 per cent of total PMMY disbursements, but also the average disbursement under this category is hardly 50 per cent of the maximum permissible loan size. Table 4.4 shows the agency-wise share across three different loan products under the PMMY.

MFIs plus SFBs make up for nearly 57 per cent share in Shishu loans, while the SBI and PSBs take up the major share under Kishor and Tarun loans. Although this is on expected lines, surprisingly even private sector banks have contributed mainly under Shishu loans. It appears that microfinance lending through banking correspondents by private sector banks is the reason behind their bigger share under Shishu loans. It is heartening that regional rural banks contribute 12 per cent to the Kishor category and are not focused on smaller loans to mitigate risk.

State-wise share in PMMY disbursements: Top five states account for 45 per cent of total disbursements

The first chapter talked about a regional skew in financial services as an issue, which is also presented in the chapter on microfinance institutions. The analysis of disbursements under MUDRA point to a similar skew, with the top five states (Tamil Nadu, Karnataka, Maharashtra, Uttar Pradesh and West Bengal) accounting for 45 per cent of total disbursements during 2017–18. It is acknowledged that this may be due to concentration of economic activity or financial institutions network, and hence it is not a plain critique, but the point is made from the perspective of this being an issue that needs further examination.

It is also noted that the names of states are also similar in the case of microfinance and the PMMY. A plausible reason seems to be the bigger share of Shishu loans in the PMMY, and nearly 50 per cent share of MFIs in Shishu loan disbursements.

Category-wise distribution of PMMY loans: Good coverage of women, SC, ST and OBC

The performance of the PMMY from this angle shows that it has done well in the coverage of women clients, as also SC, ST and OBC clients (Table 4.5).

The lack of congruence between a bigger share in loan accounts and loan amount disbursed is due to the fact that the above categories—women, SCs, STs, OBCs—dominate under Shishu loans, while

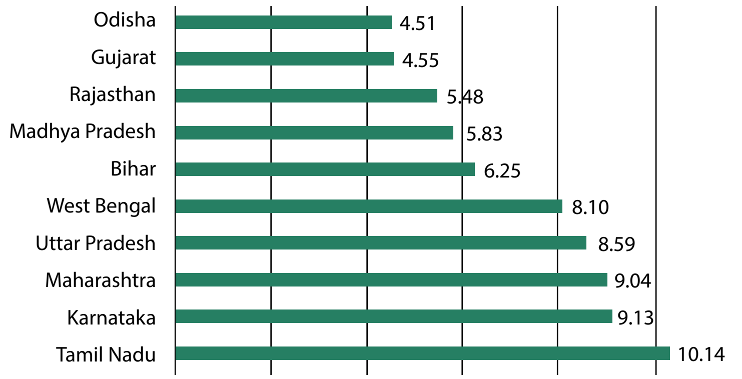


Figure 4.11: Top 10 States in PMMY Disbursements, 2017–18 (in per cent)

Source: Data given to author by MUDRA

Table 4.5: PMMY Loans to Women, SCs, STs and OBCs (in per cent)

	Loan accounts	Loan disbursed
Women	69.72	40.65
Scheduled Castes	17.67	9.61
Scheduled Tribes	5.28	3.13
Other Backward Classes	31.54	21.22

Source: Data given to author by MUDRA.

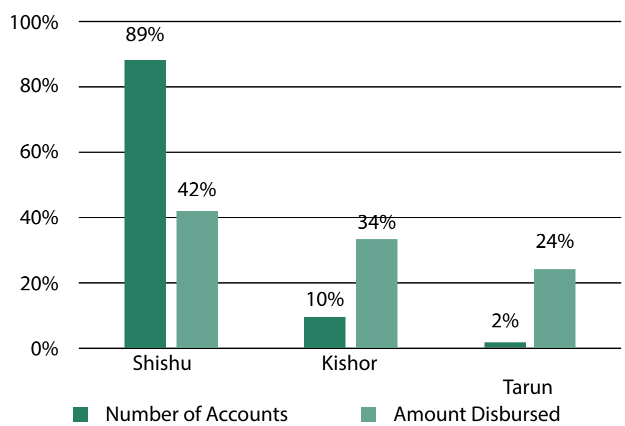


Figure 4.12: Share of Loan Categories in PMMY Loans, 2017–18 (in per cent)

Source: https://www.mudra.org.in/PMMYReport. Accessed on 2 August 2018.

their share under the highest category loan of Tarun is negligible. SCs and STs account for 1.6 per cent of Tarun loan accounts, Other Backward Classes have 9 per cent share and women have a smaller share of 9.07 per cent. The overall higher coverage of women is due to their pre-eminent share under Shishu loans, which in turn is mainly contributed by MFIs.

Based on the above discussion, it can be inferred that coverage in discrete numbers is higher under Shishu, but the disbursed amount is low under Shishu loans. For moving on to effective microenterprise lending, there is a need to do more under Kishor and Tarun by way of covering more clients as well as including all sections of society equitably.

The Contribution of MUDRA Refinance to PMMY Lending: 2.76 Per Cent in 2017–18

As MUDRA's focus has been on refinance and data collection under the PMMY, it is pertinent to put the contribution in perspective. The data collection work is appreciable, as it provides very valuable granular data which can be analysed for an effective policy design. MUDRA provides refinance to agencies backed by its equity, and contribution to the MUDRA corpus is made by banks from their priority sector shortfall. As of March 2018, MUDRA had drawn Rs 15,000 from the priority sector shortfall corpus. The present rates of refinance are given in Table 4.6.

Thus, the lending rate of all other agencies, except MFIs, on PMMY loans refinanced by MUDRA is presently in the range of 10–12 per cent. However, MFIs on account of higher operational cost, plus MUDRA refinance being a small part of their fund base, lend at higher rates. The cumulative refinance support provided by MUDRA to all agencies till 31 March 2018 stands at Rs 13,338 crore, excluding Rs 1,025 crore of securitisation transactions. The total refinance amount disbursed during 2017–18 was Rs 6,796 crore, while the total credit accounted

Table 4.6: Refinance and Lending Rate of MUDRA as of June 2018

Institution	MUDRA refinance rate (in per cent)	Ceiling on interest rate to be charged by lending institutions to the ultimate borrowers
Banks/SFBs	4.6	Not more than MCLR plus 100 bps of refinanced banks.
RRBs/Cooperative banks	4.6	Not more than 3.5% above MUDRA's lending rate or 10%, whichever is higher
NBFCs	6.85	Not more than 6% over and above MUDRA's lending rate
NBFC-MFIs	6.85	Governed by the norms of priority sector lending by banks to MFIs, which provides for 10 to 12% interest margin to MFIs

Source: MUDRA website. Accessed on 3 August 2018.

for by the PMMY during the same period was Rs 2,46,347 crore or Rs 2,463 billion. Thus, MUDRA refinance accounted for mere 2.76 per cent of the total credit. It clearly shows that the MUDRA refinance contribution to ground-level disbursements is negligible, and it is not clear whether it serves any purpose.

Since its inception, banks have been the major beneficiaries of MUDRA refinance, having 65 per cent share in cumulative disbursements, followed by MFIs at 17 per cent, which is in line with their share in PMMY loans. It is this aspect that has been questioned in various articles. In a recent unpublished monograph from the Gujarat Institute of Development Research on financing of MSMEs, the authors say that MUDRA has not made any significant contribution in the supply of funds, and the PMMY scheme 'has only made banks reclassify income generation loans up to the loan size of a million rupees sanctioned, on or after April 8, 2015 as PMMY loans'.[19] Several newspaper reports have also commented on this rebranding of small loans up to Rs 1 million as PMMY loans, adding that banks and other financial institutions have already been lending to this segment.[20]

Although the financing aspect of MUDRA is not significant in terms of numbers, field visits by the author and interaction with bankers clearly brought out the fact that the popularity of PMMY loans through advertisements has created pressure on banks to provide small loans. Agencies like NRLM and other NGOs take on the role of facilitating MUDRA loans for their members, and field-level awareness of the scheme is high. Bankers are flooded with MUDRA loan requests. However, bankers do not feel confident about the repayment capacity of prospective borrowers. It is a tough situation for bankers to balance numerous loan applications on account of wide publicity and the required prudence for ensuring credit quality. Recent newspaper reports also indicate that banks are worried about this, and a banker was quoted as saying:

> We are happy that Pradhan Mantri Mudra Yojana (PMMY) is an encouraging scheme, which generates self-employment, and instils confidence among jobless people, but at the same time its recovery from the loan takers is not guaranteed, as the tag of no-collateral is attached to it. Therefore, we urge the government to find out a proper mechanism, to prevent this small loanee segment from becoming bad loans, and protect bankers as well.[21]

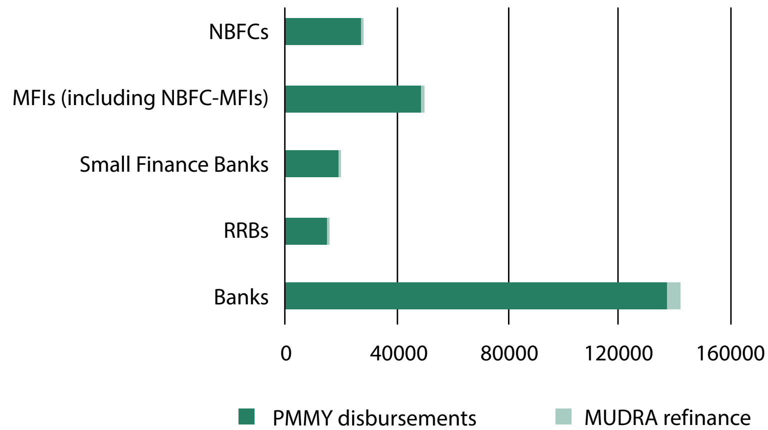


Figure 4.13: PMMY Disbursements and MUDRA Refinance during 2017–18 (in rupees)

Source: Data given to the author by MUDRA

Other Ecosystem Interventions by MUDRA

Along with the scheme, MUDRA introduced the MUDRA Card to provide hassle free credit to small borrowers, allowing loan withdrawal on demand and flexibility in operation. It is a co-branded debit card on the RuPay platform with MUDRA and the issuing bank, issued directly or in association with any MFI. Till 31 March 2018, 8.53 lakh cards have been issued with a value of Rs 4,522 crore. For the benefit of small entrepreneurs 27 indicative project profiles have been uploaded on the MUDRA website. Compared with the total disbursements classified as PMMY loans, the MUDRA Card issuance is insignificant. Perhaps RuPay debit cards with Jan Dhan bank accounts have obviated the need for another debit card.

The MUDRA Credit Guarantee Scheme, after approval by the Government of India, was notified on 18 April 2016. MUDRA Credit Guarantee is extended through the creation of a fund called Credit Guarantee Fund for Micro Units (CGFMU), which is managed by the NCGTC, an agency promoted by the Government of India. Credit guarantee has been conceptualised to address the credit risk concern of lenders, as PMMY loans are to be collateral free. Given the granularity of PMMY loans, the MUDRA Credit Guarantee Scheme provides a portfolio guarantee. Under this, credit guarantee or risk sharing is provided for a portfolio of homogeneous loans instead of individual loan-by-loan guarantees. This is expected to create administrative efficiency and increase the receptiveness of the credit guarantee product. As of 31 March 2018, 55 registered institutions have taken advantage of this facility, involving 29,38,116 loan accounts covering an amount of Rs 39,883 crore. Details of the scheme, including the risk premium amount, are available at the NCGTC website.[22] Compared to disbursements under the PMMY, the corpus of the credit guarantee fund at Rs 2,500 crore is low and needs to be enhanced. Credit risk is the main factor constraining lenders to increase their exposure under the PMMY.

MUDRA has also introduced a new funding scheme through securitisation and participated in 23 investments in PTCs aggregating to Rs 1,025.44 crore till 31 March 2018.

MUDRA is subscribing to PTCs originated by NBFCs/MFIs, wherein the portfolio is PMMY compliant. As securitisation deals are from MUDRA's own funds, it not only allows MUDRA to leverage its capital, but also enables small and medium-sized originators to access the capital market at affordable rates. MUDRA believes that securitisation will be its focus in the coming years, and this will create immense value, as it is an off-balance-sheet funding product under which capital benefit is applicable to the originator.[23] MUDRA is currently also working on a financial literacy app and has uploaded various model scheme profiles for entrepreneurs on its website.

As the financing aspect of MUDRA does not create any substantial impact owing to its limited size, and considering that availability of funds with banks or MFIs is not the primary issue, it will be worthwhile for MUDRA to focus more on ecosystem improvement. This can be done through the expansion of its current work on credit guarantee and seeding new aspects like financial literacy, skill training, including financial management training of entrepreneurs, sensitisation of bankers on the business proposition of small loans and appraisal skills, piloting of technology innovations for lenders as well as entrepreneurs, and policy advocacy for micro- and small enterprises. Focusing on refinance is neither needed by the sector nor does it seem to be impactful.

ADDITIONALITY OF INTERVENTIONS ON MSME LENDING: ABSENCE OF CLEAR EVIDENCE

The above sections show the importance attached by policy to increasing flow of credit to the MSME sector, especially to the micro and small or the 'lost middle'. While many of the measures are relatively new, it is still worthwhile to examine the outcome of these steps in terms of credit flow to MSMEs.

Data provided by the RBI on lending to MSMEs is a useful pointer to how these interventions are influencing the lending scenario of banks. Even the RBI data can be looked at in two slices: one is the category of enterprise and the other is the size of the credit facility. Under category, the RBI provides time series data on sector deployment of non-food gross bank credit in Table 49 of its publication, *Handbook of Statistics on Indian Economy.*[24] Although this offers useful insights by clubbing the micro and small categories, its usefulness for financial inclusion is limited, as small enterprises may not necessarily belong to the 'lost middle'. Moreover, since 99 per cent of enterprises are micro, clubbing does not provide insights into additionality in micro-lending.

The other slice of data available from the RBI for banks comes from Banking and Statistical Returns, which provides information on amount outstanding under various sizes of credit limit.[25] For microenterprises, loan accounts below the credit facility of Rs 1 million can be taken over a period to analyse the additionality of interventions, and this limit also corresponds with the maximum permissible loan limit under MUDRA or PMMY loans.

In addition to these sources, the analysis also draws on state-level credit by banks provided by the RBI, data on NBFCs' lending provided by the RBI, and *MSME Pulse*, the new initiative of SIDBI and TransUnion CIBIL. *MSME Pulse* provides an integrated picture of lending by clubbing banks and NBFCs, as also reporting on NPA trends, but the classification used for the categorisation of enterprises is based on the size of the credit limit. Thus, these different sources present different slices of data, and one can try to derive some conclusions by looking at each data set.

The time-series data on total industrial credit (includes lending to micro-, small, medium and large enterprises) throws up useful insights. From 2010–11 to 2017–18, while the total industrial credit has gone up from Rs 13,115 billion to Rs 26,993 billion—doubling in eight years—the annual growth has been quite uneven and even becoming negative in certain years (Figure 4.14). The pattern of uneven growth is seen for both industry as a whole and for the micro and small category. Overall, growth rates started declining from 2010–11 and have started going upwards only last year. Banking sector issues related to higher NPAs seem to be the answer for this declining trend in growth rates.

Further, in the overall industrial credit outstanding, the share of micro and small is quite

Table 4.7: Percentage Share of Various Categories in Industry Credit (2010 to 2018)

	Micro and small	Medium	Large
March 2010	15.7	10.1	74.1
March 2011	13.1	7.3	79.6
March 2012	12.2	6.4	81.3
March 2013	12.8	5.6	81.7
March 2014	13.8	4.9	81.2
March 2015	14.3	4.7	81
March 2016	13.6	4.2	82.2
March 2017	13.8	3.9	82.3
March 2018	13.8	3.8	82.3

Source: RBI, Banking and Statistical Returns. https://rbi.org.in/Scripts/AnnualPublications.aspx?head=Basic%20 Statistical%20Returns. Accessed on 26 October 2018.

low at 13.8 per cent (Table 4.7), and it has remained more or less at the same level throughout the nine-year period. The share of medium enterprises is reducing every year and is being compensated by large enterprises. The area of our concern in this report, i.e. micro and small, does not show any improvement in its share of industry credit. From the above it is clear that the exposure of banks to micro and small in their overall portfolio is not growing. Annexure 4.4 gives the time-series data of non-food credit by banks, including to MSMEs.

Another piece of analysis of the relative share of industry credit in non-food gross bank credit shows a declining trend. Much of it has to do with credit facility to large enterprises, as they account for around 80 per cent of industry credit. The share of industry credit in non-food loans outstanding was 43.15 per cent in March 2010, which came down to 37.77 per cent in March 2017.

In a recent unpublished paper referred to earlier in the section on MUDRA, the authors also point to this by doing a further sub-analysis of the share of MSMEs in non-food credit, which is a subset of the overall credit to industry (Figure 4.15). It is seen that but for a brief period from 2013 to 2015, the share has been falling.

The other way of looking at data, as mentioned earlier, is by analysing it by the size of loans. An analysis of loans below Rs 10 lakh by scheduled commercial banks in India, disaggregated into three categories (less than Rs 25,000; Rs 25,000 to Rs 2 lakh, and Rs 2 lakh to Rs 10 lakh), does not inspire much confidence. The analysis has been referred to in Chapter 1 and the key takeaways during the period 2012–17 are as follows:

- Growth in the number of loan accounts and amount outstanding in the case of loan categories

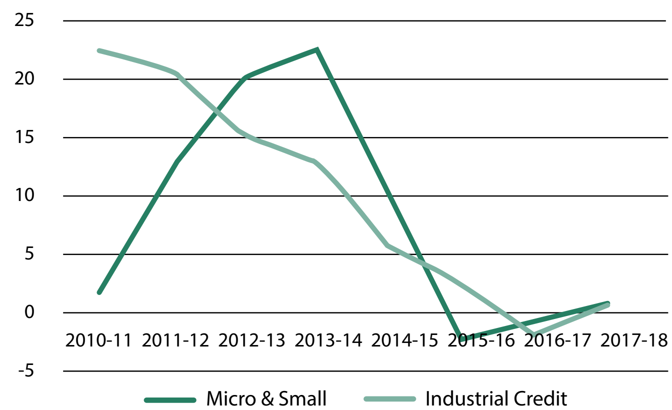


Figure 4.14: Annual Growth in Loans Outstanding to Industry (in per cent)

Source: 1. Data for FY 2010–2017: Handbook of Statistics on Indian Economy, Table 49. https://dbie.rbi.org.in/DBIE/dbie.rbi?site=publications. Accessed on 12 July, 2018.
2. Date for 2018: 'Sectoral Deployment of Bank Credit,' Press release on http://rbidocs.rbi.org.in/rdocs/content/docs/PR2858SD. Accessed on 12 July 2018.

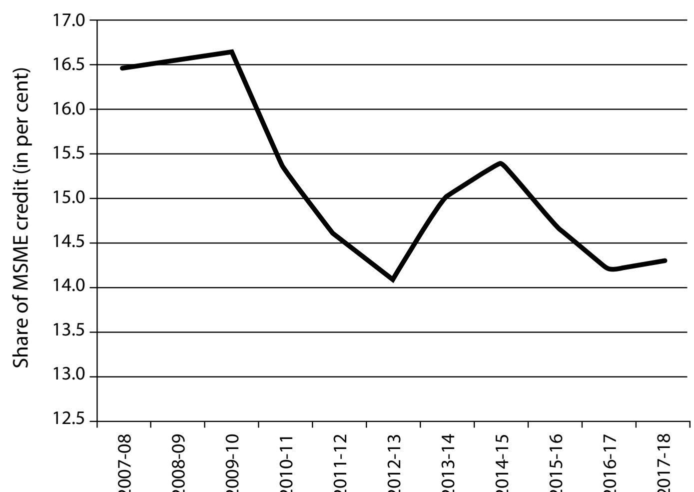


Figure 4.15: Share of MSMEs in Non-Food Credit (2007–8 to 2017–18)

Source: Tara Nair and Keshab Das, 'Financing MSMEs in India: Antecedents and Emerging Challenges', unpublished monograph, Gujarat Institute of Development Research, 2018.

of Rs 25,000 to Rs 2 lakh and Rs 2 lakh to Rs 10 lakh are stagnant, with a declining trend line.

- In the case of loan category below Rs 25,000, the trend is volatile, with wide upswings and downswings.
- The number of loan accounts below Rs 25,000 in March 2017 is 24 per cent less as compared to in 2011.
- As a consequence, the loan amount outstanding under these accounts is also 13 per cent less in 2017 than in 2011.

However, these figures cannot be attributed to industry or MSME, as they pertain to the entire lending portfolio of banks—MSMEs would be a subset of this. The problem of definition and the different data sets alluded to above are reflected in the above analysis. It would be good to have the data pertaining to micro- and small enterprises as per credit facility, which would enable an analysis of the number of microenterprises having a credit facility below Rs 1 million. Despite the unavailability of this data, the above analysis shows that the share of micro- and small enterprises in bank lending has fallen over the last 10 years, while their share in the overall industry credit at present is almost similar compared to 2011.

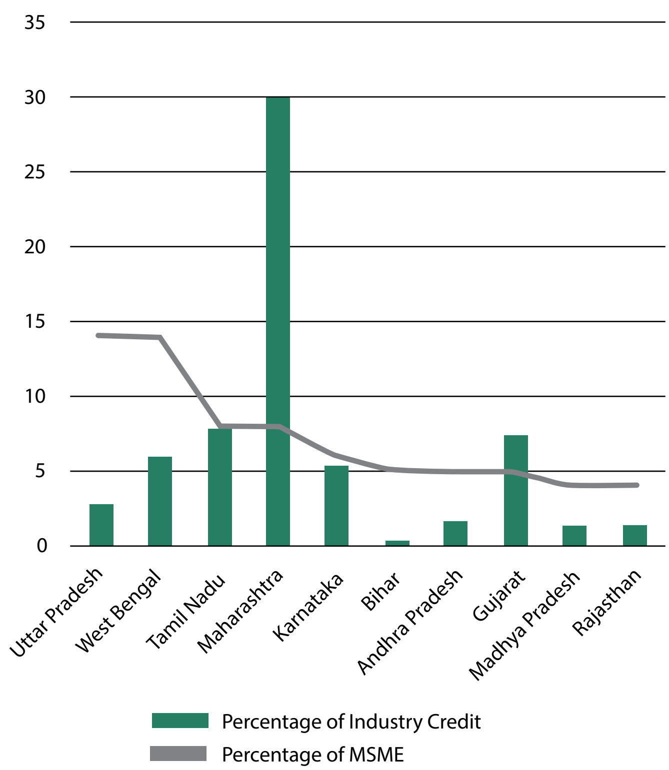


Figure 4.16: Top 10 States with MSMEs and Their Share in Industrial Credit by Banks

Source: RBI, BSR Table 5.6. https://dbie.rbi.org.in/DBIE/dbie.rbi?site=publications. Accessed on 26 October 2018.
Ministry of MSME, *Annual Report 2017–18*. https://msme.gov.in/relatedlinks/annual-report-ministry-micro-small-and-medium-enterprises. Accessed on 26 October 2018.

The data on financial assistance by banks being highly skewed towards large enterprises as well as the unavailability of state-wise data based on enterprise category do not allow a comparison of the presence of MSMEs with the credit flow. Combining data pertaining to the number of MSMEs in the top 10 states and the industrial credit flow to these states only reinforces the point that the presence of MSMEs has no relation to industry credit. As per the Ministry of MSME's data, the top 10 states account for 73 per cent of total MSMEs in the country, with the top 2 states, Uttar Pradesh and West Bengal, accounting for 14 per cent each. In the flow of state-wise industry credit, Maharashtra and the National Capital Region together account for around 50 per cent of the credit flow (Maharashtra 29.98 per cent and the NCR of Delhi 18.86 per cent). This shows the heavy regional skew in industry credit and no linkage between the presence of MSMEs in a state and the industrial credit flow, which is focused on large corporates.

Sector observers and news reports in recent times have noted that NBFCs have emerged as a major player in MSME financing. The data for NBFCs from the RBI, providing the bifurcation of industrial credit into category of enterprise for March 2016 and March 2017, shows that NBFC credit to industry is almost 30 per cent of bank credit in volume and is growing. The industrial credit by NBFCs, as of end March 2016 was Rs 8,063 billion (29.5 per cent of bank credit) and went up to Rs 8,940 billion by March 2017 (33.3 per cent of bank credit). This shows that NBFCs are playing a critical role in enterprise financing and their share is increasing.

However, when we look at NBFCs' exposure to micro- and small enterprises as a category, the exposure is quite low and is growing slowly. NBFCs' exposure to micro- and small enterprises as a percentage of their overall industry credit was a mere 5.68 per cent as on March 2017. Compared with bank credit to micro- and small enterprises, NBFC credit is 13 per cent in volume. While NBFCs have added one-third to bank credit for the enterprise sector, their contribution is tilted towards medium and large enterprises.

MSME Pulse, brought out by SIDBI and TransUnion CIBIL on a quarterly basis since March 2018, is a knowledge initiative of SIDBI's redefined vision. It is aimed at bringing out a composite picture of financing to the MSME sector, including banks and NBFCs, as well as at identifying trends in credit growth, NPA and opportunities. The March 2018 issue of *MSME Pulse* corroborates the credit constraint of MSMEs, indicating that out of 51 million MSMEs, only 5 million have access to formal credit. It provides useful data, but the definitional problem persists, as it defines enterprises based on the size of the credit facility. Microenterprise is that with less than Rs 1 crore credit, SME is Rs 1 to Rs 25 crore, mid- is Rs 25 to Rs 100 crore, and large is more than Rs 100 crore. It further subdivides micro into very small, micro 1 and micro 2; and SME into SME1, SME2 and MSME. It also introduces a new category of mid-enterprises. New parameters for classifying enterprises based on the size of the credit facility add to the existing problem of comparing available data sets.

In its June 2018 issue,[26] *MSME Pulse* shows that credit from banks, NBFCs, HFCs, cooperative banks, regional rural banks and other regulated lenders to enterprises registered an annual increase of 8.1 per cent during 2017–18. As credit from banks during the same period grew by 0.73 per cent (Figure 4.14), it is evident that the bulk of the increase has come from NBFCs and other regulated lenders. According to its classification, the micro segment registered the highest annual growth of 22.2 per cent and the large segment the lowest at 5.9 per cent. It is heartening that further classification of micro- and small enterprises shows that growth is highest in the lower segment (Table 4.8). Very small microenterprises, defined as those with a loan size below Rs 10 lakh, registered an annual increase of 35 per cent. This can be attributed to the MUDRA effect.

The report also mentions that PSBs are losing market share in the MSME category. Their share reduced to 50.4 per cent in March 2018 as compared to 60 per cent in March 2016. Among other lenders, PSBs also had the lowest annual growth of 2.1 per cent. NBFCs account for 11 per cent share in the MSME segment, while private banks have a 30 per cent share. However, private sector banks are more focused on the higher segment of MSMEs.

The green shoots in lending growth to the sector are also to be seen with the NPA trends. The report shows that except for the very small category (loans less than Rs 10 lakh), NPA rates rise with the size of the credit limit, reaching 13.9 per cent for loans between Rs 10 and 25 crore. The size–NPA correlation does not hold only in the lowest category of loans below Rs 10 lakh, which has a higher NPA of 11.1 per cent.

The NPA figures show that MUDRA loans are not maintaining good credit quality, which might have to do with the target approach being adopted in lending. More worrying is an analysis of 'new to credit' customers in the MUDRA segment during the last year (March 2016 to March 2017), which shows that NPA rates are even higher for new clients. Of new MUDRA segment clients 15.6 per cent turned NPA, and more importantly, 28.7 per cent exited the formal lending space. A recent news item,[27] based on the response to a question in the Lok Sabha by the finance minister, reported that nearly 3.91 million MUDRA loan accounts had turned into NPAs since the inception of the scheme as of June 2017. This aspect acts as a dampener to the otherwise positive story of green shoots in micro-lending and the addition of new clients.

Table 4.8: On Balance-Sheet Commercial Credit Exposure

	Very small (less than Rs 10 lakh)	Micro 1 (Rs 10–Rs 50 lakh)	Micro 2 (Rs 50 lakh–Rs 1 crore)	SME1 (Rs 1–Rs 5 crore)	SME2 (Rs 5–Rs 10 crore)	SME3 (Rs 10–Rs 25 crore)	TOTAL (up to Rs 25 crore)
March 2016	0.55	1.32	0.87	2.79	1.67	2.49	9.69
June 2016	0.56	1.39	0.93	2.98	1.76	2.59	10.22
September 2016	0.58	1.46	0.97	3.06	1.79	2.64	10.49
December 2016	0.56	1.42	0.95	3.06	1.81	2.67	10.47
March 2017	0.58	1.49	1.01	3.22	1.87	2.75	10.92
June 2017	0.64	1.57	1.06	3.36	1.93	2.80	11.37
September 2017	0.67	1.60	1.07	3.38	1.92	2.80	11.44
December 2017	0.77	1.75	1.16	3.71	2.07	3.00	12.47
March 2018	0.79	1.80	1.17	3.76	2.08	3.00	12.60
YoY credit growth (from March 2017–March 2018) (in per cent)	34.9	21.2	16.3	16.9	11.2	9.0	15.4

Source: MSME Pulse, June 2018. http://www.sidbi.in/files/MSME-Pulse-Edition-II.pdf. Accessed on 26 October 2018.

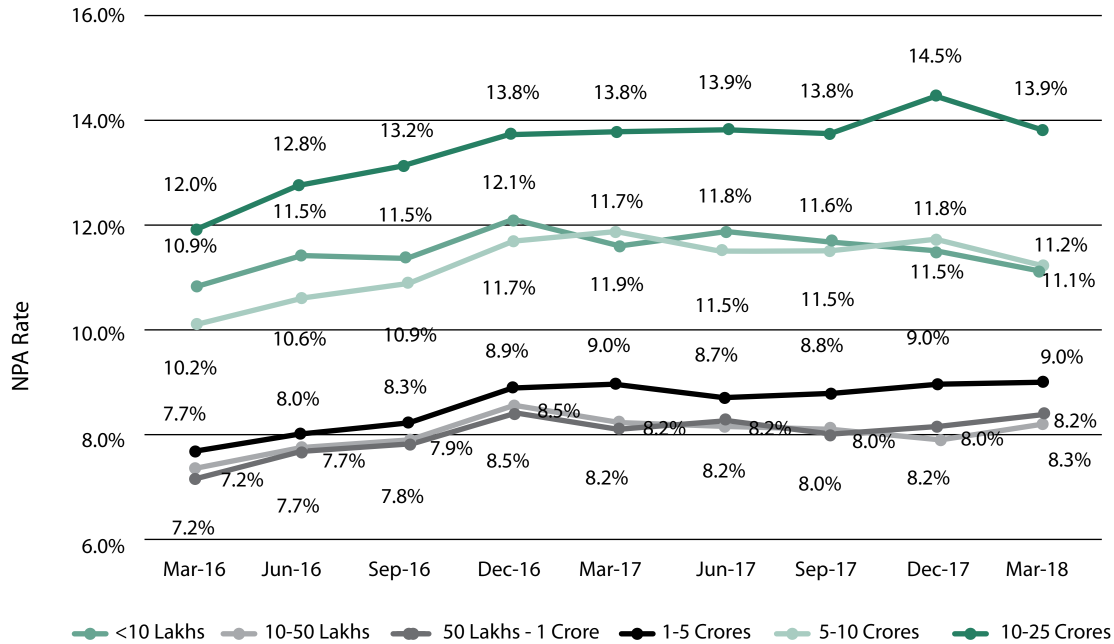


Figure 4.17: NPA Rates of the MSME Segment (in per cent)

Source: MSME Pulse, June 2018. http://www.sidbi.in/files/MSME-Pulse-Edition-II.pdf. Accessed on 26 October 2018.

The other aspect that comes out clearly from the report is that PSBs, despite losing share in the overall MSME market, maintain a dominant position in the segment below Rs 10 lakh, accounting for 79 per cent share, and their share progressively reduces in larger sized loans, dipping to 30 per cent in the loan category of Rs 5 to 10 crore. Private sector banks exhibit the reverse trend, and this is a commentary on the policy push for PSBs to increase lending for small loans. This concentration on smaller loan sizes by PSBs also reflects on their NPA position, while private sector banks and NBFCs have much lower NPAs in the range of 3 to 5 per cent.

Summing up the additional impact of policy measures to boost credit flow to MSMEs, a few critical aspects emerge. First and foremost is the issue of a lack of data uniformity, which makes analysis difficult. Figures coming from the RBI, *MSME Pulse* and MUDRA adopt different definitions, which leads to issues in comparisons and data mismatch. For example, according to PMMY statistics for 31 March 2018, the amount of loans outstanding across all agencies is Rs 2.02 lakh crore, while the on-balance-sheet commercial credit data for loans below Rs 10 lakh reported by *MSME Pulse* for 31 March 2018, is Rs 79,000 crore. As *MSME Pulse* also takes data across all lenders, it is not clear as to what explains the difference. The second trend which emerges is that there is a definite push in the micro segment (loans below Rs 10 lakh) due to the PMMY, and there is substantial growth here. However, two facts raise some alarm: (i) the inclusion of the NBFC-MFI portfolio in the PMMY has led to small loan sizes, and it is difficult to treat them as enterprise loans that can create jobs; and (ii) the higher NPAs under this category have to be seen as early warning signs that target-based lending does not work in the long run. It can give numbers in the short term, but over the long term it will create a problem of moral hazard in the credit market. The third trend that emerges is that the share of MSME lending in the overall non-food credit is falling, which implies other sectors are growing faster in credit access. Despite this fact and the almost doubling of MSMEs in the last 10 years, there is a persistence of their negligible share in industry credit, which needs to be addressed. The fourth trend relates to a skew in enterprise credit, both from the perspective of category (micro and small get a smaller share) and geographical share. Finally, one unmistakable trend is the emergence of NBFCs and private sector banks as significant players in the market, and hopefully SFBs will soon join the group.

In recent years newspapers, almost on a daily basis, carry news about fintechs entering the SME space, riding on the digital footprints established through the JAM trinity, as also mobilising private capital. Development agencies are also excited about the role of fintech in expanding credit flow to the SME sector. As shared above, SIDBI is also setting up a fintech platform for easing lending to MSMEs. This emerging landscape merits close scrutiny. In the following section, the first part describes the role and opportunities of fintech in SME lending, and the second part details the working of a new age MSME lender to showcase the building blocks of success.

FINTECH AND MSME LENDING

Emerging Models and Potential

The digital ecosystem changes in India by way of India Stack and the JAM trinity, and the former's associated features like e-KYC, are helping the fintech industry devise newer approaches to lending. India Stack (indiastack.org) is a set of APIs that allows governments, businesses, start-ups and developers to utilise a unique digital infrastructure to solve India's hard problems. It is also a move towards presence-less, paperless, and cashless service delivery. Traditional lenders, i.e. banks, primarily depended on traditional documents like income tax returns, balance sheets, VAT/sales tax returns and required hard collateral in the form of property title. This was done to minimise risk, but because of its unsuitability to the informal market, it constrains credit flow. Fintech lenders are adopting a host of newer digital methods of risk assessment, ranging from profiling of social media presence, analysis of digital footprints and psychometric testing. The assessment is also not enterprise centric but involves tie-ups with intermediaries associated with the borrowing enterprise; this provides alternate data points. In addition to risk assessment, availability of digital records through Aadhaar and e-KYC have reduced the need for feet on the street and simplified onboarding of the customer. Integration of credit bureau records in the app further lowers the cost of client acquisition. On security, new approaches, like taking payment directly from supplier to the enterprise and post-dated cheques in place of hard collateral, are emerging.

The use of fintech from onboarding to collections is depicted in Figure 4.18.

These digital approaches are also supported by emerging e-commerce or online marketplaces like Amazon, Flipkart, Ola, Uber and Oyo Rooms, which provide these lenders with a ready or captive market. The models which are emerging include:[28]

1. *Partnership between banks, lenders and e-players (hybrid model):* The SBI and Cholamandalam Finance have partnered with Ola to provide loans to its drivers.
2. *Combination of point 1 above and own balance sheet-based lending:* Capital Float, an NBFC, is an example of this. Loans on own balance sheet can also be through tie-ups with e-commerce players.
3. *P2P lenders:* Faircent is India's first P2P lending platform to receive a CoR as an NBFC-P2P from the RBI. Faircent does verification of both

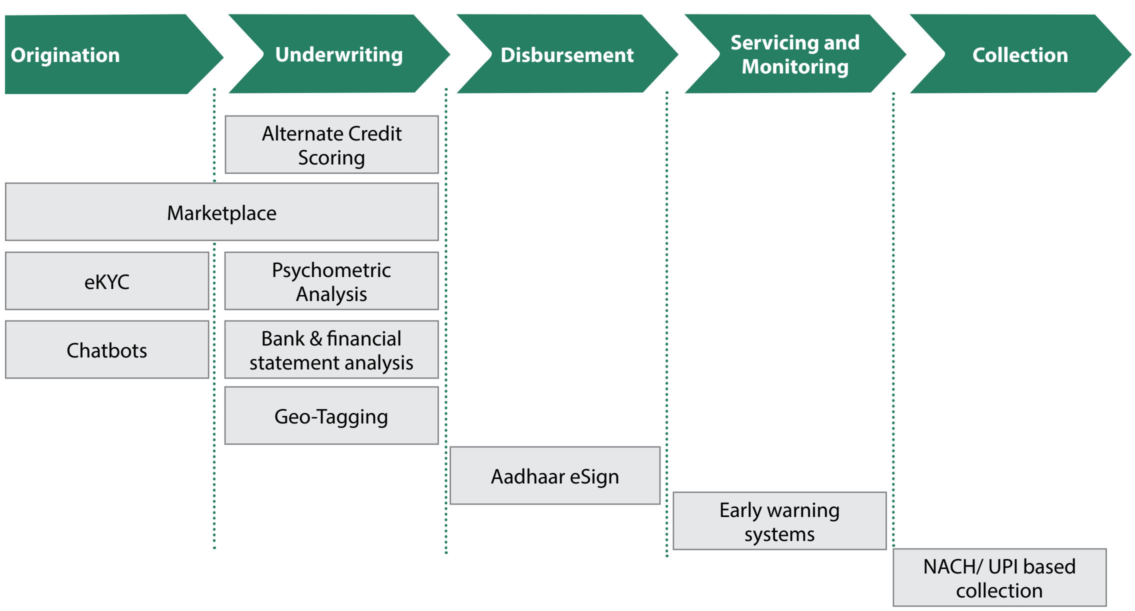


Figure 4.18: Fintech: Digital Applications through Loan Cycle

Source: blogs.worldbank.org/psd/trade/india-digital-finance-models-lending-small-businesses. Accessed on 1 August 2018.

lenders and borrowers, enables legal contract and helps lenders with recovery.

4. *Aggregators:* They do the screening and appraisal of borrowers, and link them to lenders, charging a processing fee. The product range is wide, from term loan, merchant cash advance and invoice discounting. Indifi is an example of an aggregator.

These new players and their use of digital means has created a buzz, leading people to say that 'MSME banking is likely to be the fourth-largest sector to be "disrupted" by fintech in the next five years, after consumer banking, payments, and investment/ wealth management' (PwC 2016 Global Fintech Survey Report).[29] SIDBI has also joined the space by creating what it calls a 'contactless platform' for lending to MSMEs (Box 4.2).

Box 4.2: MSME Loans in 59 Minutes

Finance Minister Arun Jaitley on 25 September, 2018 launched a portal to enable micro, small and medium enterprises (MSMEs) to get in-principle approval of loans within an hour without the need for a branch visit. The portal is for securing loan approvals only from Small Industries Development Bank of India, and five public sector banks (PSB)—State Bank of India (SBI), Bank of Baroda, Punjab National Bank, Vijaya Bank, and Indian Bank.

The web portal, www.psbloansin59minutes.com, will enable in-principle nod for loans up to Rs 10 million within 59 minutes for MSMEs. The solution uses sophisticated algorithms to read and analyse data points from various sources such as IT returns, GST data, bank statements, MCA21, etc. in less than an hour while capturing the applicants basic details using Smart analytics from available documents. The platform will be integrated with the Credit Guarantee Fund Trust for Micro and Small Enterprises scheme for checking the eligibility of borrowers. The loan processing will take place without any manual intervention till sanction or disbursement stage and the MSME borrower will not be required to submit any documents physically for in-principle approval

Source: https://www.business-standard.com/article/economy-policy/govt-launches-portal-to-grant-msme-loans-within-an-hour-118092600043_1.html. Accessed on 30 September 2018.

However, a careful analysis of the operating models shows that while digital can be an enabler in some stages of the loan cycle in the case of MSMEs, application of full contact-less solutions based on digital are not being able to reach the lower end of MSMEs—who are the largest in number and also most devoid of credit. Alternate data-based models, be it personal bank statements or social profile, have severe limitations in the BOP market. Microenterprise clients in this space do not have the needed velocity in their bank accounts—if they do have bank accounts—to be subjected to data analytics. They often do not have significant social network footprints either. Psychometric testing can work in such situations, but even new-age lenders believe that psychometry-based appraisal can only work as a second check and not as the primary and only check. The document requirements even in a contact-less or fintech platform—though submitted digitally—remain onerous. Aadhaar, address proof, bank statement of the last six months, and in some cases business registration, are required, the last automatically ruling out unincorporated enterprises. As discussed above, the Udyamimitra portal of SIDBI, despite having 360-degree information and catering to a loan size of up to Rs 2 crore, has seen low traction on online applications.

Fintechs or lenders wanting to cater to the micro-segment will have to combine elements of feet-on-the-ground model with digital means, like e-KYC and automated credit bureau checks, as well as flexibility in collateral and loan terms. Pure digital will cater to the higher end of enterprises that are formal entities and have the required documents as well as digital footprints. A recent newspaper report quoting a study supported by J.P. Morgan backs this inference by suggesting:

> Most Fintechs serve the affluent, tech literate customers in Tier I geographies, leaving over 80% of the addressable lower and middle income group untapped.... The study highlights the skewed nature of the Fintech business in the country. There are 1500 fintechs in India and 82% of them are located in three metros—Delhi, Mumbai and Bangalore.[30]

Though still few, there are also examples of lenders who have taken the combined approach of feet on the ground plus digital in serving microenterprises. Aye Finance, headquartered in Gurgaon, is one such lender and its operational model provides useful insights on microenterprise lending.

AYE FINANCE: INNOVATIVE LENDING APPROACH TO THE 'LOST MIDDLE'

Aye[31] Finance is a new-age finance company set up in April 2014 as an NBFC, with a committed vision of providing business loans to microenterprises (with an annual turnover ranging from Rs 10 to 100 lakhs) across the MSME sector in India. The founder has an extensive background in mainstream banking across countries. Along with the co-founder, he also has experience in microfinance, having worked with an earlier NBFC-MFI, now an SFB.

Aye believes that the credit needs of microenterprises typically fall below the radar of banks and established NBFCs, although they are positioned above the microfinance segment (Figure 4.19).

Backed by the belief that lending to these largely excluded businesses could be viable with appropriate methods and automation, the founders of Aye spent three months in the field conducting a detailed study of five such micro-business clusters in Meerut (sports), Aligarh (brass), Agra (shoe), Delhi (garment and footwear) and Jaipur (block printing and lacquer work). The intensive cluster-based studies covered areas such as business profile, technology used, seasonality in sales and payments, margins, loan preferences and availability of documents. The common elements that emerged through these studies are shown in Figure 4.20.

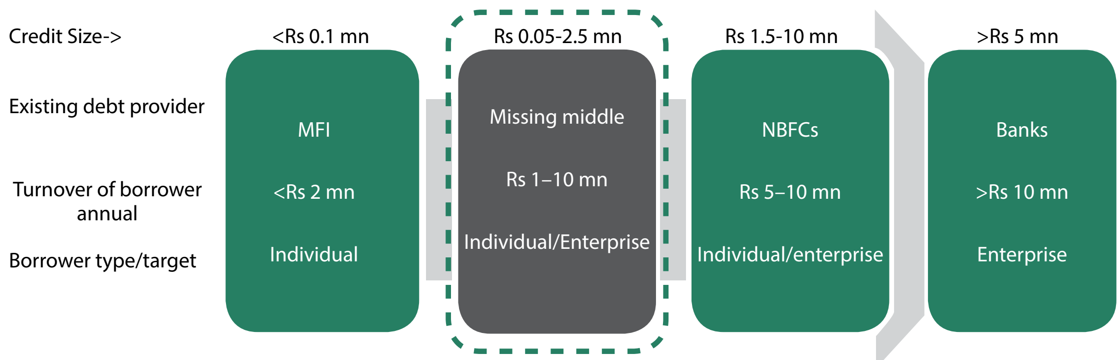


Figure 4.19: Market Segmentation for MSMEs as per Aye Finance

Source: Aye Finance, personal communication with author.

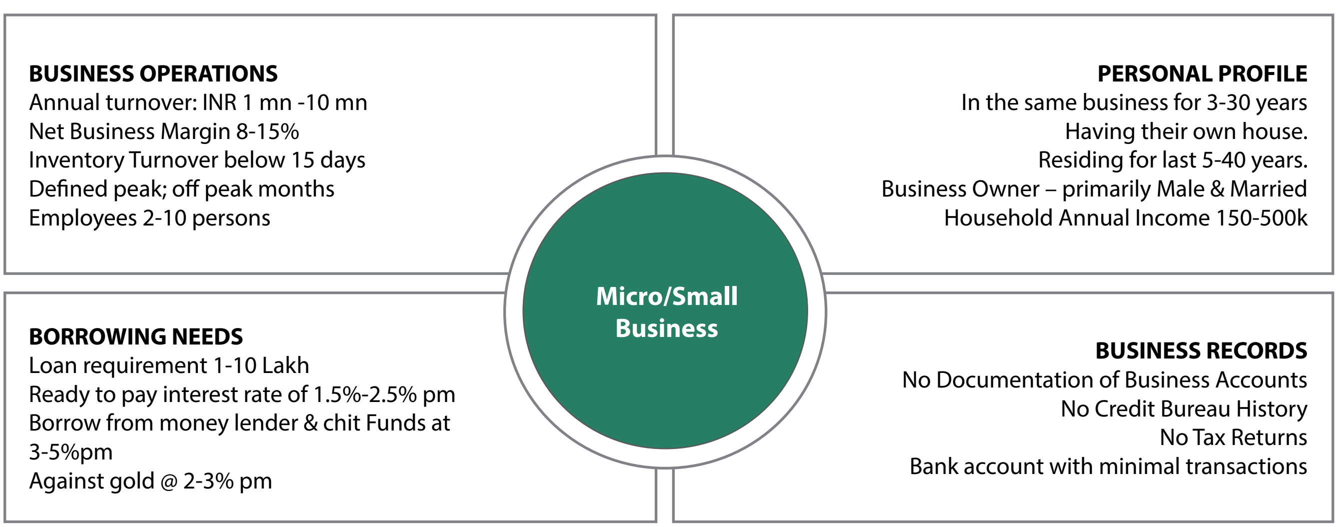


Figure 4.20: Key Findings across Clusters

Source: Aye Finance, primary market research.

While the financial need was evident, the challenge was in designing a credit appraisal tool in the absence of formal documents such as tax returns, accounts, bills, no previous credit history, and each business having its own typical way of maintaining records. Aye's philosophy in solving this puzzle has been to develop a deep understanding of each cluster and having cluster-specific financial and operational benchmarks, as well as the art of constructing financial statements and approximation of margins based on whatever documentation is available. This cluster-intensive and specific system is termed the Industry Cluster Enterprise (ICE) methodology, which is built on three pillars of credit appraisal, technology and analytics (Table 4.9).

The key to success has been extensive knowledge of the cluster. For example, an Aye staff member working with a shoes cluster has benchmarks on operational metrics—like number of shoes produced per worker, margin on sale, and production cycle—from inventory to receipt of sale proceeds. Deep insights into businesses operating in a cluster and learning the art of working with incomplete documents require intensive interaction with clients as well as investment in training the field staff. Aye has an elaborate training programme for its field staff, starting with a five-day induction, followed by refresher trainings every two months. Cluster knowledge is backed by investment in technology. Field officers capture the micro-business information on a tablet in an Android-based application developed by Aye and upload it to the cloud-based central server at the head office – the tablet is integrated with the Aadhaar-based KYC check as well as credit bureau checks. Normally, working with incomplete documentation and centralised credit decision making would require frequent back and forth between the field offices and the head office. Aye's investment in staff training and its ability to interpret the state of business from whatever data is available have helped it remove friction in customer processes and minimise

Table 4.9: ICE Methodology of Aye Finance

Credit appraisal—ICE method

- Lending targeted only at specified business clusters
- Insights around the industry–cluster–enterprise hierarchy build assessment model using input–output parameters with specified tolerance levels
- Buyer–supplier chain referenced for a business cluster
- Components of credit risks based on probability and impact of a default data modelled

Technology

- Automation focus on low-cost delivery and controls
- Cloud and mobile tech-based loan application process with integrated digital verifications (KYC, Credit Bureau, etc.) and business reference validations
- Systems with metrics to optimise TAT

Analytics

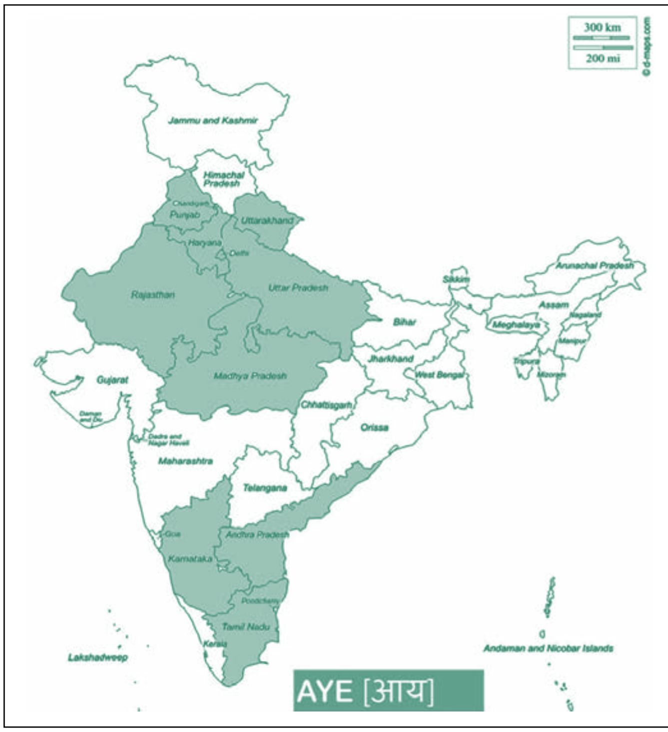
- Analysis of credit habits and seasonal swings in business
- Data analytics of financial, behavioural and psychometric parameters for new and repeat business customers
- Industry-specific early warning triggers

Source: http://www.ayefin.com/our-method/. Accessed on 18 July 2018.

Table 4.10: Loan Products of Aye

Mortgage loan	Hypothecation loan	Add-on loan
• Loan amount: Rs 3 to Rs 10 lakh • Repayment period: 2–5 years • Interest rate: 22–26% per annum • Secured against mortgage over marketable real property	• Loan amount: Rs 50,000 to Rs 3 lakh • Repayment period: 6 months to 3 years • Interest rate: 26–28% per annum • Secured against working assets of business	• Seasonal and festival loan requirement of Rs 50,000 to Rs 1 lakh • Repayment period: 2–6 months • Interest rate: 22–28% per annum • Existing loan customers with a good repayment track record can apply after 6 months of taking their 'primary' loan

Source: http://www.ayefin.com/products/. Accessed on 17 July 2018.



State	Branch	Industry Cluster **NOT EXHAUSTIVE**
Delhi	karampura	Women's shoes manufacturing
	Gandhinagar	Garment manufacturing
Haryana	Panipat	Rugs and Carpet power loom
	Ambala	Scientific Instrument
	Ludhiana	Hosiery work
Punjab	Jalandhar	Sports good manufacturing
	Abohar	Phulkari
Rajasthan	Jaipur	Lac bangle, Block printing and handicrafts
	Pali	Umbrella
	Ajmer	'Gota' work, power loom and marble work
UP	Firozabad	Glass work
	Aligarh	Brass, Iron work and lock making
MP	Indore	Light machinery, Trading
Karnataka	Yelahanka	Powerloom
	Tumkur	Wood/wooden furniture
Tamil Nadu	Trichy	Textiles
	Kumbakonam	Brasswork /Utensils
Andhra Pradesh	Vijayawada	Handloom

Figure 4.21: Aye's Outreach

Source: Aye Finance, personal communication with author.

Table 4.11: Loan Portfolio Details as on 31 March 2018

No. of loans disbursed	55,000
Loans disbursed (in Rs million)	6,750
No. of clusters covered	67
Hypothecation loans as % of total	70
'First-time' borrowers (in per cent)	89

Source: Aye Finance, personal communication with author.

unnecessary process bottlenecks. All disbursements are through bank accounts and repayment is through the e-NACH mandate. Post-dated cheques are mainly used for the interim period when the NACH mandates are being set up.

In its four-year journey Aye has spread to 10 states and reaches 67 different types of clusters through its 72 branches. The clusters cover a variety of manufacturing, trading as well as servicing industries, as shown in Figure 4.21.

The product line of Aye has been kept simple and flexible to meet the requirement of its target customers. Aye has primarily three loan products, the details of which are given in Table 4.10.

Despite loan products going up to Rs 10 lakh, the average size of loans remains at around Rs 1 lakh which is reflective of Aye's focus being on 'micro'.

6.1 Continued Focus on Client-centricity and Innovation

Working with micro-businesses hitherto excluded from the formal sector, Aye realised that these micro-units needed help with maintaining simplified business accounts. To meet this requirement, Aye has developed a mobile phone-based app which can be downloaded by micro-unit owners and Aye's staff is able to handhold them through its workings. This supports the philosophy at Aye, namely for the inclusion of microenterprises, providing funds has to be supplemented by the adoption of modern business methods.

In order to reinforce its credit appraisal tool built on assessing a micro-business, based on financial and operational benchmarks, Aye has developed a psychometric test with the help of academics from the Tata Institute of Social Sciences. At present, the psychometric test is used with repeat clients, and with improvement in probability of default estimation and predictive accuracy, it will be mainstreamed.

These innovations have helped Aye maintain a healthy portfolio quality, with gross NPA remaining below 2 per cent. This is creditworthy, as Aye works with a segment which has the highest potential of

Figure 4.22: A Screenshot of the mAye App

contributing to jobs and growth but has remained beyond the reach of formal finance.

CONCLUDING OBSERVATIONS

The above discussion shows that the intense policy focus on increasing credit flow to MSMEs is not showing the desired result, and much of the incremental lending to the micro-segment has come from the traditional base of NBFC-MFIs and PSBs. Higher NPAs in the case of PSBs and smaller loan sizes in the case of MFIs further affect lending quality and quantity. The policy stance of the government on increased formalisation of the sector through GST registration may create short- to medium-term problems for microenterprises. It is clear that a completely technology-driven model will not work in the micro-segment, nor will a target-driven approach. Conflating low-value, personal or consumption-smoothing loans with enterprise loans is also unhelpful. In a country, where microenterprises account for 99 per cent of enterprises, a majority of which are unincorporated, the policy should focus on evolving a syncretic approach, that is, drawing best practices of each agency—client connect of MFIs, fintech of NBFCs and new-generation banks, and the branch network of PSBs—to develop a model(s) for catering to microenterprises in a meaningful way. MUDRA, in place of existing refinance focus, can play this role. Attention also needs to be paid to demand-side issues by way of skill building, financial management skills and technology upgrade, which can lead to gradual formalisation. These aspects require an integrated national effort. It needs to be realised that microenterprises are here to stay. They will be the key engine of inclusive growth and we need to have a holistic perspective on meeting their needs in a meaningful way. The present approach of having a host of agencies and programmes targeting specific pieces of the puzzle without much of integration is not an optimal use of resources. The policy framework and institutions have, to their credit, always placed MSMEs as central to the development agenda, and more so in the last four years, but a holistic acceptance of the structural issues on the demand and supply side remains elusive. It is a difficult path with no quick solutions, but it is the right path and must be integral to any financial inclusion discourse.

ANNEXURE 4.1:
Mudra Loan Scheme—Salient Features

1. Brief background for introduction of MUDRA Loan Scheme by Govt. of India

As per NSSO survey (2013), there are around 5.77 crore small/micro units in the country, engaging around 12 crore people, mostly individual proprietorship/Own Account Enterprises. Over 60% of units are owned by persons belonging to Scheduled Caste, Scheduled Tribe or Other Backward Classes. Most of these units are outside the formal banking system, and hence are forced to borrow from informal sources or use their limited owned funds. MUDRA Loan Scheme has been proposed to bridge this gap.

MUDRA Loan Scheme will aim to increase the confidence of the aspiring young person to become first generation entrepreneurs as also of existing small businesses to expand their activities.

2. Brief details of the Product

MUDRA loans are extended by banks, NBFCs, MFIs and other eligible financial intermediaries as notified by MUDRA Ltd. The Pradhan Mantri MUDRA Yojana (PMMY) announced by the Hon'ble Prime Minister on 8th April 2015, envisages providing MUDRA loan, upto ₹ 10 lakh, to income generating micro enterprises engaged in manufacturing, trading and services sectors. The overdraft amount of ₹ 5000 sanctioned under PMJDY has been also classified as MUDRA loans under Prime Minister MUDRA Yojana (PMMY). The MUDRA loans are extended under following three categories:

✓ Loans upto ₹ 50,000/- (Shishu)
✓ Loans from ₹ 50,001 to ₹ 5 lakh (Kishore)
✓ Loans from ₹ 5,00,001/- to ₹ 10 lakh (Tarun)

More focus would be given to Shishu.

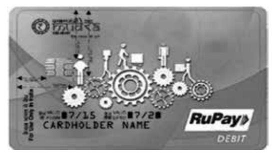
Accordingly, all advances granted on or after 8th April 2015 falling under the above category are classified as MUDRA loans under the PMMY. The application forms for such loans shall also carry the name "Pradhan Mantri MUDRA Yojana".

3. Eligible borrowers

✓ Individuals
✓ Proprietary concern.
✓ Partnership Firm.
✓ Private Ltd. Company.
✓ Public Company.
✓ Any other legal forms.

The applicant should not be defaulter to any bank or financial institution and should have a satisfactory credit track record. The individual borrowers may be required to possess the necessary skills/experience/knowledge to undertake the proposed activity. The need for educational qualification, if any, need to be assessed based on the nature of the proposed activity, and its requirement.

4. Purpose of Assistance/Nature of assistance.



Need based term loan/OD limit/composite loan to eligible borrowers for acquiring capital assets and/or working capital/marketing related requirements. The MUDRA loans are provided for income generating small business activity in manufacturing, processing, service sector or trading. The Project cost is decided based on business plan and the investment proposed. MUDRA loan is not for consumption/personal needs.

For the purpose of working capital limit, MUDRA has launched a new product called "MUDRA Card", which is a Debit card issued on RuPay platform, and provides hassle free credit in a flexible manner.

5. Amount of assistance

Upto to ₹ 10 lakh in three categories viz. Shishu, Kishore and Tarun.

6. Margin/Promoters Contribution

Margin/Promoters Contribution is as per the policy framework of the bank, based on overall guidelines of RBI in this regard. Banks may not insist for margin for Shishu loans.

7. Interest rate

Interest rates are to be charged as per the policy decision of the bank. However, the interest rate charged to ultimate borrowers shall be reasonable. Scheduled Commercial Banks, RRBs and Cooperative Banks wishing to avail of refinance from MUDRA will have to peg their interest rates, as advised by MUDRA Ltd., from time to time.

8. Upfront fee/Processing charges.

Banks may consider charging of upfront fee as per their internal guidelines. The upfront fee/processing charges for Shishu loans are waived by most banks.

9. Security

A. First charge on all assets created out of the loan extended to the borrower and the assets which are directly associated with the business/project for which credit has been extended.

B. DPN (wherever applicable).

C. CGTMSE (wherever felt desirable)/MUDRA Guarantee cover (as and when introduced).

In terms of RBI guidelines issued vide Master Circular on lending to MSME Sector (para 4.2) dated July 01, 2014, in respect of loans upto ₹ 10 lakh, banks are mandated not to accept collateral security in the case of loans upto ` 10 lakh extended to units in the Micro Small Enterprises (MSE) Sector. Banks are required to encourage their branch level functionaries to avail of the Credit Guarantee Scheme cover, wherever felt desirable.

10. Tenor of Assistance

Based on the economic life of the assets created and also the cash flow generated. However, MUDRA's refinance assistance will be for a maximum tenor of 36 months which will also be aligned to terms of allotment of MUDRA funds by RBI from time to time.

11. Repayment

Term Loan :- To be repaid in suitable installments with suitable moratorium period as per cash flow of the business.

OD & CC Limit : Repayable on demand. Renewal and Annual Review as per internal guidelines of the Bank.

12. Availability of the loan

Mudra loan under PMMY is available at all bank branches across the country. Mudra loan is also issued by NBFCs / MFIs who are engaged in financing for micro enterprises in small business activities.

ANNEXURE 4.2:
State-wise Progress under Various Schemes of PMMY during 2017–18

Bank Type : ALL Bank : ALL State : ALL
Scheme : ALL Financial Year : 2017-2018 Data Till Date : 31-03-2018

	State name	Shishu			Kishore			Tarun			Total		
		No. of accounts	Sanction amount (in Rs crore)	Disbursement amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disbursement amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disbursement amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disbursement amount (in Rs crore)
1	Andaman and Nicobar Islands	1,710	5.15	5.15	1,363	37.79	36.73	756	59.72	58.38	3,829	102.66	100.26
2	Andhra Pradesh	3,53,879	1,218.82	1,187.66	4,13,415	7,142.93	6,566.76	34,551	2,540.77	2,459.67	8,01,845	10,902.51	10,214.10
3	Arunachal Pradesh	9,137	23.28	23.14	1,236	36.51	32.91	631	49.71	47.22	11,004	109.50	103.27
4	Assam	15,58,335	4,320.53	4,311.15	1,45,421	1,646.95	1,583.47	9,248	702.26	675.70	17,13,004	6,669.74	6,570.32
5	Bihar	40,63,534	9,919.75	9,646.78	2,24,316	3,845.57	3,690.52	27,011	2,154.09	2,059.46	43,14,861	15,919.40	15,396.75
6	Chandigarh	9,391	29.94	29.08	6,786	224.08	219.72	2,080	165.96	160.35	18,257	419.98	409.15
7	Chhattisgarh	8,71,455	2,016.69	1,938.40	73,732	1,439.24	1,316.49	16,892	1,291.36	1,246.59	9,62,079	4,747.29	4,501.48
8	Dadra and Nagar Haveli	2,437	7.71	7.69	768	13.47	13.41	203	15.61	15.21	3,408	36.79	36.30
9	Daman and Diu	462	0.93	0.78	470	10.28	10.15	154	12.34	11.63	1,086	23.55	22.56
10	Delhi	1,45,979	458.02	450.08	65,530	1,715.87	1,684.47	30,288	2,276.26	2,222.80	2,41,797	4,450.15	4,357.35
11	Goa	26,766	85.87	84.42	10,028	215.89	209.43	2,603	197.51	190.60	39,397	499.27	484.45
12	Gujarat	12,30,455	3,529.28	3,506.40	2,24,098	4,437.87	4,336.13	46,673	3,419.38	3,359.99	15,01,226	11,386.52	11,202.52
13	Haryana	6,60,709	1,791.08	1,757.46	98,920	2,118.54	2,023.27	26,699	2,030.78	1,964.31	7,86,328	5,940.40	5,745.03
14	Himachal Pradesh	41,978	123.60	112.39	40,262	993.76	939.15	9,752	783.19	749.90	91,992	1,900.55	1,801.44
15	Jammu and Kashmir	19,532	69.04	67.74	73,095	1,725.60	1,678.84	10,498	792.15	768.26	1,03,125	2,586.80	2,514.84
16	Jharkhand	11,18,607	2,582.15	2,498.51	78,942	1,654.18	1,598.00	15,122	1,174.07	1,136.54	12,12,671	5,410.40	5,233.05
17	Karnataka	40,65,431	10,487.14	10,351.83	4,34,785	7,382.66	7,177.23	68,277	5,139.93	4,971.61	45,68,493	23,009.73	22,500.67
18	Kerala	20,35,426	3,219.71	3,167.46	2,25,274	4,033.16	3,971.94	29,105	2,207.09	2,143.16	22,89,805	9,459.97	9,282.57
19	Lakshadweep	612	1.93	1.62	400	8.57	7.72	32	2.45	2.20	1,044	12.95	11.53

	State name	Shishu			Kishore			Tarun			Total		
		No. of accounts	Sanction amount (in Rs crore)	Disbursement amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disbursement amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disbursement amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disbursement amount (in Rs crore)
20	Madhya Pradesh	26,48,183	7,090.18	7,011.07	2,04,239	4,391.28	4,130.88	46,701	3,404.69	3,215.57	28,99,123	14,886.15	14,357.52
21	Maharashtra	31,45,685	8,093.38	7,980.26	3,54,818	7,529.90	7,343.40	96,117	7,128.12	6,942.55	35,96,620	22,751.40	22,266.20
22	Manipur	27,973	81.55	80.88	4,507	82.49	71.47	706	55.55	48.33	33,186	219.59	200.68
23	Meghalaya	23,858	70.66	70.48	4,143	83.00	80.55	845	62.58	61.01	28,846	216.25	212.04
24	Mizoram	6,474	26.03	25.64	5,536	100.31	97.23	390	31.29	30.02	12,400	157.62	152.90
25	Nagaland	11,069	39.02	38.57	2,461	48.94	44.25	611	48.01	41.79	14,141	135.98	124.61
26	Odisha	33,22,007	7,531.78	7,278.07	1,26,864	2,416.40	2,302.14	21,441	1,610.73	1,535.67	34,70,312	11,558.91	11,115.88
27	Pondicherry	1,30,970	370.58	370.04	16,982	318.52	311.10	2,525	206.05	200.63	1,50,477	895.16	881.77
28	Punjab	6,69,630	1,918.06	1,880.28	1,19,363	2,410.17	2,325.78	30,843	2,395.59	2,318.06	8,19,836	6,723.82	6,524.12
29	Rajasthan	14,30,399	3,715.15	3,629.75	2,54,867	5,530.44	5,350.55	61,482	4,616.96	4,523.46	17,46,748	13,862.55	13,503.76
30	Sikkim	18,878	42.62	41.99	2,315	42.12	40.29	395	31.55	30.37	21,588	116.30	112.65
31	Tamil Nadu	53,66,167	13,266.17	13,237.23	4,31,666	7,407.89	7,176.10	62,332	4,657.62	4,567.59	58,60,165	25,331.68	24,980.92
32	Telangana	6,37,258	1,534.28	1,523.82	1,21,014	2,742.36	2,668.37	31,043	2,268.63	2,238.61	7,89,315	6,545.26	6,430.81
33	Tripura	3,66,127	1,048.51	1,046.92	32,049	348.26	330.41	1,123	88.20	83.27	3,99,299	1,484.96	1,460.60
34	Uttar Pradesh	39,63,399	8,581.82	8,396.56	3,62,732	7,596.67	7,171.13	75,086	5,899.40	5,606.77	44,01,217	22,077.89	21,174.46
35	Uttarakhand	1,88,604	572.65	559.58	55,269	1,149.70	1,101.81	10,910	850.87	818.69	2,54,783	2,573.22	2,480.09
36	West Bengal	44,97,279	12,128.52	11,909.15	4,36,208	5,850.78	5,555.31	33,799	2,572.89	2,506.30	49,67,286	20,552.19	19,970.76
	Total	4,26,69,795	1,06,001.60	1,04,228.05	46,53,874	86,732.16	83,197.09	8,06,924	60,943.34	59,012.25	4,81,30,593	2,53,677.10	2,46,437.40

Source: Data Provided by MUDRA to Author

ANNEXURE 4.3:
Institution wise Progress under PMMY in 2017-18

Bank Type : ALL   Bank : ALL   State : ALL
Scheme : ALL   Financial Year : 2017-2018   Data Till Date : 31-03-2018

	Bank name	Shishu (Loans up to Rs 50,000)			Kishore (Loans from Rs 50,001 to Rs 5.00 lakh)			Tarun (Loans from Rs 5.00 to Rs 10.00 lakh)			Total		
		No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)
1	**Bank Type: SBI and associates**												
1.1	State Bank of India	7,98,577	1,893.80	1,873.21	409067	11,258.15	11,093.39	2,02,361	15,638.95	15,596.52	14,10,005	28,790.89	28,563.12
	Total	7,98,577	1,893.80	1,873.21	409067	11,258.15	11,093.39	2,02,361	15,638.95	15,596.52	14,10,005	28,790.89	28,563.12
2	**Bank Type: Public sector commercial banks**												
2.1	Allahabad Bank	26,859	111.13	110.16	79422	1,552.03	1,531.86	16,188	1,136.56	1,124.39	1,22,469	2,799.73	2,766.41
2.2	Andhra Bank	1,58,748	440.11	426.53	100514	2,003.32	1,776.41	11,255	945.53	880.89	2,70,517	3,388.97	3,083.82
2.3	Bank of Baroda	61,594	246.30	237.94	141854	2,905.84	2,770.05	25,229	2,153.33	2,095.75	2,28,677	5,305.47	5,103.73
2.4	Bank of India	2,02,844	551.31	546.09	129465	2,807.42	2,652.65	30,483	2,403.12	2,271.63	3,62,792	5,761.86	5,470.37
2.5	Bank of Maharashtra	11,732	47.37	41.11	39438	1,002.46	895.43	12,895	1,103.27	995.82	64,065	2,153.10	1,932.36
2.6	Canara Bank	2,67,394	991.68	985.38	212343	4,001.67	3,868.17	34,032	2,671.52	2,581.73	5,13,769	7,664.88	7,435.28
2.7	Central Bank of India	46,856	186.59	132.39	57705	1,326.50	1,180.45	15,990	1,302.81	1,164.30	1,20,551	2,815.91	2,477.14
2.8	Corporation Bank	50,624	219.16	209.04	46631	934.07	924.74	12,710	1,051.44	1,048.90	1,09,965	2,204.67	2,182.67
2.9	Dena Bank	1,02,478	222.34	206.72	17636	381.40	360.05	3,326	268.28	260.41	1,23,440	872.02	827.17
2.1	Indian Bank	40,218	140.36	137.97	87167	1,380.67	1,253.77	8,210	664.58	645.72	1,35,595	2,185.61	2,037.46
2.11	Indian Overseas Bank	69,356	225.25	222.20	79743	1,222.78	1,173.66	6,428	508.31	487.13	1,55,527	1,956.34	1,882.99
2.12	Oriental Bank of Commerce	24,737	84.81	81.43	44953	1,029.68	958.96	15,550	1,309.84	1,300.79	85,240	2,424.34	2,341.18
2.13	Punjab National Bank	2,17,731	515.46	398.45	176323	3,465.05	2,948.14	34,343	2,857.37	2,441.81	4,28,397	6,837.89	5,788.39
2.14	Syndicate Bank	54,876	226.29	188.96	114791	2,471.14	2,112.78	15,710	1,247.87	969.74	1,85,377	3,945.30	3,271.48
2.15	Union Bank of India	41,160	162.37	143.47	128058	2,654.85	2,408.48	15,919	1,191.20	1,041.53	1,85,137	4,008.43	3,593.48
2.16	United Bank of India	15,243	62.06	60.34	47428	1,013.05	965.48	7,874	635.51	621.22	70,545	1,710.62	1,647.03

	Bank name	Shishu (Loans up to Rs 50,000)			Kishore (Loans from Rs 50,001 to Rs 5.00 lakh)			Tarun (Loans from Rs 5.00 to Rs 10.00 lakh)			Total		
		No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)
2.17	Punjab & Sind Bank	9,434	36.29	30.80	21600	464.35	408.99	6,462	509.15	464.52	37,496	1,009.79	904.30
2.18	UCO Bank	1,35,888	367.74	312.49	97360	1,632.39	1,496.03	8,145	669.84	589.56	2,41,393	2,669.97	2,398.08
2.19	Vijaya Bank	97,154	257.16	255.53	61191	1,170.03	1,131.35	11,601	925.77	903.18	1,69,946	2,352.95	2,290.06
2.2	IDBI Bank Limited	75,889	224.79	224.79	27160	623.56	623.56	9,722	785.60	785.60	1,12,771	1,633.95	1,633.95
	Total	17,10,815	5,318.59	4,951.76	1710782	34,042.27	31,441.01	3,02,072	24,340.93	22,674.60	37,23,669	63,701.79	59,067.37
3	Bank Type: Private sector commercial banks												
3.1	Federal Bank	880	3.96	3.79	2596	86.98	78.29	1,442	119.40	105.85	4,918	210.35	187.93
3.2	Dhanlaxmi Bank	5	0.03	0.03	36	1.01	1.01	3	0.22	0.22	44	1.26	1.26
3.3	Jammu & Kashmir Bank	12,476	41.68	41.28	54229	1,259.99	1,233.07	7,658	570.56	556.30	74,363	1,872.24	1,830.66
3.4	Karnataka Bank	904	2.42	1.33	4888	122.77	72.50	2,177	155.63	70.35	7,969	280.82	144.18
3.5	Karur Vysya Bank	1,267	5.91	5.86	3316	78.01	74.50	932	69.08	66.77	5,515	153.00	147.13
3.6	City Union Bank	120	0.53	0.53	101	1.78	1.78	9	0.75	0.75	230	3.07	3.07
3.7	Lakshmi Vilas Bank	3	0.01	0.01	60	1.06	1.05	41	2.31	2.31	104	3.38	3.37
3.8	The Nainital Bank Limited	283	0.95	0.94	532	14.87	14.85	215	16.84	16.84	1,030	32.67	32.64
3.9	Ratnakar Bank	87,450	156.95	156.95	13533	355.30	355.30	2,763	227.65	227.65	1,03,746	739.90	739.90
3.1	South Indian Bank	389	1.79	1.77	596	17.23	16.99	330	26.90	26.76	1,315	45.93	45.52
3.11	Tamilnad Mercantile Bank	1,366	5.51	5.38	4480	121.99	120.75	2,788	229.58	228.43	8,634	357.09	354.56
3.12	ICICI Bank	2,55,304	782.72	756.31	59893	1,892.91	1,892.77	39,502	2,843.23	2,841.14	3,54,699	5,518.85	5,490.22
3.13	Axis Bank	6,54,119	1,357.78	1,357.78	22264	752.05	752.05	19,907	1,479.95	1,479.95	6,96,290	3,589.77	3,589.77
3.14	IndusInd Bank	10,90,031	2,878.24	2,878.24	114619	2,279.00	2,279.00	15,326	839.96	839.96	12,19,976	5,997.20	5,997.20
3.15	Yes Bank	5,10,205	1,332.45	1,332.45	4997	140.73	140.58	3,316	236.74	236.55	5,18,518	1,709.92	1,709.57
3.16	HDFC Bank	12,87,952	3,191.84	3,191.84	58878	1,928.94	1,928.94	23,596	1,500.63	1,500.63	13,70,426	6,621.41	6,621.41
3.17	DCB Bank	123	0.30	0.30	5100	181.43	181.43	2,309	153.08	153.08	7,532	334.82	334.82
3.18	Kotak Mahindra Bank	95,665	266.45	266.45	2134	81.52	81.52	3,238	244.60	244.60	1,01,037	592.57	592.57
3.19	Bandhan Bank	41,26,509	14,107.28	14,107.28	549741	3,550.08	3,550.08	0	0.00	0.00	46,76,250	17,657.36	17,657.36
3.2	IDFC Bank Limited	12,77,920	3,550.09	3,550.08	25517	220.09	219.55	441	35.79	22.66	13,03,878	3,805.97	3,792.29
	Total	94,02,971	27,686.91	27,658.61	927510	13,087.75	12,996.01	1,25,993	8,752.94	8,620.81	1,04,56,474	49,527.59	49,275.43

	Bank name	Shishu (Loans up to Rs 50,000)			Kishore (Loans from Rs 50,001 to Rs 5.00 lakh)			Tarun (Loans from Rs 5.00 to Rs 10.00 lakh)			Total		
		No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)
4	**Foreign banks**												
4.1	Citibank	0	0.00	0.00	137	4.04	4.04	96	7.46	7.46	233	11.51	11.51
4.2	Standard Chartered Bank	0	0.00	0.00	0	0.00	0.00	62	6.02	6.02	62	6.02	6.02
	Total	0	0.00	0.00	137	4.04	4.04	158	13.48	13.48	295	17.52	17.52
5	**Regional rural banks**												
5.1	Andhra Pradesh Grameena Vikas Bank	18,487	74.02	74.02	2089	51.53	51.53	313	22.29	22.29	20,889	147.84	147.84
5.2	Andhra Pragathi Grameena Bank	56,512	303.31	303.31	34447	426.29	411.68	295	20.03	17.06	91,254	749.63	732.05
5.3	Chaitanya Godavari Grameena Bank	11,693	52.44	48.89	13573	200.00	88.57	409	32.04	24.70	25,675	284.47	162.16
5.4	Telangana Grameena Bank	8,310	33.93	33.93	3082	39.61	39.61	45	3.67	3.67	11,437	77.21	77.21
5.5	Saptagiri Grameena Bank	6,957	22.29	22.29	11197	336.75	336.75	698	50.91	50.91	18,852	409.96	409.96
5.6	Assam Gramin Vikash Bank	2,594	8.68	8.47	3022	63.78	55.18	225	18.21	17.75	5,841	90.67	81.40
5.7	Langpi Dehangi Rural Bank	377	1.47	1.47	121	3.02	3.02	14	1.01	1.01	512	5.50	5.50
5.8	Arunachal Pradesh Rural Bank	6	0.03	0.03	8	0.16	0.16	7	0.52	0.52	21	0.71	0.71
5.9	Uttar Bihar Gramin Bank	26,909	133.56	132.28	13065	285.70	283.90	19	1.37	1.36	39,993	420.63	417.54
5.1	Madhya Bihar Gramin Bank	12,883	53.43	53.43	31823	605.05	569.07	386	32.80	31.62	45,092	691.28	654.12
5.11	Bihar Gramin Bank	2,487	11.20	11.20	3289	79.06	79.06	70	5.48	5.48	5,846	95.73	95.73
5.12	Chhattisgarh Rajya Gramin Bank	18,217	62.04	30.06	15986	215.45	141.34	245	19.62	17.08	34,448	297.10	188.48
5.13	Dena Gujarat Gramin Bank	1,635	6.30	6.28	4684	87.36	77.33	99	7.07	6.66	6,418	100.73	90.27
5.14	Baroda Gujarat Gramin Bank	6,011	19.12	19.12	4109	62.32	62.09	102	6.02	4.41	10,222	87.45	85.62
5.15	Saurashtra Gramin Bank	504	1.87	1.86	1654	27.01	26.94	146	12.27	12.20	2,304	41.14	41.00
5.16	Sarva Haryana Gramin Bank	4,031	14.75	14.11	9217	144.83	133.45	355	30.23	26.18	13,603	189.81	173.74
5.17	Himachal Pradesh Gramin Bank	825	3.88	3.88	2462	61.26	61.26	251	22.00	22.00	3,538	87.14	87.14
5.18	Jharkhand Gramin Bank	3,042	14.14	13.97	5884	82.38	75.83	60	4.28	4.19	8,986	100.80	93.99
5.19	Vananchal Gramin Bank	1,285	6.05	6.05	147	3.73	3.73	31	1.93	1.93	1,463	11.71	11.71
5.2	J&K Grameen Bank	1,011	4.77	4.75	5445	117.22	112.78	236	19.38	17.83	6,692	141.38	135.36
5.21	Ellaquai Dehati Bank	483	2.35	2.35	1049	19.68	19.68	96	7.57	7.57	1,628	29.59	29.59

	Bank name	Shishu (Loans up to Rs 50,000)			Kishore (Loans from Rs 50,001 to Rs 5.00 lakh)			Tarun (Loans from Rs 5.00 to Rs 10.00 lakh)			Total		
		No. of accounts	Sanction amount (in Rs crore)	Disbursement amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disbursement amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disbursement amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disbursement amount (in Rs crore)
5.22	Kaveri Grameena Bank	11,366	47.34	47.04	11605	142.55	142.14	316	26.35	25.88	23,287	216.24	215.06
5.23	Karnataka Vikas Grameena Bank	18,453	77.72	77.72	38137	638.94	638.94	1,142	89.57	89.57	57,732	806.22	806.22
5.24	Pragathi Krishna Gramin Bank	1,84,975	587.48	587.48	100688	1,338.09	1,324.71	6,720	500.10	500.10	2,92,383	2,425.67	2,412.29
5.25	Kerala Gramin Bank	1,82,100	436.62	436.47	114414	1,601.45	1,598.89	2,798	232.42	228.63	2,99,312	2,270.49	2,263.99
5.26	Maharashtra Gramin Bank	2,939	12.84	12.84	11235	251.16	251.16	981	78.15	78.15	15,155	342.15	342.15
5.27	Vidharbha Konkan Gramin Bank	2,480	10.73	10.45	2436	39.45	37.93	54	4.12	3.27	4,970	54.29	51.66
5.28	Narmada Jhabua Gramin Bank	5,621	25.74	23.74	7813	150.91	134.72	686	49.41	46.68	14,120	226.05	205.14
5.29	Central Madhya Pradesh Gramin Bank	3,601	16.48	15.75	1701	24.87	24.16	156	11.84	11.03	5,458	53.19	50.95
5.3	Madhyanchal Gramin Bank	11,951	43.94	39.55	3818	68.99	61.89	105	8.67	7.78	15,874	121.60	109.22
5.31	Manipur Rural Bank	1,873	8.06	8.03	790	11.43	10.63	45	3.23	3.07	2,708	22.72	21.73
5.32	Meghalaya Rural Bank	1,158	5.36	5.36	35	0.50	0.50	0	0.00	0.00	1,193	5.86	5.86
5.33	Mizoram Rural Bank	1,294	6.05	5.92	4231	73.02	72.65	18	1.62	1.62	5,543	80.68	80.19
5.34	Nagaland Rural Bank	254	0.60	0.60	53	2.11	2.11	6	0.45	0.45	313	3.16	3.16
5.35	Odisha Gramya Bank	21,891	95.43	95.42	9322	125.73	125.73	477	34.92	34.92	31,690	256.08	256.07
5.36	Utkal Grameen Bank	1,777	7.07	3.00	1385	35.62	8.22	197	16.04	2.81	3,359	58.73	14.03
5.37	Punjab Gramin Bank	8,325	35.22	33.46	9547	150.21	139.32	183	14.62	11.49	18,055	200.05	184.27
5.38	Malwa Gramin Bank	754	3.29	3.29	475	7.35	7.35	18	1.46	1.46	1,247	12.11	12.11
5.39	Sutlej Gramin Bank	196	0.84	0.84	100	1.30	1.30	2	0.16	0.16	298	2.30	2.30
5.4	Puduvai Bharathiar Grama Bank	593	2.87	2.87	802	8.52	8.52	1	0.07	0.07	1,396	11.46	11.46
5.41	Baroda Rajasthan Kshetriya Gramin Bank	6,025	27.01	26.87	16451	257.56	239.44	96	6.33	6.33	22,572	290.90	272.64
5.42	Rajasthan Marudhara Gramin Bank	11,334	49.37	42.50	2618	57.65	42.73	48	3.87	1.49	14,000	110.88	86.72
5.43	Pandyan Grama Bank	22,718	75.56	75.56	21351	223.46	223.46	55	4.06	4.06	44,124	303.08	303.08
5.44	Pallavan Grama Bank	2,317	8.80	8.80	12908	207.00	207.00	3,421	245.03	245.03	18,646	460.83	460.83
5.45	Tripura Gramin Bank	19,789	69.37	68.63	5025	89.04	83.51	189	14.65	12.75	25,003	173.06	164.89
5.46	Allahabad UP Gramin Bank	3,836	16.37	13.53	2049	38.14	31.43	228	18.28	13.73	6,113	72.79	58.69

	Bank name	Shishu (Loans up to Rs 50,000)			Kishore (Loans from Rs 50,001 to Rs 5.00 lakh)			Tarun (Loans from Rs 5.00 to Rs 10.00 lakh)			Total		
		No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)
5.47	Baroda UP Gramin Bank	15,536	65.77	60.98	7054	127.02	110.94	864	62.04	54.63	23,454	254.83	226.55
5.48	Gramin Bank of Aryavrat	21,209	90.08	88.81	24628	374.51	308.57	496	37.51	34.76	46,333	502.10	432.14
5.49	Kashi Gomti Samyut Gramin Bank	13,129	60.33	60.33	4114	78.32	78.32	688	56.07	56.07	17,931	194.72	194.72
5.5	Prathama Bank	7,769	31.17	31.17	12229	221.27	221.27	1,671	144.85	144.85	21,669	397.29	397.29
5.51	Purvanchal Bank	10,964	33.97	33.97	1080	48.07	48.07	5	0.30	0.30	12,049	82.34	82.34
5.52	Sarva UP Gramin Bank	14,256	39.24	39.14	10036	156.99	136.42	169	12.01	10.25	24,461	208.25	185.81
5.53	Uttarakhand Gramin Bank	1,777	7.12	7.11	3711	72.94	72.63	381	29.14	29.12	5,869	109.21	108.86
5.54	Bangiya Gramin Vikash Bank	5,887	17.31	16.17	10587	197.29	183.01	235	18.30	16.19	16,709	232.90	215.37
5.55	Paschim Banga Gramin Bank	4,960	15.59	15.59	24217	483.84	483.84	1,109	103.59	103.59	30,286	603.01	603.01
5.56	Uttarbanga Kshetriya Gramin Bank	868	3.02	1.92	9281	223.18	125.82	34	2.55	2.27	10,183	228.76	130.01
	Total	8,08,234	2,863.39	2,792.66	652279	10,440.66	9,820.31	27,696	2,150.47	2,078.96	14,88,209	15,454.51	14,691.93
6	**Regional rural banks**												
6.1	Non NBFC-Microfinance institutions	18,00,974	1,815.62	1,815.62	7846	140.72	140.72	0	0.00	0.00	18,08,820	1,956.34	1,956.34
	Total	18,00,974	1,815.62	1,815.62	7846	140.72	140.72	0	0.00	0.00	18,08,820	1,956.34	1,956.34
7	**NBFC-**												
7.1	Agora Microfinance India Ltd	11,251	28.35	28.35	0	0.00	0.00	0	0.00	0.00	11,251	28.35	28.35
7.2	Vedika Credit Capital Ltd	1,44,453	370.77	370.61	0	0.00	0.00	0	0.00	0.00	1,44,453	370.77	370.61
7.3	Pahal Financial Services Pvt. Ltd	99,577	248.45	248.45	1385	10.13	10.13	0	0.00	0.00	1,00,962	258.58	258.58
7.4	Annapurna Microfinance Pvt. Ltd	7,04,707	1,891.58	1,890.18	2173	20.66	20.66	12	1.52	1.52	7,06,892	1,913.76	1,912.35
7.5	Varam Capital Pvt. Ltd	6,946	16.73	16.73	0	0.00	0.00	0	0.00	0.00	6,946	16.73	16.73
7.6	Village Financial Services Pvt. Ltd	3,00,504	824.93	824.93	0	0.00	0.00	0	0.00	0.00	3,00,504	824.93	824.93
7.7	Muthoot Microfin Ltd	49,281	137.69	137.69	0	0.00	0.00	0	0.00	0.00	49,281	137.69	137.69
7.8	BSS Microfinance	1,34,796	352.70	352.70	0	0.00	0.00	0	0.00	0.00	1,34,796	352.70	352.70
7.9	ASA International India Microfinance Pvt. Ltd	3,67,050	877.35	877.35	0	0.00	0.00	0	0.00	0.00	3,67,050	877.35	877.35
7.1	Samasta Microfinance Ltd	3,42,697	856.73	856.73	0	0.00	0.00	0	0.00	0.00	3,42,697	856.73	856.73

Bank name	Shishu (Loans up to Rs 50,000)			Kishore (Loans from Rs 50,001 to Rs 5.00 lakh)			Tarun (Loans from Rs 5.00 to Rs 10.00 lakh)			Total		
	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)
7.11 Jagaran Microfin Pvt. Ltd	2,11,871	427.79	427.79	0	0.00	0.00	0	0.00	0.00	2,11,871	427.79	427.79
7.12 Spandana Sphoorty Financial Ltd	14,91,977	3,414.91	3,414.91	2165	16.00	16.00	2	0.14	0.14	14,94,144	3,431.05	3,431.05
7.13 Sarvodaya Nano Finance Ltd	72,273	135.52	135.52	0	0.00	0.00	0	0.00	0.00	72,273	135.52	135.52
7.14 Nightingale Finvest Pvt. Ltd	32,504	74.80	74.80	0	0.00	0.00	0	0.00	0.00	32,504	74.80	74.80
7.15 Grameen Koota Financial Services Pvt. Ltd	15,37,857	4,136.88	4,136.88	5856	52.05	52.05	0	0.00	0.00	15,43,713	4,188.93	4,188.93
7.16 M Power Microfinance Pvt. Ltd	62,808	177.44	177.44	0	0.00	0.00	0	0.00	0.00	62,808	177.44	177.44
7.17 Madura Micro Finance Ltd	3,70,566	937.30	937.30	0	0.00	0.00	0	0.00	0.00	3,70,566	937.30	937.30
7.18 Chaitanya India Fin Credit Pvt. Ltd	2,16,376	491.44	491.44	0	0.00	0.00	0	0.00	0.00	2,16,376	491.44	491.44
7.19 MSM Microfinance Ltd	22,824	92.01	92.01	0	0.00	0.00	0	0.00	0.00	22,824	92.01	92.01
7.2 Share Microfin Ltd	4,85,113	1,144.06	1,144.06	9663	50.79	50.79	0	0.00	0.00	4,94,776	1,194.85	1,194.85
7.21 Asmitha Microfin Ltd	25,539	57.92	57.92	196	1.01	1.01	0	0.00	0.00	25,735	58.93	58.93
7.22 Belstar Investment and Finance Pvt. Ltd	6,32,648	1,801.99	1,801.99	0	0.00	0.00	0	0.00	0.00	6,32,648	1,801.99	1,801.99
7.23 Namra Finance Ltd.	1,58,960	363.60	363.60	0	0.00	0.00	0	0.00	0.00	1,58,960	363.60	363.60
7.24 Svatantra Microfin Pvt. Ltd	2,18,480	567.25	567.25	0	0.00	0.00	0	0.00	0.00	2,18,480	567.25	567.25
7.25 Janalakshmi Financial Services Ltd	5,36,161	1,938.66	1,938.59	29439	269.29	269.22	429	33.97	33.87	5,66,029	2,241.92	2,241.68
7.26 Saija Finance Pvt. Ltd	1,59,088	335.56	335.56	0	0.00	0.00	0	0.00	0.00	1,59,088	335.56	335.56
7.27 Satin Creditcare Network Ltd	15,08,679	4,497.88	4,497.88	9745	48.73	48.73	0	0.00	0.00	15,18,424	4,546.60	4,546.60
7.28 Margdarshak Financial Services Ltd	98,648	159.03	159.03	1182	7.53	7.53	0	0.00	0.00	99,830	166.56	166.56
7.29 Navachetana Microfin Services Pvt. Ltd	72,973	159.38	159.38	0	0.00	0.00	0	0.00	0.00	72,973	159.38	159.38
7.3 Asirvad Microfinance Pvt. Ltd	13,35,343	2,428.20	2,428.20	0	0.00	0.00	0	0.00	0.00	13,35,343	2,428.20	2,428.20
7.31 Intrepid Finance & Leasing Pvt. Ltd	2,38,668	617.02	617.02	0	0.00	0.00	0	0.00	0.00	2,38,668	617.02	617.02
7.32 Fusion Microfinance Pvt. Ltd.	7,03,849	1,706.02	1,670.53	0	0.00	0.00	0	0.00	0.00	7,03,849	1,706.02	1,670.53
7.33 Hindusthan Microfinance Pvt. Ltd	22,021	52.42	52.42	0	0.00	0.00	0	0.00	0.00	22,021	52.42	52.42
7.34 Arohan Financial Services Pvt. Ltd	10,45,013	2,518.84	2,518.84	228	1.84	1.84	0	0.00	0.00	10,45,241	2,520.68	2,520.68

	Bank name	Shishu (Loans up to Rs 50,000)			Kishore (Loans from Rs 50,001 to Rs 5.00 lakh)			Tarun (Loans from Rs 5.00 to Rs 10.00 lakh)			Total		
		No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)	No. of accounts	Sanction amount (in Rs crore)	Disburse-ment amount (in Rs crore)
7.35	SKS Microfinance Ltd	65,65,614	13,682.24	12,439.02	0	0.00	0.00	0	0.00	0.00	65,65,614	13,682.24	12,439.02
7.36	Light Microfinance Pvt. Ltd	30,902	102.00	102.00	1632	9.79	9.79	0	0.00	0.00	32,534	111.79	111.79
7.37	Shikhar Microfinance Pvt. Ltd	15,611	35.03	35.03	312	3.52	3.52	0	0.00	0.00	15,923	38.55	38.55
	Total	2,00,33,628	47,660.44	46,380.11	63976	491.34	491.26	443	35.63	35.53	2,00,98,047	48,187.41	46,906.90
8	**Non-banking financial companies**												
8.1	Reliance Capital Ltd	4,72,272	1,149.65	1,149.63	12052	170.18	170.05	1,406	98.05	97.99	4,85,730	1,417.88	1,417.67
8.2	Capital First Ltd	1,79,024	766.33	763.19	286688	2,776.35	2,776.33	3,639	249.13	249.13	4,69,351	3,791.81	3,788.65
8.3	Veritas Finance Pvt. Ltd	4,247	13.13	13.13	557	4.27	4.27	0	0.00	0.00	4,804	17.41	17.41
8.4	Mahindra and Mahindra Financial Services Ltd	0	0.00	0.00	1108	105.15	50.42	3,923	236.08	236.08	5,031	341.23	286.51
8.5	Magma Fincorp Ltd	0	0.00	0.00	37564	1,233.45	1,233.45	8,695	579.43	579.43	46,259	1,812.88	1,812.88
8.6	Bajaj Finance Ltd	2,571	3.42	3.42	9631	416.30	416.30	14,736	978.42	978.42	26,938	1,398.13	1,398.13
8.7	Edelweiss Financial Services	8	0.04	0.04	1300	56.39	56.39	2,317	193.50	193.50	3,625	249.93	249.93
8.8	Fullerton India Credit Company Ltd	11,88,002	3,297.25	3,297.25	183915	3,320.00	3,320.00	20,370	1,337.86	1,337.86	13,92,287	7,955.10	7,955.10
8.9	Shriram Transport Finance Co. Ltd	4,162	18.40	18.40	215604	6,079.16	6,079.16	60,376	3,936.21	3,936.21	2,80,142	10,033.78	10,033.78
	Total	18,50,286	5,248.23	5,245.06	748419	14,161.25	14,106.37	1,15,462	7,608.68	7,608.62	27,14,167	27,018.15	26,960.05
9	**Small finance banks**												
9.1	Suryoday Micro Finance Ltd	3,87,203	1,089.05	1,089.05	9591	144.65	144.60	247	19.25	18.31	3,97,041	1,252.94	1,251.95
9.2	Utkarsh Small Finance Bank	12,77,396	3,206.32	3,205.65	6589	79.32	78.59	332	30.32	28.87	12,84,317	3,315.96	3,313.12
9.3	Fincare Small Finance Bank	6,71,832	1,798.96	1,796.02	581	25.21	24.98	922	227.30	226.29	6,73,335	2,051.47	2,047.30
9.4	Ujjivan Small Finance Bank	13,87,698	4,015.68	4,015.68	27701	276.44	276.44	0	0.00	0.00	14,15,399	4,292.12	4,292.12
9.5	Equitas Small Finance Bank	5,54,183	1,566.11	1,566.11	0	0.00	0.00	0	0.00	0.00	5,54,183	1,566.11	1,566.11
9.6	North East Small Finance Bank Ltd	5,22,815	1,127.27	1,127.27	0	0.00	0.00	0	0.00	0.00	5,22,815	1,127.27	1,127.27
9.7	AU Small Finance Bank Ltd	95	0.47	0.47	86802	2,514.89	2,513.89	30,924	2,099.05	2,083.90	1,17,821	4,614.40	4,598.26
9.8	ESAF Small Finance Bank	14,63,040	710.56	710.56	691	7.22	7.22	0	0.00	0.00	14,63,731	717.77	717.77
9.9	Capital Small Finance Bank	48	0.20	0.20	1903	58.27	58.27	314	26.36	26.36	2,265	84.83	84.83
	Total	62,64,310	13,514.62	13,511.02	133858	3,105.99	3,103.98	32,739	2,402.27	2,383.74	64,30,907	19,022.88	18,998.73
	Grand Total	4,26,69,795	1,06,001.60	1,04,228.05	4653874	86,732.16	83,197.09	8,06,924	60,943.34	59,012.25	4,81,30,593	2,53,677.10	2,46,437.40

Source: Data Provided by MUDRA to Author

ANNEXURE 4.4: Sectoral Deployment of Non-food Gross Bank Credit

	Sector	Outstanding as on (in Rs billion)							
		2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17
	Non-food Credit (1 to 4)	**30,396.15**	**36,673.54**	**42,897.45**	**48,695.63**	**55,296.01**	**60,029.52**	**65,469.03**	**70,946.89**
1	**Agriculture & allied activities**	**4,157.41**	**4,806.34**	**5,466.26**	**5,899.14**	**6,659.79**	**7,658.80**	**8,829.42**	**9,923.87**
2	**Industry (micro & small, medium & large)**	**13,114.51**	**16,045.76**	**19,373.25**	**22,301.79**	**25,164.83**	**26,576.27**	**27,306.77**	**26,800.25**
2.1	Micro & small	2,064.01	2,102.06	2,366.57	2,843.48	3,481.94	3,800.28	3,714.67	3,697.32
2.2	Medium	1,326.36	1,164.87	1,247.89	1,247.04	1,240.69	1,245.36	1,148.21	1,048.13
2.3	Large	9,724.15	12,778.82	15,758.80	18,211.27	20,442.20	21,530.63	22,443.89	22,054.80
3	**Services**	**7,267.90**	**8,942.01**	**10,229.60**	**11,518.86**	**13,374.51**	**14,130.97**	**15,410.67**	**18,022.43**
3.1	Transport operators	525.16	697.45	762.93	796.30	923.42	915.66	997.43	1,104.46
3.2	Computer software	125.43	138.58	142.97	169.10	185.89	172.14	190.96	178.84
3.3	Tourism, hotels & restaurants	194.10	276.38	323.19	354.41	398.75	370.36	370.53	375.03
3.4	Shipping	92.00	79.16	79.44	82.20	102.43	101.17	104.30	83.75
3.5	Professional services	434.01	451.88	479.61	564.21	796.49	844.17	1,046.00	1,376.50
3.6	Trade	1,644.97	1,850.41	2,249.77	2,759.53	3,257.77	3,656.82	3,810.98	4,278.95
3.6.1	Wholesale trade (other than food procurement)	863.57	946.89	1,203.65	1,500.99	1,675.70	1,800.77	1,686.08	1,932.08
3.6.2	Retail trade	781.40	903.52	1,046.12	1,258.54	1,582.07	1,856.04	2,124.90	2,346.87
3.7	Commercial real estate	921.28	973.41	1,126.52	1,260.70	1,532.40	1,664.61	1,776.13	1,855.64
3.8	Non-banking financial companies (NBFCs)	1,134.41	1,902.81	2,332.21	2,602.57	2,937.73	3,117.44	3,527.42	3,910.32
3.9	Other services	2,196.54	2,571.94	2,732.96	2,929.83	3,239.63	3,288.58	3,586.93	4,858.95
4	**Personal loans**	**5,856.33**	**6,879.44**	**7,828.35**	**8,975.84**	**10,096.89**	**11,663.48**	**13,922.16**	**16,200.34**
4.1	Consumer durables	82.94	62.87	71.31	83.81	128.28	153.05	177.53	207.91
4.2	Housing (including priority sector housing)	3,009.29	3,499.25	3,970.53	4,566.65	5,386.10	6,285.35	7,467.80	8,600.86

	Sector	Outstanding as on (in Rs billion)							
		2009-10	**2010-11**	**2011-12**	**2012-13**	**2013-14**	**2014-15**	**2015-16**	**2016-17**
4.3	Advances against fixed deposits (including FCNR{B}, NRNR deposits etc.)	486.54	493.11	569.72	610.87	635.96	625.16	666.83	661.15
4.4	Advances to individuals against share, bonds, etc.	28.63	28.80	30.00	31.09	38.21	54.34	64.19	47.50
4.5	Credit card outstanding	201.45	180.98	204.35	249.12	248.57	304.62	376.79	521.32
4.6	Education	368.63	427.04	499.33	549.70	600.05	633.20	682.24	700.88
4.7	Vehicle loans	637.91	726.01	890.54	1,110.89	1,063.00	1,246.10	1,529.08	1,705.25
4.8	Other personal loans	1,040.95	1,461.38	1,592.58	1,773.72	1,996.71	2,361.65	2,957.71	3,755.47
5	**Priority sector**	**10,921.79**	**12,624.45**	**14,210.45**	**15,397.96**	**18,297.24**	**20,103.24**	**22,259.07**	**24,356.53**
5.1	Agriculture & allied activities	4,157.41	4,806.34	5,466.26	5,899.14	6,659.79	7,658.80	8,825.90	9,909.22
5.2	Micro & small enterprises	3,735.30	4,428.48	4,986.25	5,622.96	7,078.13	8,003.43	8,475.87	9,019.75
5.2(a)	Manufacturing	2,064.01	2,102.06	2,366.57	2,843.48	3,481.94	3,800.28	3,714.67	3,697.32
5.2(b)	Services	1,671.30	2,326.42	2,619.69	2,779.47	3,596.18	4,203.14	4,761.20	5,322.43
5.3	Housing	2,178.77	2,391.05	2,658.51	2,672.03	3,020.07	3,223.86	3,422.76	3,683.44
5.4	Micro-credit	217.99	192.31	160.24	165.07	172.13	177.01	188.46	188.94
5.5	Education loans	362.47	425.89	480.67	526.12	578.88	591.84	601.37	604.36
5.6	State-sponsored organisations for SC/ST	12.34	0.87	1.79	1.24	3.28	3.48	5.14	6.38
5.7	Weaker sections	1,891.64	1,906.13	2,333.59	2,733.98	3,860.00	4,048.84	4,773.97	5,545.99
5.8	Export credit	302.00	318.21	391.00	422.34	483.13	426.26	423.82	425.02

Source: Reserve Bank of India

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28. There are several players in each segment described above; the mention of a few names is purely for illustration of the model and in no way signifies their pre-eminent position in the segment.
29. PwC 2016 Global Fintech Survey Report. https://www.pwc.com/gx/en/industries/financial-services/assets/pwc-global-fintech-report-2017.pdf. Accessed on 26 October 2018.
30. https://economictimes.indiatimes.com/small-biz/startups/newsbuzz/fintechs-in-india-cater-mostly-to-the-affluent-huge-potential-in-lower-middle-class-j-p-morgan/articleshow/64998037.cms. Accessed on 25 July 2018.

Microfinance Institutions: Recovery and Growth

5

The microfinance space now comprises of multiple players. Banks lend directly through the group methodology as well as through the BC route; SFBs that have graduated from microfinance are an important part; NBFCs also lend in this space; and NBFC-MFIs and NGO-MFIs continue to grow. Counting all the players, the total sector size is Rs 1,30,055 crore (excluding SHG lending by banks), with NBFC-MFIs accounting for 37 per cent and banks accounting for 32 per cent. The share of NGO-MFIs is less than 1 per cent, though they have a large off-balance-sheet portfolio as a BC, which is counted as banks' portfolio. This chapter is focused on NBFC-MFIs as other than banks and SFBs. They are the major player in the segment, contributing significantly to the portfolio of banks and NBFCs through the off-balance-sheet segment (BC lending, assigned portfolio and securitisation), and can also be said to be setting the contours of group-based microfinance lending. However, while looking at concentration, the data of all JLG lenders is also analysed to give a complete picture.

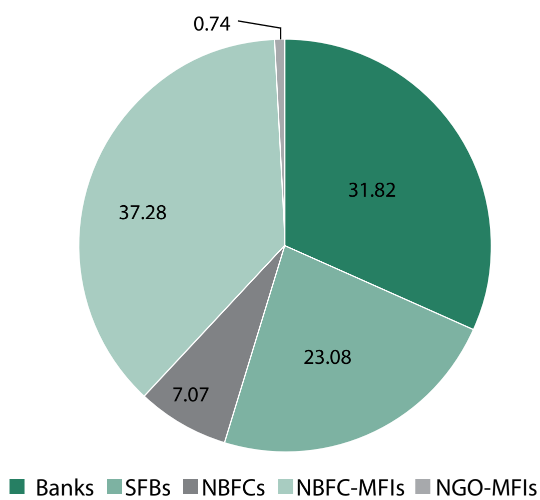


Figure 5.1: Share of Microfinance Lending as of March 2018

Note: Adjustments made to MicroLend III data by author.
Source: MFIN Micrometer, 25. http://mfinindia.org/resource-center/mfin-publications/. Accessed on 26 October 2018.
MicroLend III: March 2018. Data provided by CRIF High Mark.

AN EVENTFUL LAST YEAR: GROWTH RETURNS BUT PROFITABILITY DIPS

The MFI sector ended the financial year 2017–18 on a positive note, as growth returned. This was a cause for cheer, as in the wake of demonetisation disbursements had reduced to a trickle in the affected areas. However, while the top line saw a growth of 50 per cent, the adverse financial impact due to demonetisation is markedly seen in the bottom line on account of the provisions for bad loans. According to the estimates of the ICRA, the net interest margin for the sector dipped to 5.9 per cent in 2017–18 from 9.4 per cent during the previous year, mainly on account of interest reversals on delinquent loan accounts. The comforting fact is that the sector has bounced back from a position when Portfolio at Risk >30 days touched 15 per cent. While considering the sector history, it still remains high at 4.4 per cent—the legacy impact of the previous year—the fact that the recovery rate for fresh loans has come back to old benchmarks is a heartening sign.

Along with growth and improvement in portfolio quality, the sector also saw developments that could change its composition. Bharat Financial Inclusion Ltd (BFIL), which accounts for 16 per cent share of NBFC-MFI's portfolio as of 31 March 2018, announced its merger with IndusInd Bank in October 2017. This came after months of news reports on the issue, suggesting that various banks were in talks with the BFIL for a possible merger. While there have been mergers of MFIs with banks in the past, for instance, Kotak Mahindra Bank's acquisition of the Bangalore-based MFI BSS last year, the size of the BFIL and its merger has raised critical questions on the future of MFIs. A detailed newspaper report suggested that the decision of merger with a bank was based on multiple factors. It says that the BFIL's application to be an SFB showed its initial intent to move up, but the demonetisation experience, wherein MFIs were at a disadvantage compared to banks and BCs, further accentuated the desire for a merger as part of a de-risking strategy. In the deal BFIL investors will get 639 shares of IndusInd Bank, while the entire loan book of the BFIL will be absorbed in the bank. IndusInd will transfer the employees and operations into a wholly owned subsidiary, in other words making it a captive BC. The pros and cons of the merger are discussed later in the chapter, with its possible impact on the future of MFIs.

To look at other developments, the latter half of 2018 saw the successful Initial Public Offer (IPO) of CreditAccess Grameen (the erstwhile Grameen Kota) and the filing of Draft Red Herring Prospectus (DHRP) with SEBI for IPO by two other players, Spandana and Muthoot. CreditAccess Grameen, at a price band of Rs 418–Rs 422 per share, raised Rs 1,131 crore in August 2018 by way of sale of around 10 per cent holding by the promoter group as well as a fresh issue of shares. The IPO was subscribed to 2.21 times, though the retail segment did not see full subscription. Some observers feel that the IPO rush has more to do with investors cashing out as risks increase, and the BFIL merger is also added as an example. While there can be some merit in the argument, it needs to be stressed that private equity investors do have time horizons for their investment, and an IPO seems to be the best route in terms of transparency and judging the market sentiment. The success of the CreditAccess IPO also reflects market belief in the business model of MFIs.

During the past year, the MFI sector also saw quite a few changes in operational and policy norms. After the AP crisis, the RBI, based on the Malegam Committee's recommendations, had stipulated norms on total indebtedness of borrowers at Rs 60,000 under joint liability group-based microfinance loans, which was subsequently revised to Rs 1 lakh in 2015. The Microfinance Institutions Network (MFIN) had then decided that considering the economic condition of borrowers, its member NBFC-MFIs would stick to the Rs 60,000 limit. Three years since, considering the general increase in price level, as also larger loans by other players like banks, MFIN raised the indebtedness cap to Rs 80,000 in April 2018. It is still below the limit prescribed by regulation and some state chapters like Odisha are contemplating continuing with the old norm of Rs 60,000. Considering the average loan size from NBFC-MFIs to be Rs 22,273 during 2017–2018, this seems more of an enabling measure, with the potential for higher loan sizes in the future.

Multiple lending has been a key concern in the sector. With the establishment of credit bureaus and high enrolments under Aadhaar, MFIN had decided to adopt Aadhaar for KYC and had mandated its members to achieve the Aadhaar saturation level of their states. Realising the potential of Aadhaar as a unique identifier, MFIs have moved to the new system and quite a few are going ahead with more robust measures like demographic authentication and Aadhaar based e-KYC. Linking with Aadhaar has also enabled MFIs to tap into the JAM trinity for cashless disbursements. However, the privacy debate and the subsequent hearing of the matter by the Supreme Court have created confusion in the sector. MFIs at present provide loan origination data along with the Aadhaar number to the CIC, but now only Global AUA can collect Aadhaar data and has to store it in the Aadhaar vault, while earlier it was applicable to all other agencies. UIDAI has suggested that other agencies (MFIs not being Global AUA come under 'other agencies') think of a system in which the Aadhaar number, if required, can be entered and transmitted digitally without the need of being stored. Alternatively, they could consider the option of generating a unique identifier distinct from Aadhaar. CICs having been categorised as Local AUA can also not store Aadhaar data, even in the Aadhaar vault, and the generation of a unique key would lead to problems in dedupe of the client at the CIC level.

Linked to the above is another policy change induced by the RBI. In August 2017, the RBI issued a circular to all credit bureaus, stipulating that the credit information report of a borrower should not be limited to microfinance loans but should include all outstanding loans, be it consumer loans or commercial loans. At present, credit bureaus offer two different reports—a limited report focusing on JLG loans and a comprehensive report, both priced differently. Due to cost consciousness, most MFIs use the limited version even though it does not provide a complete risk assessment of the borrowers. Post this directive, there has to be only one comprehensive report. Although the directive has still not been implemented, once it happens MFIs will have a double impact, that is, both the cost of client acquisition and rejection rates will go up. It has not been clarified whether the borrower indebtedness cap prescribed by regulation is to be seen with the comprehensive report or if it will continue to be restricted to microfinance loans. However, logically, assessing overall indebtedness seems to be appropriate and will reduce credit risk. It is a welcome decision by the RBI, especially when different players are lending to the typical microfinance borrower, and it is imperative to get a complete picture. However, the related question of regulatory arbitrage is also associated with it and needs to be tackled (discussed in detail later).

Summing up, the MFI sector, after its slow growth in the last fiscal, has picked up again in 2017–2018. More importantly, this has happened despite the moving away of major players, as SFBs have regained top share in microfinance lending. Portfolio quality and profitability were impacted during the year due to demonetisation in 2016, but fresh lending has regained old characteristics in terms of portfolio quality

Key Highlights of NBFC-MFI Performance during 2017–18

Box 5.1: Key Highlights 2017–18—NBFC-MFIs (47 MFIN members)

- Gross Loan Portfolio (GLP) touched Rs 48,094 crore (GLP includes both on balance sheet and off balance sheet exposure
- 50% growth in GLP over 2016-17
- GLP includes portfolio created as BC (3,203 crore), Assigned Portfolio (Rs3081 crore) and Securitised Portfolio (Rs3,125 crore)
- There was a marked decline in securitized portfolio from Rs5,538 crore as on March 17 and a threefold jump in BC portfolio from Rs1,078 crore in March 2017
- 66% of GLP comes from rural areas, while 34% is from urban areas. This is a reversal from the earlier trend. In March, 2016, 60% of GLP came from metropolitan/urban/semi urban areas. The exit of SFBs is the reason for higher rural share
- Purpose wise, 50% of GLP is accounted by agriculture and allied activities, 46% by non-agriculture and 4% by household finance
- During the year 2017-18, NBFC-MFIs disbursed credit to the tune of Rs59,629 crore, jump of 50%.
- Average loan disbursed per account was Rs22,273, while average loan outstanding per account was Rs19,031 crore. Average per account figures do not reflect the position adequately as accounts with higher loan sizes and lower loan sizes get equal weight. Field observations show that average size of microfinance loan has gone up to Rs40,000.
- During the year, NBFC-MFIs mobilized debt funding of Rs20,695 crore. Of which, 57% was from banks and rest from other sources including NBFCs.
- The capital adequacy remains high with NBFC-MFIs reporting a leverage of 3.9. 55% of equity is from foreign sources and 45% from domestic sources. However, a definition of domestic and foreign sources is not available
- NBFC-MFIs through their field operations provide financial services to 25.4 million low income clients as on 31 March, 2018.

Source: MFIN Micrometer, 17 and 25. http://mfinindia.org/resource-center/mfin-publications/. Accessed on 26 October 2018.

Notes: MFIN micrometer issue 25 does not include Quarter four data for three MFIs – CreditAccess Grameen, Satin and Share, which places the aggregate figures on a lower side. This is one of the reason why there is a mismatch in portfolio reported by MFIN and Crif High Mark. Crif High Mark in its publication MicroLend for March, 2018 reports total on balance sheet portfolio of NBFC-MFIs at Rs 48,482 crore. Even considering that Crif figures include the universe of NBFC-MFIs and is not limited to MFIN membership, the figures are higher as non-MFIN members have low market share.

DETAILED REVIEW OF NBFC-MFI OPERATIONS DURING 2017–18

This section aims to present a detailed analysis of the performance of NBFC-MFI operations in terms of outreach, regional spread, growth dimensions across entities, drivers of productivity and the depth versus breadth dimensions of growth. Growth per se is a good indicator but there are other critical dimensions which can make the growth unsustainable, notably portfolio concentration, multiple borrowings related indebtedness and field staff productivity. Growth of microfinance is essential to financial inclusion in India, as MFIs remain key players in the last-mile segment. But often growth is not accompanied by prudence, which is a cause for concern, as it has the potential to lead to black swan events, jeopardising gains. This section has to be read with section 4 of this chapter that deals with the analysis of credit bureau data for a holistic understanding of geographical coverage.

Outreach and Regional Spread

Coverage of districts: 82 per cent

Over the years, operations of NBFC-MFIs have spread far and wide despite the moving away of SFBs, which accounted for a major market share of the NBFC-MFI universe. These operations cover 549 districts in India, out of a total of 712 districts. If the 44 districts of Andhra Pradesh and Telangana are excluded from the analysis, 82 per cent of districts in India will remain covered by NBFC-MFIs. This is a significant outreach, which is reiterated by the fact that 379 districts have more than five lenders (Figure 5.2). If the entire micro-lending space is considered, including banks, SFBs and NBFCs, the outreach goes up to 588 districts. The fact that including the universe increases the outreach only marginally is a pointer to the NBFC-MFIs driving the outreach story. That SFBs' exit from the NBFC-MFI universe has not had much impact on district outreach (in 2016, MFI operations covered 569 districts that included SFBs) shows that operations of both SFBs and NBFC-MFIs overlap.

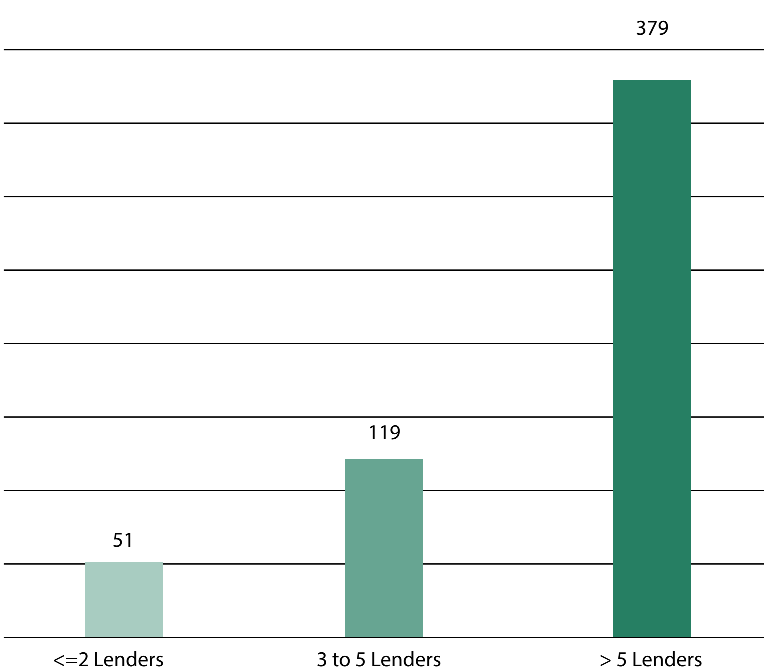


Figure 5.2: NBFC-MFI's District Presence

Source: Data provided by CRIF High Mark.

East and northeast have the maximum share in portfolio

The share of various regions has undergone a dramatic shift, which has been accentuated by two factors, namely major players in the south transforming into SFBs and a change in the classification of regions reported by the MFIN. Over the years, the sector started with a dominant share in the southern region in its portfolio, which later changed to equal shares in all four regions in March 2016 (Figure 5.3). This was labelled as balanced growth across regions, with concentration at the state and district levels. The March 2018 position shows that the addition of one more region—central, including Chhattisgarh and Madhya Pradesh that were earlier part of the western region—and the inclusion of Bihar in the east and northeast have changed the regional picture (Figure 5.4). It will be apt to say that regional classification done now is more in sync with the geographical reality of the country. The NBFC-MFI portfolio shows a dominant share in the east and northeast (NE) at 33 per cent followed by the south at 27 per cent. The high share of the east and NE in the portfolio seems to be a welcome feature, as these states have relatively higher levels of exclusion as well as low socio-economic parameters. When Bandhan transformed into a bank, it was argued that the share of the east would dip, but that seems to have not been the case. However, Bihar, Odisha and West Bengal account for 85 per cent of the share in the east and NE. Similarly, Uttar Pradesh accounts for 65 per cent of the share in the north, Karnataka accounts for 46 per cent in the south and Maharashtra accounts for 66 per cent in the western region. Details of state-wise and region-wise portfolio are given in Annexure 5.1.

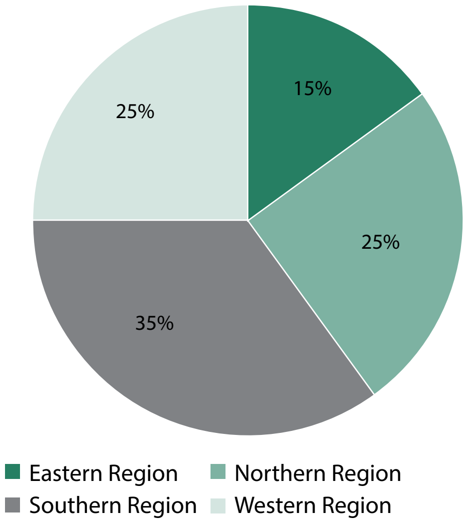


Figure 5.3: Region-wise Share in NBFC-MFI Loan Portfolio, March 2016

Source: MFIN Micrometer, 17. http://mfinindia.org/resource-center/mfin-publications/. Accessed on 26 October 2018.

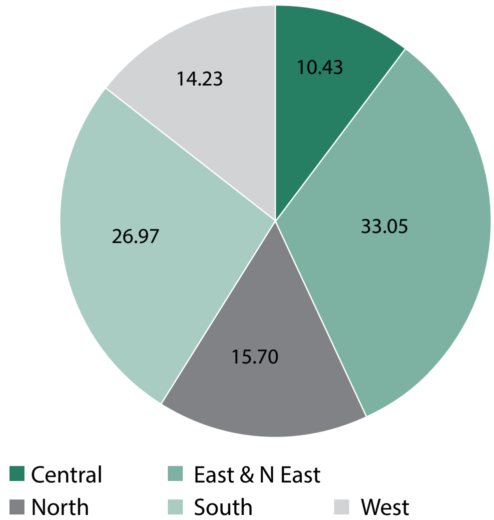


Figure 5.4: Region-wise Share in the NBFC-MFI Portfolio as on 31 March 2018

Note: Corrected by the author
Source: MFIN Micrometer 25, http://mfinindia.org/resource-center/mfin-publications/. Accessed on 26 October 2018.

States account for 62 per cent of the NBFC-MFI portfolio

The high state-wise concentration is reflected in the fact that six states account for 62 per cent of the portfolio (Table 5.1).

The share gets more skewed when seen at the district level (section 3 of this chapter). While it is heartening to see states like Bihar, Odisha and Uttar Pradesh in the top six, it also raises concern on the credit absorption potential of these states. Other micro-lenders also have operations in these states, and the situation is analysed in detail in section 3. The smaller share of traditional high concentration states like Karnataka and Tamil Nadu is on account of the fact that major players in Karnataka like Janalakshmi and Ujjivan are now SFBs. So is Equitas, a major player in Tamil Nadu. Despite these developments, both states together account for around 25 per cent share of the MFI portfolio.

Portfolio growth across states shows a mixed trend during 2017–18. Compared with the national growth of 50 per cent, nine states recorded more growth than the national average and seven states less than the national average (Figure 5.5). States with a portfolio more than Rs 500 crore have been considered for analysis.

Bihar and Odisha, which are part of the top six states in loan portfolio size, grew more than the national average, while the other four states recorded below national average growth. The reasons for this are that Uttar Pradesh, Karnataka, Tamil Nadu and Maharashtra have more to do with situational constraints than with institutional prudence. All four states were affected by high delinquency rates in the wake of demonetisation: UP, Karnataka and Maharashtra were among the worst affected. As against the all-India figure of 4.4 per cent for PAR >30 as of March 2018, the figure for Uttar Pradesh was 10.8 per cent, Maharashtra 10.4 per cent and Karnataka 3.7 per cent, while for Bihar and Odisha it was 0.8 and 0.6, respectively. But for the higher delinquency, these states would have also recorded higher growth.

Table 5.1: Share of the Top Six States in NBFC-MFI Portfolio as of March 2018

States	Portfolio (in Rs crore)	Percentage of All-India portfolio
Karnataka	6,068	12.64
Odisha	5,283	11
Uttar Pradesh	4,804	10
Bihar	4,677	9.74
Tamil Nadu	4,573	9.52
Maharashtra	4,516	9.40

Source: MFIN Micrometer, 25. http://mfinindia.org/resource-center/mfin-publications/. Accessed on 26 October 2018.

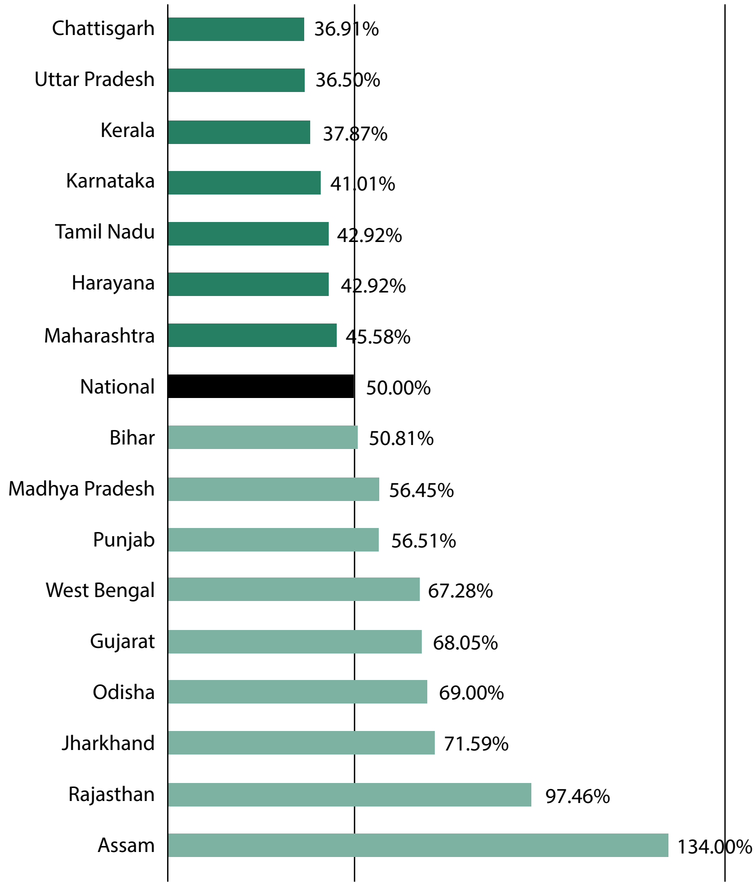


Figure 5.5: Annual Portfolio Growth Rate across States with >500 Crore Portfolio in 2017–18

Source: MFIN Micrometer, 25. http://mfinindia.org/resource-center/mfin-publications/. Accessed on 26 October 2018.

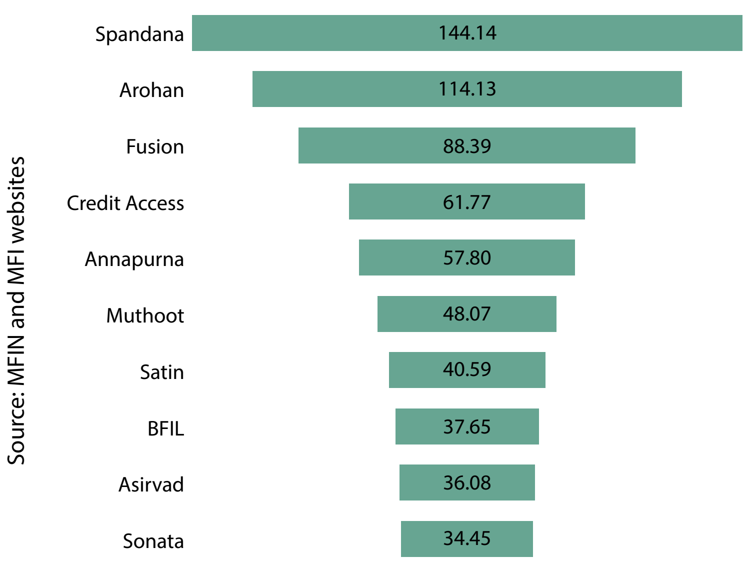


Figure 5.6: Growth Rate of the Top 10 NBFC-MFIs in 2017–18 (in per cent)

Source: MFIN Micrometer, Issue 25

What Is Happening on the Institutional Side?

Dominance by a few continues: The top 20 have 92 per cent market share; the bottom 27 have 8 per cent

An analysis of growth based on individual NBFC-MFIs also throws up critical insights. Predominance of a few MFIs continues to be the characteristic of the market. In 2015 Bandhan constituted 23.75 per cent of the total NBFC-MFI portfolio, while in 2016 Janalakshmi accounted for a 20 per cent share. The top 20 institutions had 89 per cent market share. After the exit of Bandhan and eight other SFBs, the situation has become further skewed. As of March 2018, the top 20 NBFC-MFIs had 92 per cent market share, and the top 10 had 77 per cent market share. Below the top 20 are 27 institutions that hold a mere 8 per cent of the market share. BFIL which will soon become a wholly owned BC subsidiary of IndusInd Bank has 25 per cent market share, and its exit will shrink the NBFC-MFI pie substantially.

The growth of the top 10 MFIs during 2017–18 shows great divergence. The range of annual growth varies from 144 per cent in the case of Spandana to 34 per cent in the case of Sonata (Figure 5.6). While the growth of the sector came down to 50 per cent from 91 per cent in 2016, statistics show that some institutions are still growing at a scorching pace. In 2016, Janalakshmi grew at 194 per cent, and the subsequent problems with its portfolio quality are well known. It seems that lessons of the past get watered down with time and the logic of 'huge untapped potential' starts dominating the growth discourse again.

Time and again it has been argued that high growth rates lead to infirmities in processes and control systems. Spandana, which grew by 144 per cent during 2017–18, has filed its DHRP for an intended IPO. Is the IPO with its consequent objective of building book size the reason for such growth? The high growth is not limited to the top 10, as in the 11 to 20 category by loan book size, six institutions clocked a growth rate in excess of 75 per cent.

Growth Dynamics

Combination of depth and breadth strategies

MFIs can either grow by expanding their branch network or by adding more clients to the existing branch. While the first approach typically leads to greater breadth in operations, the second approach leads to depth within the existing area of operation. During the year 2017–18, an analysis of the operations of the top 10 NBFC-MFIs shows that a mixed approach was the trend (Figure 5.7). Except in the case of Spandana, Muthoot and Asirvad, growth in the number of clients is either similar to growth in branches or slightly less. The overall data for 47 NBFC-MFIs also confirms this trend, as the sector average was 25 per cent annual growth in both the number of branches and clients. A logical corollary of this aspect is that the existing operational areas of MFIs are saturated, necessitating a move to new geographies. As the number of districts with NBFC-MFI presence did not see a corresponding increase during the year, it can be inferred that most of the new branches are within existing districts. It is a positive development because in previous years the focus was more on depth, that is, adding more branches. A word of caution needs to be added here. The granular data for two large MFIs, CreditAccess and Satin, is not available for March 2018 and the data of the previous quarter is used. Any large changes in their strategy can tilt the picture.

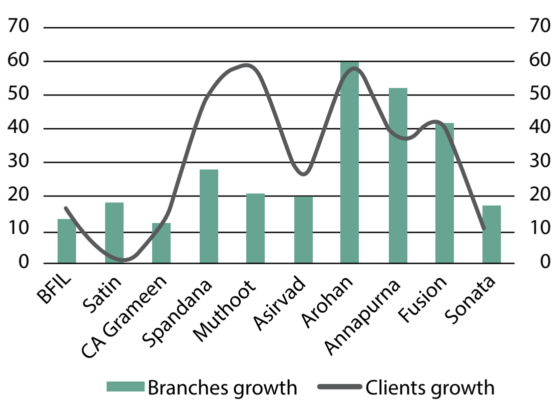


Figure 5.7: Annual Growth (%) in Branches and Clients of the Top 10 NBFC-MFIs

Source: MFIN Micrometer, 21 and 25. http://mfinindia.org/resource-center/mfin-publications/. Accessed on 26 October 2018.

Along with growing the branch network for additional clients, the growth strategy also included increase in loan sizes, as seen through average loan outstanding per client.1 Except Muthoot and Asirvad, the other eight MFIs recorded a decent growth in average loan outstanding per client.

Spandana stands out with an increase of 63.2 per cent, but that has to be seen with its low average loan outstanding in the previous year. Despite the growth, the average loan outstanding per client is reasonable and comforting. Field-level visits by the author

Table 5.2: Average Loan Outstanding per Client and Growth Rate

	Average loan outstanding per client	Growth
BFIL	20,351.6	18.41
Satin	18,501.1	17.56
CreditAccess Grameen Limited	24,510.9	15.59
Spandana	19,968.6	63.20
Muthoot Microfin	24,139.1	–6.31
Asirvad	16,227.6	8.12
Arohan	19,079.6	35.60
Annapurna	15,838.8	15.05
Fusion	15,233.4	35.10
Sonata	19,645.9	33.11

Source: MFIN Micrometer, 25. http://mfinindia.org/resource-center/mfin-publications/. Accessed on 26 October 2018.

gave the impression that loan sizes have increased significantly, with the average loan size of group loans having gone up to around Rs, 35,000–40,000. However, the data reported by MFIN does not reflect this, which may be due to two reasons. First, the higher loan sizes are for mature clients with two or more loan cycles, and second, the addition of new clients brings down the overall average outstanding per client, which includes both new and old clients. It would be better if data is reported cycle-wise, that is, average outstanding for clients in the first loan cycle, second loan cycle and so on. Such cycle-wise data will also inform the sector on client attrition rates, as institutions with high attrition will have lesser clients in higher cycle brackets.

Workload of loan officers: Signs of consolidation or necessitated by diversification?

Loan officers are the foot soldiers in microfinance, responsible for client acquisition, group formation, group training, loan appraisal, loan utilisation verification and collection of repayments. While the past crisis brought attention to clients, the concerns of loan officers have not been mainstreamed. At present, 65 per cent of the MFI workforce consists of loan officers. There have been persistent concerns about the workload of these officers, measured in terms of the number of clients handled and the volume of portfolio under a loan officer. In the last three to four years, the number of clients handled has gone up substantially, and it has been rationalised by referring to the increase in the

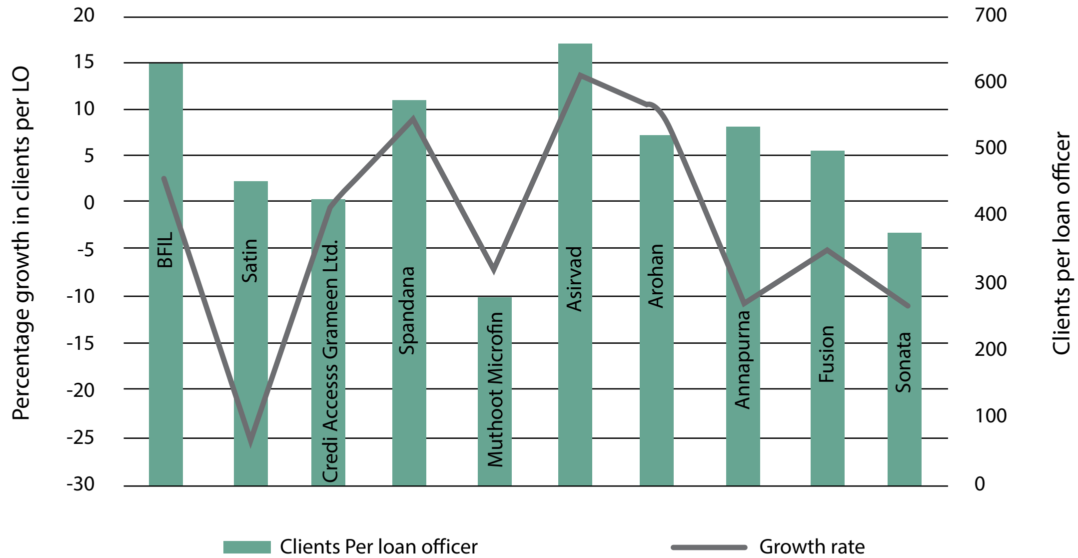


Figure 5.8: Top 10 MFIs: Clients per Loan Officer and Growth Rate

Source: MFIN Micrometer, 21 and 25. http://mfinindia.org/resource-center/mfin-publications/. Accessed on 26 October 2018.

repayment frequency—while earlier most loans were based on weekly repayments, the sector has increasingly adopted fortnightly and monthly repayment schedules. As of March 2018, there are signs of consolidation, as six of the top ten MFIs saw a decline in the number of clients handled by loan officers. Also, in other cases the increase ranged from 3 to 13 per cent, which is not a major increase. This is a good sign and it seems productivity ratios in the sector have reached their maximum. This has also to be seen with the repayment frequency—data from CRIF suggests that the movement towards longer repayment cycles has been halted. As of March 2018, 65 per cent of loans are on a weekly repayment model—the classic old style microfinance. The two big players, BFIL and CreditAccess, have continued to follow the weekly model, and a few others have also opted for shorter repayment cycles post-demonetisation. During demonetisation, a common experience was that longer repayment cycles lead to the weakening of client relationship, which further leads to credit quality issues in stress situations.

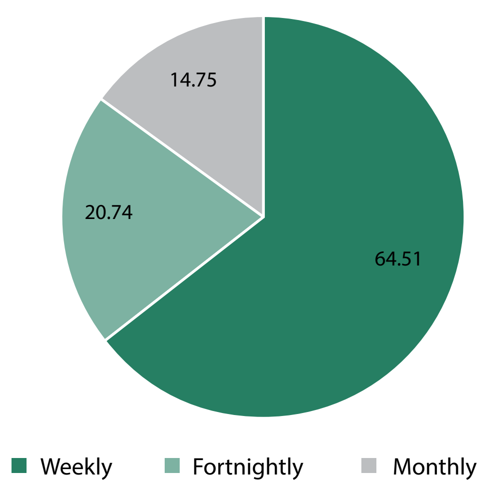


Figure 5.9: Repayment Frequency of MFI Loans

Source: Data provided by CRIF High Mark.

The other related issue is the increased adoption of the sale of third-party products by MFIs. Barring a few, most MFIs retail a variety of third-party products ranging from phones to cycles to solar lights. This selling is also done by loan officers as part of their operational duties and incentive structure. It also seems that the extra load of retailing third-party products has a role in checking a further rise in the productivity ratio of clients per loan officer. Even with similar or smaller number of clients, a loan officer is handling more products, which is reflected in the portfolio handled. There is no industry data on third-party products being sold by each MFI, though in the field it is quite a common practice, and there are reports of it turning away from being voluntary.

Portfolio quality: Improvement but effect of demonetisation lingers

During demonetisation, the inability of MFIs to accept demonetised notes led to clients not being able to pay their instalments. As it took time for new currency to get circulated, the default or non-paid loan amount kept rising adding to the burden. Incitement of group members by local leaders in several areas of Madhya Pradesh, Uttar Pradesh, Uttaranchal and Maharashtra not to pay their dues saying loans have been waived added to the problem. Clients already under stress latched on to the political narrative of loan waiver as an escape route. The author conducted a study for the MFIN in January 2017 in two of the worst-affected districts, Beena in Madhya Pradesh and Amravati in Maharashtra. Findings from the field indicated that it was a complex situation. Clients had multiple loans in both regions and their tenuous livelihoods implied that they are perpetually in need of credit. Demonetisation did cause some initial problems, such as stoppage of wage labour and lower prices for their produce like vegetables or milk, but it alone did not lead to this default situation. At best, it caused initial defaults/part payments, though the situation would have normalised in a month or so.

The major reason seems to be the involvement of local political leaders calling for non-repayment. Similar statements made by ministers in both states worsened the situation. On the whole, the default situation was produced by a complex set of factors: (i) multiple loans in a stressed livelihood scenario; (ii) initial cash/income shortage due to demonetisation; (iii) the inability of MFIs to accept withdrawn notes; and (iv) political interference at the local level.

The situation aggravated to such an extent that the PAR <30 days shot up to 11.04 per cent at an all-India level, and in some of the worst-affected districts in Uttar Pradesh and Maharashtra, it touched around 80 per cent. The situation has improved a lot (Figure 5.10) but compared to the past when PAR figures used to be below 1 per cent, it is still not so good.

State-level position of PAR shows the lingering impact more fully. In three states, PAR >30 days still remains far above the national average of 4.4 per cent. These are Uttar Pradesh (10.8 per cent), Maharashtra (10.4 per cent) and Haryana (10.5 per cent). In addition, Madhya Pradesh at 6.3 per cent and Punjab at 5.9 per cent are above the national average. The point of comfort is that PAR >180 days makes up for the bulk share, which indicates that fresh loans are now getting back to normal recovery levels. The PAR >180 days bracket comprises loans affected post-demonetisation and yet to be fully provided for in the financial statements. MFIs tried to get over the post-demonetisation situation by extending fresh credit to delinquent clients and that has reduced the PAR, but in some pockets it can lead to credit quality issues in the future: evergreening can mask the PAR but its impact comes with a time lag.

PAR 31–90 days at 4.44 per cent indicates persistence of default in fresh loans

CRIF High Mark has also reported PAR figures as of March 2018 across various micro-lenders in its publication *MicroLend*. It uses different PAR buckets like 1–30, 31–180, and 180 and above, which make only the last bucket of >180 days comparable with the MFIN's reported figures.

CRIF reports higher PAR >180 days for NBFC-MFIs as compared to the MFIN, and the data across agencies shows that SFBs have the worst portfolio

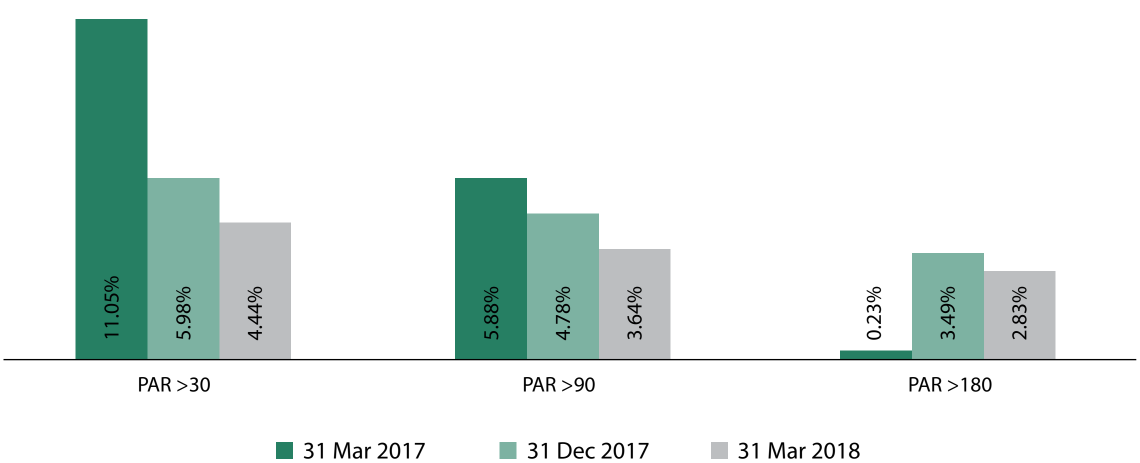


Figure 5.10: NBFC- MFI Portfolio at Risk (in per cent)

Source: MFIN Micrometer, 25. http://mfinindia.org/resource-center/mfin-publications/. Accessed on 26 October 2018.

Table 5.3: PAR >180 Days across Micro-lenders as of 31 March 2018

	PAR >180 days (in per cent)
NBFC-MFI	4.70
Banks	2.01
SFBs	15.49

Source: MicroLend III: March 2018. Data provided by CRIF High Mark.

quality. CRIF also pegs the size of PAR >180 days portfolio at Rs 8,400 crore, reflecting the persisting problem. Past experience shows that it is almost impossible to recover dues older than 180 days, which in turn implies that these loans will have to be written off. It is being estimated that much of the provisioning will be done in the 2017–18 financial year, bringing down profitability ratios.

Across lenders possible write-off of Rs 8,400 crore in 2017–18

Where are interest rates headed?

Interest rate charged on microfinance loans has always been contentious, and the sector has faced allegations in the past of charging high interest rates.

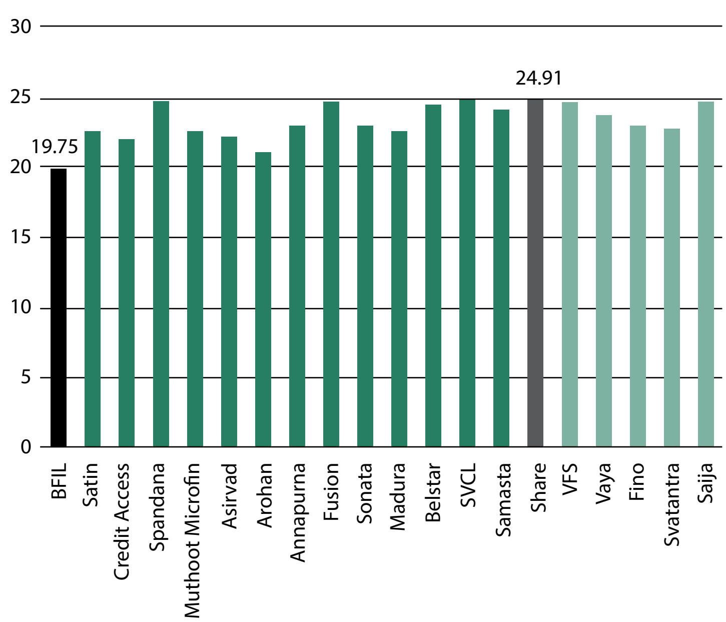


Figure 5.11: Average Interest Rate for Major Portfolio of the Top 20 NBFC-MFIs

Source: MFIN Micrometer, 25. http://mfinindia.org/resource-center/mfin-publications/. Accessed on 26 October 2018.

Though much of the criticism has been unfounded and based on ignoring the high cost of retailing micro loans, the latter being unsecured and consequently high risk, and the cost of borrowing by NBFC-MFIs as they cannot mobilise deposits. These allegations and the subsequent Andhra Pradesh crisis saw a policy response in the form of an interest rate cap linked to the cost of borrowings. At present, NBFC-MFIs' pricing depends on the following formula:

The pricing has to be the lower of the two options:

1. The cost of funds plus margin (margin to be 10 per cent for large MFIs—loans portfolios exceeding Rs 100 crore—and 12 per cent for the others).
2. The average base rate of the five largest commercial banks by assets multiplied by 2.75. The average of the base rates of the five largest commercial banks shall be advised by the RBI on the last working day of the previous quarter, which shall determine interest rates for the ensuing quarter.

Further, the RBI has also clearly specified the components of cost of funds to be: (i) expenses incurred towards interest payments; (ii) processing fee including service tax (amortised monthly); (iii) stamp duty charges (amortised monthly); (iv) demand draft charges (amortised monthly) reduced by; (v) interest accrued on security deposit. This has induced transparency in the process of interest rate calculation and the sector has seen a lowering of interest rates. Considering that interest charged by MFIs is primarily dependent on two factors: (i) size of the MFI (since larger MFIs are able to borrow at a cheaper rate compared to smaller ones); and (ii) operating expense ratio (OER)—MFIs with low OER are able to offer loans at cheaper rates, the current scenario in the case of the top 20 MFIs exhibits mixed trends (see Figure 5.11. MFIs are arranged according to size, with the BFIL being the largest.)

BFIL, as the largest MFI in terms of portfolio, also has a high productivity ratio of 633 clients per loan officer and it has been able to bring down the rates to below 20 per cent—the only MFI to do so. For all others, the evidence is mixed as no pattern emerges and the rates are range bound between 22 and 24.60 per cent. This indicates that despite the size advantage, many MFIs have not been able to bring down interest rates owing to either higher operating costs or retaining high profit margins. It must be stressed here that interest rate reduction beyond a point riding on cutting down operating expenses can be counterproductive. The two drivers

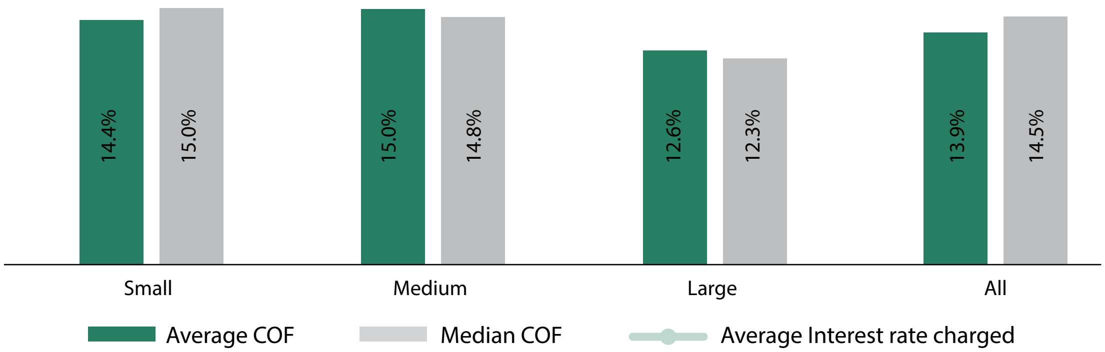


Figure 5.12: Average and Median Cost of Funds as of June 2018

Source: MFIN Micrometer, 26. http://mfinindia.org/resource-center/mfin-publications/. Accessed on 26 October 2018.

for reduced OER are increase in average loan size and loan officer productivity. Both these factors stretched outside the limit are at variance with the long-term sustainability perspective. Higher loan sizes beyond the repayment capacity of clients can lead to defaults, while increased workload for loan officers leads to attrition and lapses in the appraisal of clients. Over the years, the OER in the sector has come down to the range of 5–7.5 per cent, and there is little scope for further reduction.

In the above scenario, it is the cost of funds (COF) which plays a major part in determining interest rates. Evidence from the June 2018 issue of Micrometer brought out by the MFIN shows that the COF across entities differs widely (Figure 5.12).

Small MFIs have a portfolio less than Rs 100 crore, medium MFIs have a portfolio between Rs 100–500 crore and large MFIs have a portfolio that is more than Rs 500 crore. There is a 2.7 per cent difference between median COF of a small MFI and a large MFI, and 2.5 per cent difference between that of a medium MFI and a large MFI. This is mainly on account of small and medium MFIs having a larger share of borrowings from NBFCs at a higher rate, as against large MFIs that have better access to borrowings from banks at a lower rate.

Thus, despite a general decline in interest rates and the fact that small and medium MFIs avail borrowings at a higher cost, there is no clear industry-wise pattern in interest rates charged by MFIs.

SECTOR-LEVEL AND INSTITUTIONAL INITIATIVES

While the past year was mainly spent on addressing credit quality concerns and their impact on profitability, environmental changes also led to a few important initiatives like the push for cashless transactions, building ground for a common code for all micro-lenders agnostic of their legal form and the financial literacy of clients. At the institutional level also, some good initiatives were made to leverage technology and improve processes and products. It is no mean achievement that a sector which got its portfolio quality severely affected in 2017 also kept on initiating new things to build its value proposition, even as it returned to the growth path.

March towards Cashless: Does it Pass the Client Convenience Test?

Recognising the virtual ubiquity brought about by the PMJDY, MFIs realised that its clients now have bank accounts, a thing missing in the past. The usual practice in microfinance has been disbursement and collection of loan repayments in cash at group meetings or in the branch. This feature added to their comparative advantage, as clients excluded from the formal sector found doorstep delivery convenient and hassle free. Opening of bank accounts changed this scenario. It must be added that there has been another factor in the push to go cashless in microfinance. MFIs have been struggling with cases of theft and burglary while transporting cash in the field, which has often harmed human life as well. Transfer of loan amount directly into the bank account saves MFIs from cash transportation related issues and also saves on cost as loan officers can use the time more productively.

The data reported from 42 member MFIs out of 48 for June 2018 shows that 87 per cent of disbursements are now happening through bank accounts and a majority of MFIs are doing >90 per cent cashless disbursements (Figures 5.13 and 5.14). However, non-inclusion of a major MFI, CreditAccess Grameen, which continues to believe

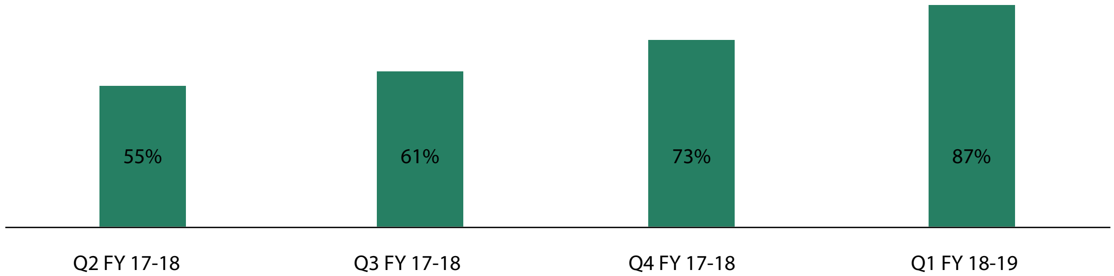


Figure 5.13: Cashless Disbursement by MFIs (in per cent)

Source: MFIN Micrometer, 26. http://mfinindia.org/resource-center/mfin-publications/. Accessed on 26 October 2018.

that cash disbursements are more convenient for clients, pegs the cashless disbursement percentage to a higher level.

Since this move towards cashless disbursements seems to be the in thing and is being justified from the perspective of Digital India, a line of caution needs to be added. As brought out in the chapter on digital finance, transferring money through digital channels is the easy part of the digital journey, whereas creating a setting wherein the client spends money digitally without resorting to cash is the true test of the digital ecosystem. At a time when most MFIs are disbursing loans through bank accounts, the absence of digital spending by clients necessitates withdrawal of cash from bank accounts. Most clients with PMJDY bank accounts are able to withdraw only Rs 10,000 per transaction at an ATM and have to visit the branch or BC for the withdrawal of the full amount. Going to the faraway branch is time-consuming and has an implicit as well as explicit cost to the client: they have to manage the lost production time as well as bear the transport cost. Withdrawals at BCs have their own constraints, as BCs often have cash float issues, which limit withdrawal amounts. In addition, field observation in Bihar by the author showed that BCs are not undertaking off-us transactions (transactions from a different bank's account) on instructions from banks to which they are attached. Due to errors in technology, BCs often do not get the credit in their account of off-us transactions, leading to the amount being paid to the customer without credit being matched to the BC. The problem of frequent dry ATMs in rural areas also compounds the situation. Other operational problems have also been reported by MFIs. MFIs that tried APBS (Aadhaar Payment Bridge System) for loan disbursement find it a good model, but under this, the NPCI populates the latest bank account in which the client has seeded their Aadhaar. In many cases clients are not aware of the last seeded bank account, so MFIs have to confirm the bank account for disbursement with them, which is a time-consuming process. In such a scenario, the microfinance community has to rethink its push for cashless disbursements, as it should not come at the cost of inconveniencing clients.

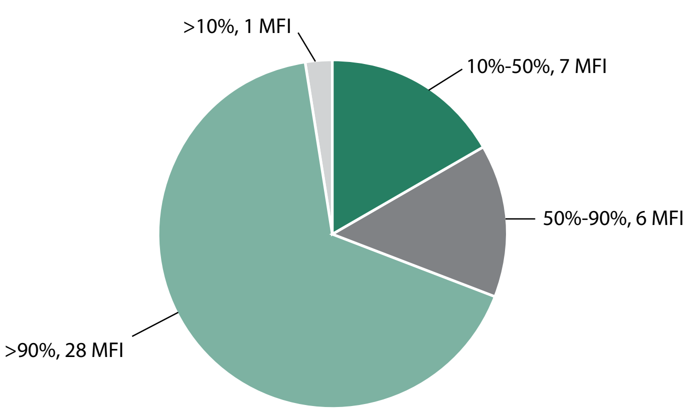


Figure 5.14: Cashless Disbursement across NBFC-MFIs (in per cent range)

Source: MFIN Micrometer, 26. http://mfinindia.org/resource-center/mfin-publications/. Accessed on 26 October 2018.

> Disbursement in bank accounts at present has an inconvenience cost to the microfinance client

Being easy, cashless disbursement has been widely adopted. However, if the digital ecosystem is developed to enable clients to make cashless repayments, that would be a more worthwhile service improvement. Making cash repayments of small amounts and having exact denomination notes create difficulties. Moreover, if cashless repayment would have been in place, demonetisation-related issues would not have surfaced. Realising this, the MFIN, with grant support from the HSBC, initiated a pilot project in 2018, which aims to find an appropriate model to provide a basic standard of digital engagement to facilitate cashless disbursement and collections. A technical agency (Spice Digital) has been commissioned to test models for digitising disbursements and collections from microfinance clients that:

- are cost-effective (for the customer as well as the MFI);
- can lead to a positive customer experience and hence demonstration for wider adoption and use; and
- are scalable and can effectively plug into MFIs' existing IT and MISs.

It is expected that the lessons from the pilot would pave the way for a nationwide rollout of the most appropriate model(s) and for the establishment of an affordable and common platform that all MFIs can use for digitising disbursements and collections. In order to make it a sector-wide initiative, all sizes of MFIs (small, medium and large) have been included in the pilot. Based on an interaction with the MFIN, it emerges that all possible models, like the UPI, AEPS, E-NACH and wallet-based solutions, will be tested in the pilot. In the author's experience, the project will have to surmount a few critical issues. For example, UPI-based transactions will require the availability of suitable mobile phones, digital literacy and the required bank balance. Similarly, availability of the required amount in the bank account will also be essential for AEPS or E-NACH. Field observations show that the biggest issue with clients for digital collection is their reluctance to go to the bank/BC and deposit cash in their bank account to facilitate digital transaction.

The pilot project has appropriately built in a baseline survey of clients to capture their profile, requirements and preferences. It will feed into designing the models as well as into assessing the efficacy and impact of the approaches at the end of the project. The evaluation of the pilot will be conducted by an independent third party.

Financial Literacy for Microfinance Clients: A Big Proposed Push

The RBI has been according prime priority to financial education, and microfinance clients are an ideal target market for it. While individual MFIs have their own initiatives, during the year both self-regulatory organisations, the MFIN and Sa-Dhan, came together to propose a nationwide financial literacy drive funded by Depositors Education and Awareness (DEA), held by the RBI. It is learnt that the RBI believes the countrywide presence of the MFIN and Sa-dhan through their member MFIs would be a great advantage in expanding the reach of workshops to various states. It is also noteworthy that the training is not limited to microfinance but will cover broad-based topics.

The focus of the workshops on financial literacy as envisaged by the DEA includes depositors' awareness on aspects like opening of bank accounts, KYC and AML, according to the guidelines of the RBI. The workshops will also promote good credit behaviour, and utilisation and timely repayment culture. They will make clients aware of the benefit of maintaining good credit history, the risk of taking multiple loans, and the need to assess cash flows while applying for loans. The delivery channel will be classroom-based workshops, with around 60 target participants. Each workshop will be 4–5 hours long and will cover standard topics on depositor education as mandated by the DEA. Further, the approach towards the workshops will be to impart generic concepts of saving, credit and other financial services of formal financial institutions. In terms of location, the workshops shall focus on unbanked and under-reached (selected) locations in all regions (north, south, central, east and northeast, and west) of India. The proposal aims at conducting 4,500 workshops by MFIN and Sa-Dhan members across 160 districts. It is significant that the districts' selection has been based on three crucial parameters—Crisil Inclusix score (50 per cent weight), literacy percentage (25 per cent weight) and aspirational district (25 per cent weight).

> Through 4500 workshops across 160 districts, the financial literacy workshops will cover ~3 lakh low income clients

The RBI will provide workshop training material and modules for the project. The overall objective of the project is to develop and disseminate financial literacy workshops around the topics mentioned under the DEA mandate in an engaging and cost-effective manner.

To evoke curiosity and engage participants for effective transmission of concepts and ideas, it has been proposed that the workshops will use methods to connect at a psychological level to ensure behavioural change. Since the participants will be adults and mostly uneducated women borrowers of member MFIs, emphasis will be laid on adult learning principles, where participants shall Learn-Act-Do (LAD model).

The science and art of helping adults learn, the practice of adult education referred to as andragogy distinguishes itself from the traditional children focused pedagogy. Andragogy is based on the fact that adults learn best when:

- they feel the need to learn;
- they have some input into what, why and how they learn; and
- the learning's content and processes have a meaningful relationship to the learner's experience.

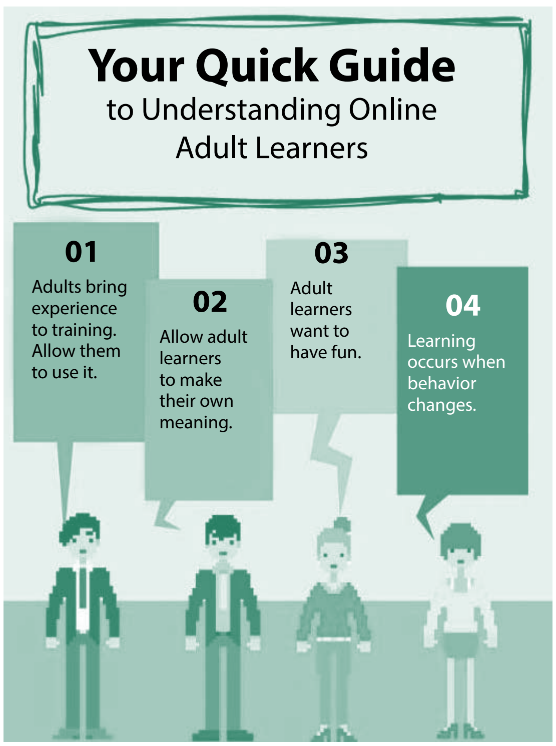


Figure 5.15: Basics of Adult learning

Note: A summary of MFIN's proposal on awareness workshops.

Since the focus of the proposed workshops is on adults in rural, semi-urban or urban locations that might be first generation entrants in the formal financial sector, the content and workshop design will have to keep in mind the basic elements of andragogy. Both the MFIN and Sa-Dhan have proposed imparting information in the workshops through role plays, stories, video, audio, posters, banners and comics to make the learning process engaging for clients. The project will be implemented in one year and will cover roughly 15 per cent of microfinance clients directly. Along with the intended objective of financial literacy, the field-level workshops will also have a positive externality in the form of better recognition and legitimacy of the work done by MFIs for last-mile financial inclusion.

Code of Conduct across Micro-Lenders: Aspiration Needs to Become Reality

Since 2011, when the RBI issued detailed regulatory guidelines for microfinance lending, MFIs were the main or only lender, and accordingly guidelines were made applicable to NBFC-MFIs. These guidelines related to critical business aspects like household income level of clients, indebtedness threshold, maximum number of loans and pricing. Over the years, major changes have taken place in the sector. The largest NBFC-MFI (Bandhan) became a bank in 2014, and between 2017 and 2018, eight of the bigger NBFC-MFIs have become SFBs. Despite the change in legal form, these banks continue to focus on microfinance as part of building on their core competence. Other mainstream banks have also started lending directly in microfinance as well as indirectly through the BC route—where the MFI creates the microfinance portfolio on behalf of banks. NBFCs like L&T and Fullerton are also active players in the microfinance space. On account of these developments, around 60 per cent of microfinance lending is accounted for by players other than NBFC-MFIs, yet these institutions are not subject to the micro-regulations faced by NBFC-MFIs. The role of players other than NBFC-MFIs is discussed in more detail in the following section on concentration risk in microfinance.

Realising the need to ensure a level playing field, the MFIN undertook extensive deliberations with other stakeholders during 2016 and 2017 and came out with a voluntary Mutually Accepted Code of Conduct (MACC) in 2017. MACC applies to the provision of microcredit to customers, individually or in groups either on its own or as an agent. The code has five elements:

1. Customer engagement
2. Employee behaviour and recruitment
3. KYC and reporting standards
4. Risk management unit
5. Enforcement and accountability

> MACC stipulates maximum three lenders per customer within the RBI prescribed indebtedness level

As lending by different lenders to similar segments has the potential to create indebtedness and consequent client distress, guidelines on indebtedness threshold have been included as part of the customer engagement pillar. The code specifies that lenders must conduct due diligence to assess the need and repayment capacity of the customer based on information from the applicant, credit bureau and/or field-level intelligence before disbursing a loan. It also limits the number of lenders to one borrower at three and specifies that no lender should become the fourth lender to a customer. In addition, the total indebtedness of the customer cannot exceed the RBI prescribed level of Rs 1 lakh.

Going further, in order to ensure inter-agency coordination, MACC provides for a joint risk management unit (RMU) to be set up within the MFIN, where all lenders who have signed up will provide all ground-level information regarding episodes, stress points and intelligence from a risk perspective on a real-time basis. The RMU, in turn, will share this information with all the members of MACC as an early warning instrument for necessary mitigating measures.

MACC is a very laudable voluntary initiative to avoid over-lending to low-income clients, which has, however, not seen much traction. Only a few banks and NBFCs have signed MACC, though major players in the ecosystem like Bandhan and SFBs have not. Even with limited signatories, the mechanism to ensure adherence to MACC has not taken shape and it has remained an aspirational document. However, the MFIN has recently formed a working group to broaden the coverage of MACC and bring other major players on board. As the intent behind MACC is customer protection, the RBI endorsing or nudging players into signing and adhering to MACC will probably go a long way towards promoting sustainable inclusion of low-income clients. It also fits in with the RBI's commitment to move towards activity-based regulation over legal form-based regulation.

Institutional Initiatives

Initiatives by various MFIs during the year have been primarily focused on cashless disbursements. Besides disbursements in bank accounts, most MFIs now have field staff equipped with Android tablets or mobile phones to take technology to the last mile, which work in both online and offline modes. With tablet-based field operations, KYC and credit bureau check is done at clients' doorstep and the latter can know their loan eligibility in real time. Considering these initiatives have now become common and have been covered earlier, they are not being detailed here.

MFIs are now introducing digital solutions for other operational features. The SVCL has developed a mobile phone-based application for monitoring and supervision, as well as for audit. The SVCL claims to be the first microfinance company that has launched a mobile application for audit. The app provides end-to-end solution and is loaded with all the necessary features like on-the-spot remark, location capturing and evidence capturing. It also has the flexibility for addition of questions. Vaya Finserv has a system wherein collections are recorded and reflected in the MIS, including dashboards, on a real-time basis. Customers with unpaid dues, absence from centre meetings or with delayed repayment history are flagged as early warning signals to the risk monitoring team. Renewal loans and subsequent products are offered to select clients with a good track record of attendance and repayments, determined through data analytics.

The focus here is on capturing new developments in processes, products and other client-centric initiatives.

Process improvements/innovations

The concept of joint liability and its enforceability has been engaging the minds of practitioners for some time. Field experiences show that the rise in loan amounts and the consequent increased burden on disciplined members of defaulting members' share are making people uneasy with group loans. As a solution to this, while some MFIs have started giving individual larger-sized loans, Satya Micro Capital has brought in the concept of limited liability. In this model, the share of responsibility of defaulted clients of a group on disciplined clients is limited to a certain time and amount. Under the LLG model, good customers have limited liability (up to 10 per cent of the loan amount through joint liability) in the event of default by a delinquent member. Satya takes ownership of this delinquency and relieves disciplined/regular customers from the obligation of making payment on behalf of delinquent customers. The institution believes that as delinquencies are controlled through its credit appraisal and its seven-layer approval process, it would enable the institution to take the responsibility of defaulting customers beyond a point.

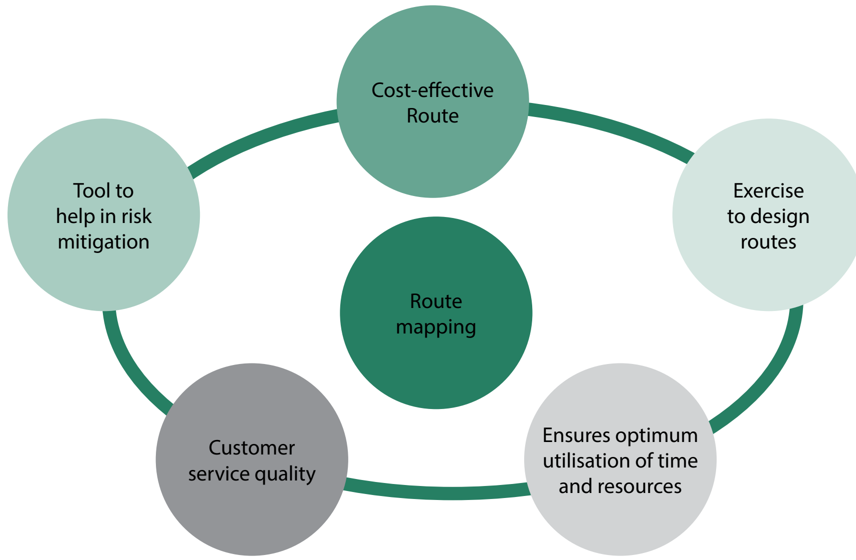


Figure 5.16: Route Mapping—An Overview

Source: Satin Creditcare, in a note to author.

> Satya Micro Capital has an all-women zone in eastern Uttar Pradesh and has also brought in the limited liability concept in group lending

Microfinance being a women-focused business, Satya Micro Capital has introduced an all-women zone in eastern Uttar Pradesh by opening six branches in Azamgarh, Varanasi, Balia, Gorakhpur, Sultanpur and Jaunpur during the financial year 2017–18. All-women zone implies that all employees are women, starting from entrepreneurship development officers (EDOs), branch heads and assistant/deputy credit managers (that is, the entire chain of the branch and zonal business team). The all-women staff act as a catalyst for the socio-economic upliftment of poor and vulnerable women's households. Satin Creditcare implemented quality management services in its operations during the year through: (i) implementation of the 5S project at its branch and regional offices and (ii) route mapping exercise for its field officers. 5S (comprising sort, systematise, spic-n-span, standardise and sustain) is a process for implementing and maintaining a clean, safe and organised work area. The objective of implementing 5S was to have streamlined processes, clean and safe working environment for staff and clients, with the belief that the visual workplace affects everyone. GPS route mapping for loan officers has been done earlier by other MFIs, with the BFIL as the pioneer again. The SCNL believes that with the help of the route-mapping exercise it can optimise the route and conduct load balancing, load consolidation and productivity enhancement.

At a time when the productivity of field staff is a key driver in maintaining profitability within the regulatory permissible margin, more and more institutions will adopt this to avoid wastage of time in route duplication.

Product initiatives: Old-time IGL dominates the landscape

Client centricity being the key of microfinance, it is expected that MFIs will continuously improve their product offerings based on client needs. MFIs in India have regulatory limitations on what products they can offer as well as guidelines relating to loan size and tenure for eligible products. MFIs cannot on their own accept deposits or provide insurance and pension services, though they can offer these services as a BC and through insurance companies. The credit side is hemmed in by regulations on loan size-linked tenure, maximum loan size, target clientele, income definitions, eligible activities as well as total indebtedness. In such a scenario, the fact that the typical income generating loan (IGL) continues to be the main offering has to be seen with the ecosystem, and it will not be entirely fair to critique MFIs for negligible product innovation. Still, even the freedom allowed by regulation to the extent of 15 per cent of total assets—wherein MFIs can lend without micro guidelines pertaining to microfinance lending—has not been optimally used. While most MFIs have loans for emergency, housing, sanitation and education, their share in the portfolio remains marginal. More importantly, these loans have similar features as the IGL, albeit with higher loan amounts and repayment periods. There is no comprehensive sector-wide data on the diversity of loan products and their relative share in the loan portfolio. Industry associations also do not publish data on product diversity. Based on the information submitted by MFIs for this report it can be seen that few new initiatives on this front were taken during the last twelve months.

In 2016, CreditAccess Grameen (CA Grameen) introduced retail finance loans on a pilot basis through its first branch in Bangalore. Retail finance is a new business line that fulfils higher loan requirements of graduated group-lending clients for their income-generation activities. The following products are offered through this initiative:

- Grameen Udyog Loan: This loan is referred to as a business loan, where loan amount up to Rs 1.25 lakh is offered to existing CA Grameen customers to meet their business expansion, working capital and purchase of plant and machinery requirements.
- Grameen Savaari Loan: This loan is offered to existing CA Grameen customers for loan amounts ranging from Rs 25,000 to Rs 60,000 for the purchase of new two-wheelers to support their income-generation activities.
- Grameen Vikas Loan: This loan is offered to CA Grameen customers who look at high-ticket loan amounts between Rs 1 and 5 lakh to meet their business-related requirements, which include purchase of inventory or machinery, business expansion, or closure of existing borrowings where property is taken as collateral.
- Grameen Suvidha Loan: These loans are offered as intermediate loans to the main loans, to fulfil the working capital requirements in the case of business loans, and insurance/maintenance-related activities in the case of two-wheeler loans. These can be up to 15 per cent of the main loan amount.

As of March 2018, the retail finance portfolio stands at around Rs 120 crore with a 16,000 customer base. At present, it forms a negligible share of 2.5 per cent in CA Grameen's overall loan portfolio, but it has huge growth potential.

Arohan's product diversification has taken on an entirely different scale with a new business line termed as Strategic Asset Alliance. Arohan's initial efforts in this direction during 2015–16 were to support industry peers in managing their liquidity situation. During 2015–16, Arohan undertook two direct assignment transactions with an industry peer to help the entity grow by easing its capital requirement. Another industry peer who was in need of servicing its huge pool of deserving borrowers in a fairly neglected region of a low-income state was supported by Arohan that entered into a sourcing and collection arrangement with the peer. Sourcing and collection are essentially replicating a BC function, building and maintaining loans for Arohan at a commission. Initially, Arohan envisaged sourcing and collection arrangements and portfolio purchase through direct assignments as the mechanism to support industry peers service their customers. But over time, it came up with the concept of a bridge loan, where initial funding support will be given to an MFI to build its assets. Once this asset becomes eligible for selling according to the RBI's extant policy on securitisation/assignment, Arohan will purchase the portfolio of the books of the MFI. This was designed to help peer MFIs grow beyond their capital adequacy limits. The initiative allowed Arohan to leverage the local expertise of partners to build its own book and also provide partners with a business model without stringent capital requirement. As of 31 March 2018, this Strategic Asset Alliance initiative of Arohan caters to about 70,000 target customers across Assam, West Bengal, Bihar, Jharkhand, Chhattisgarh, Odisha and Uttar Pradesh. With total assets under management of Rs 107 crore and partnerships with 11 industry peers and grassroots organisations, Arohan is the only NBFC-MFI to have a fully functional business vertical dedicated to working through collaboration. Some of these relationships, especially sourcing and collection, have moved beyond funding. Arohan's proposition in the industry is made unique by the process efficiency, reduced TAT of loan processing, technology-enabled sourcing, access to high quality data and MIS, support on training on processes, risk management, HR practices and other value-added services.

Training

Field staff being the key to effective client engagement, its training is integral to any MFI's functioning. The large, scattered scale of operations and the availability of quality trainers have been the challenge on this front. Vaya Finserv has tried to overcome this challenge by using technology. It has built Abhyas, an eLearning platform that enables access to training anytime, anywhere on any device, including a smartphone, tablet or laptop. The content of the training has been designed through relatable characters, with animation, to make the

Figure 5.17: Screenshot of Online Training through Abhyas of Vaya

Source: Vaya Finserv. Accessed on14 August, 2018

training relevant, contextual and at the same time a unique learning experience. These training modules provide insights into the microfinance industry in general and the roles and responsibilities of the trainee in particular.

Assessments during the training and afterwards provide an opportunity to the trainee to instantaneously assess their learning. Data of the employee is also provided to the training team to analyse and determine training needs specific to each individual, circle or state. Under this, Gurukul is a virtual classroom where training is delivered by subject experts from a central location and is received by about 30 employees across locations countrywide. Gurukul is now a platform for quick trainings designed based on feedback from finance or audit on operations. Gurukul trainings are scheduled on a monthly training calendar and conducted with multiple mixed groups across locations.

Fusion Microfinance did a digital literacy project during the year. The project leveraged videos and role plays to facilitate making women clients digitally literate by imparting knowledge on various modes of cashless transaction, accessing account details and by promoting digital payments. The duration of the workshops was kept between 3 to 4 hours. In parallel, financial literacy programmes and skill development workshops were conducted on topics such as money management, right borrowing, household budgeting and benefits of thrift. Digital literacy workshops were conducted across 199 districts in 14 states covering 48,031 villages in an effort to make one million rural households digitally literate. The need for massive efforts at both the government and institutional levels to further the cause of Digital India has been discussed in the chapter on digital finance.

Having reviewed the progress of MFIs during the year, growth drivers, sector and institutional initiatives, it is critical to examine the micro-lending space from a risk perspective based on data from the credit bureau. Client indebtedness in the wake of excessive credit and multiple lending has been the cause for numerous localised and a few pan-India black swan events in the sector.

INSIGHTS ON THE MICROFINANCE MARKET FROM CREDIT BUREAU DATA

While it is acknowledged that the events of client unrest and interference by state functionaries are often misdirected at MFIs, as they are the most vulnerable part of the financial sector, retailing unsecured loans but often the interplay of operational features of MFIs also add to the problem. Past events of Krishna, Kolar and Andhra Pradesh seem far away, especially as post-2010 the RBI has put in a detailed regulatory framework. However, sporadic events continue to occur and one such large-scale event was the defaults post-demonetisation, which were also partly attributed to high debt levels among microfinance clients. As long as clients were able to get credit from another institution to pay existing loans, the cycle worked, but decline in fresh credit short-circuited the process. However, the role of local political leaders in inciting unrest and default during demonetisation is well known, as described in the section above.

> MFIs continue to be affected by local events often beyond their control. There is a need to ensure that their operations do not add to the problem

During the year 2018, various localised events continued to dot the operating landscape of MFIs. Most of these events were related to illegal interference by state functionaries in MFI operations, incitement by local leaders and incidents of cash robbery during field operations. For example, it was reported that the police in Nadia district in West Bengal sealed the branch of an MFI despite the availability of legal papers with the latter. However, there were also cases related to the operations of MFIs. The problem of ringleaders was widespread pre-2010 as a means to grow a portfolio rapidly. In such cases the ringleader or the dominant person used to pipeline the loans of other members. Odisha reported two such cases during 2018 in Jharsaguda and Mayurbhanj districts, where the ringleader absconded with loans of group members. Group members later approached the district collector for remedy. The year also saw an incident in Tuljapur, Maharashtra, where a group of women marched in a protest rally against forced selling of solar lamps by MFIs—an issue flagged as a pain point in this report. MFIs need to be cautious, as despite their legitimate place in the financial sector, they continue to be the favourite whipping boys of the local media and leaders, and they cannot allow any room for these tirades against them to be justified. As an example of the external unjustified campaign against MFIs, during the year it was reported that a television soap in West Bengal portrayed MFIs as chit funds duping people. More recently in August 2018, Hoshangabad district in Madhya Pradesh witnessed encouragement to default. MFI borrowers in two villages in Hoshangabad district were approached by local leaders of a party promising low interest bearing loans through SHGs after the assembly elections instead of MFI loans. They even went so far as to promise a waiver of microfinance loans. In such a volatile situation, where any event or a series of events has the potential to snowball into a wider crisis, MFIs need to be cautious that they do not provide any ground for criticism. The sector has to also contemplate that these events are often reported in areas of high market saturation, which implies that the sector has also a role to play. However, in the changed scenario, when other players like banks and SFBs are major micro-lenders, the situation has to be analysed holistically. Accordingly, this section presents findings related to the concentration of operations in an integrated manner, including all micro-lenders.

Geographical Spread of Microfinance Operations

88 per cent districts have micro-lending operations

Geographical spread of microfinance operations is an important indicator of the breadth of inclusion. In the first chapter it was mentioned that there is a strong regional skew in financial sector operations. The data from CRIF High Mark shows that as of March 2018 micro-lending is spread over 588 districts in India, of which 501 have more than five lenders. Considering that 44 districts of Andhra Pradesh and Telangana have not seen resumption of micro-lending post-2010 AP ordinance, micro-lending operations now cover 88 per cent districts in India.

The influence of NBFC-MFIs in this space is evident from the fact that as against coverage of 588 districts by all lenders, NBFC-MFIs cover 563 districts. This validates the feeling that the operations of NBFC-MFIs act as a catalyst for attracting other lenders. The other important feature which emerges out of district-wise distribution is that an overwhelming number of districts have more than five lenders, implying enough market

Table 5.4: Presence of Micro-Lenders across Districts in India

	NA (districts in AP and Telangana)	0	<=2	3 to 5	>5	Total
All agencies	44	80	46	41	501	712
MFIN members	44	119	51	119	379	712
All NBFC-MFI	44	105	59	88	416	712

Source: http://mfinindia.org/resource-center/mfin-publications/

players. In 2016, micro-lending operations covered 569 districts, which means that in the last two years only 19 districts have been added by micro-lenders.

Breadth does not show much, depth remains highly skewed

While coverage of 88 per cent districts is a thing to be proud of, analysis of the depth data shows concentration of operations. In section 2 of this chapter, state-level concentration in the operations of NBFC-MFIs was presented where the top six states account for 62 per cent of the portfolio. In this section, analysis of district-wise data in respect of all micro-lenders (banks, SFBs, NBFCs, NBFC-MFIs) and only NBFC-MFIs is presented. This data represents the group-lending portfolio.

Of 588 districts, the top 100 districts account for 50 per cent of the portfolio, the bottom 100 have a 0.4 per cent share

District-wise portfolio analysis shows a similar trend across all micro-lenders as well as NBFC-MFIs. Even though the operations cover nearly 600 districts, the majority of the portfolio is in the top 200 districts in terms of portfolio size. If data is analysed in terms of the top 10, 25, 50 and 100 districts, the skew gets more accentuated. To illustrate the point, while the top 100 districts account for nearly 50 per cent of the portfolio, the top 10 districts have nearly a 10 per cent portfolio share. As the number of districts is reduced, the percentage of the portfolio becomes similar to the number of districts (Figure 5.18).

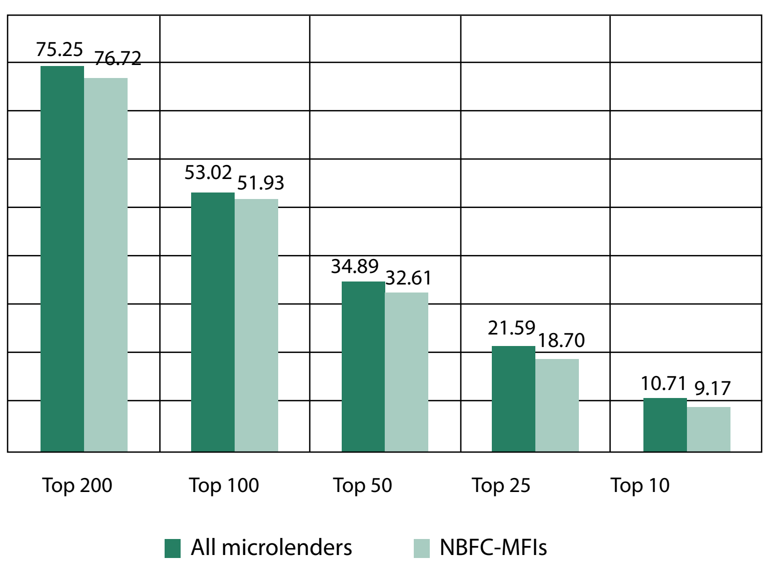


Figure 5.18: Districts' Share in the Micro-Lending Portfolio (in per cent)

Source: Data provided by CRIF High Mark

Table 5.5: District-wise Share in the Portfolio

Districts	All micro-lenders	NBFC-MFIs
Top 200	75.25	76.72
Top 100	53.02	51.93
Bottom 200	3.55	4
Bottom 100	0.37	0.44

Source: Data provided by CRIF High Mark.

Despite the fact that the total micro-lending portfolio across all lenders at Rs 137 lakh crore is nearly 180 per cent higher than the portfolio of NBFC-MFIs as of March 2018, the district-level concentration exhibits a similar pattern.

District-level analysis shows it amply that there is a strong portfolio concentration at the district level. The point becomes starker when the share of districts other than the top 200 is seen. It is striking that the bottom 200 districts in both cases make up less than 4 per cent share in the portfolio. Considering overall micro-lending operations along with this data point, it can be said that effectively the presence is restricted to around 350 districts. In other districts the portfolio is so small that it can only be termed as a token presence. To illustrate the point further, the district with the highest portfolio had a Rs 1,900 crore micro-lending portfolio as on March 2018, the 100th district had a Rs 400 crore portfolio, and the 200th district had a Rs 210 crore portfolio.

Top districts are concentrated in a few states

In the case of NBFC-MFIs, section 2 of the chapter mentions that six states account for 62 per cent of the portfolio—Karnataka, Odisha, Uttar Pradesh, Bihar, Tamil Nadu and Maharashtra. For all micro-lenders, state-wise data is not available but can be inferred from the location of the top 25 districts. An analysis of the top 25 districts across all micro-lenders and NBFC-MFIs shows some definite patterns (Figure 5.19). In both cases, the top 25 districts are located in five states—Odisha is the only state which is distinct in the top 25 districts' list of NBFC-MFIs and of all lenders. The common states are West Bengal, Tamil Nadu, Maharashtra, Karnataka and Bihar. Considering the similarity of portfolio distribution across districts in the case of MFIs and all lenders, we can infer that other lenders' operations are also concentrated in these five or six states.

8 out of Top 10 districts are in West Bengal

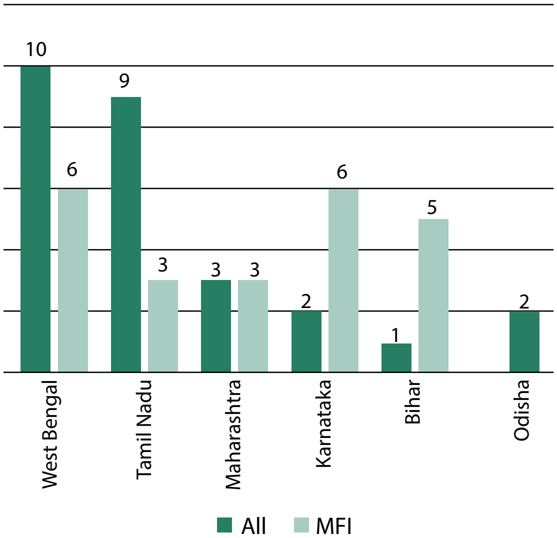


Figure 5.19: State-wise Distribution of the Top 25 Districts

Source: http://mfinindia.org/resource-center/mfin-publications/. Accessed on 26 October 2018.

The other interesting pattern is that 12 districts are common in the top 25 districts' list of all lenders and NBFC-MFIs, which shows that operations are concentrated and overlap not only at the state level but also at the district level. While the distribution of the top 25 districts is more even across states in the case of NBFC-MFIs, West Bengal stands out when all micro-lenders are included in the analysis—operations of Bandhan Bank seem to be the plausible explanation for the West Bengal tilt.

The clustering of operations in a few states/districts is a clear pointer of the concentration risk continuing to persist in the microfinance sector. The geographical risk pattern is shared by all lenders and only MFIs cannot be held accountable for this. This overlap underlies the importance of setting common ground rules across institutional forms to avoid over-indebting clients and keeping the sector sustainable.

Number of Lenders and Heat Maps: 75 Districts with >500 Crore Portfolio

To add to the points being made, an analysis of the presence of lenders and the classification of districts based on portfolio size throw up data that reinforces that micro-lending is highly concentrated and much of the growth is taking place in these areas, though some new areas get added every year.

If all micro-lenders are considered, 31 districts in the country having more than 30 lenders shows market potential in these districts, but it also demonstrates the high level of market saturation.

Table 5.6: Frequency Distribution of Lenders in the Top 100 Districts

Number of lenders	All lenders	NBFC-MFIs
45–50	4	0
40–44	6	1
35–39	11	0
30–34	10	1
25–29	6	8
20–24	6	20
15–19	7	15
10–14	0	5

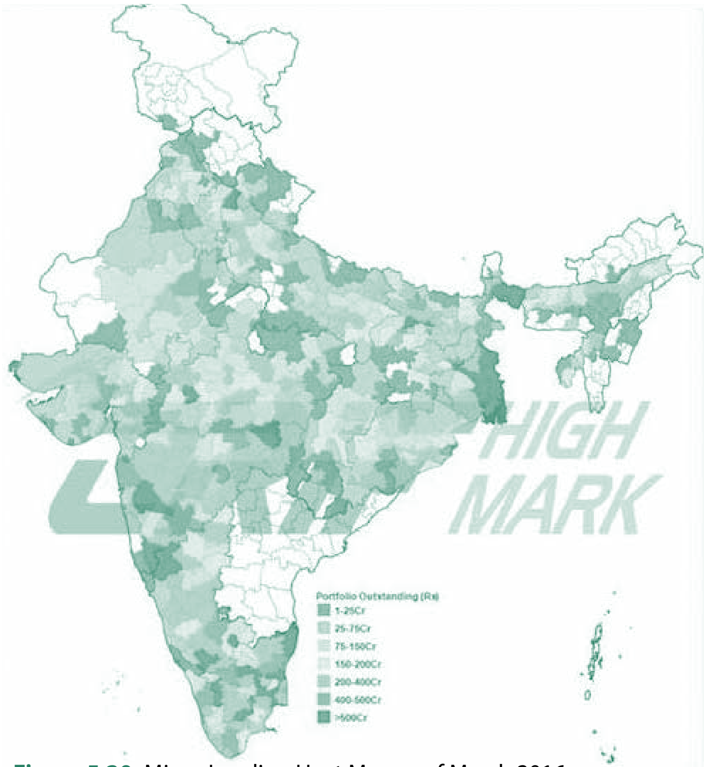
Source: Data provided by CRIF High Mark.

Indore in Madhya Pradesh is the district with the highest number of lenders at 50. This is a reflection of the practice that institutions find it easier to expand in places where there is an existing vibrant microfinance market. The chances of getting clients who already know microfinance operations are high in this market, and thus the operational cost of training and group formation lessens. At the same time, a clear correlation is seen between the number of micro-lenders and the ranking of districts by portfolio in the top 50 districts. Higher ranked districts have more lenders, but this is not good for the universe. To illustrate the point, while even in the top 100 districts there are 7 districts with 15–19 lenders, there are 23 lenders in the 200th district (Karnal in Haryana).

The number of lenders thins very fast after the top 200 districts in line with the steep tail in the portfolio. The point about increasing the number of lenders and the consequent higher portfolio is more clearly seen in the heat maps. As the picture pertaining to all micro-lenders is more appropriate for seeing the increase in concentration along with a comparison of year-wise position, Figures 5.20 and 5.21 present the heat maps for March 2016 and March 2018.

Annexure 5.2 gives details of the top 100 districts for all lenders and Annexure 5.3 for NBFC-MFIs.

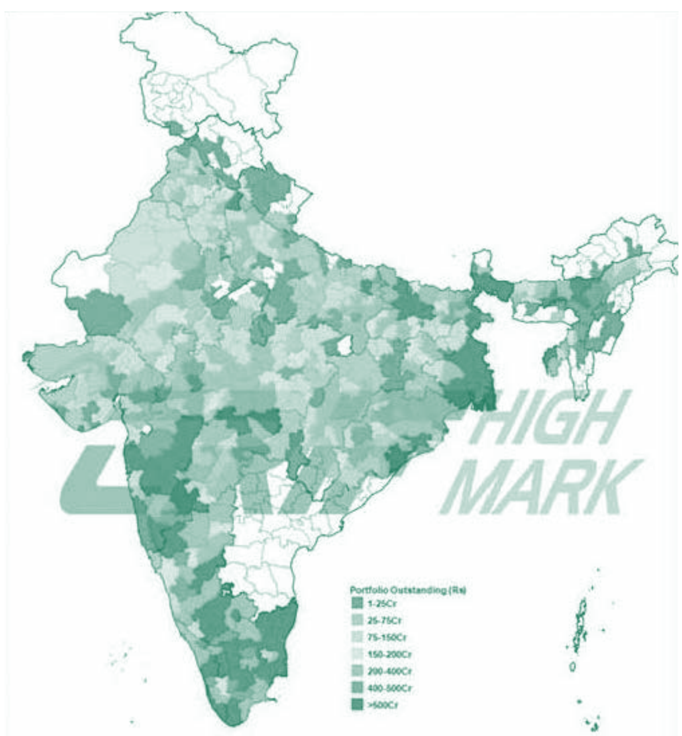
The two maps clearly show the rapid increase in portfolio concentration in south, west and east India. The highest class (>Rs 500 crore) has seen a major jump of 47 districts, and that >500 crore is a very wide class is underlined by the fact that 16 districts have a portfolio in excess of Rs 1,000 crore. North 24 Parganas in West Bengal has the highest portfolio size of Rs 1,900 crore.



Portfolio (in Rs crore)	No. of districts
>500	28
400–500	17
200–400	88
150–200	49
75–150	106
25–75	132
1–25	117

Figure 5.20: Micro-Lending Heat Map as of March 2016

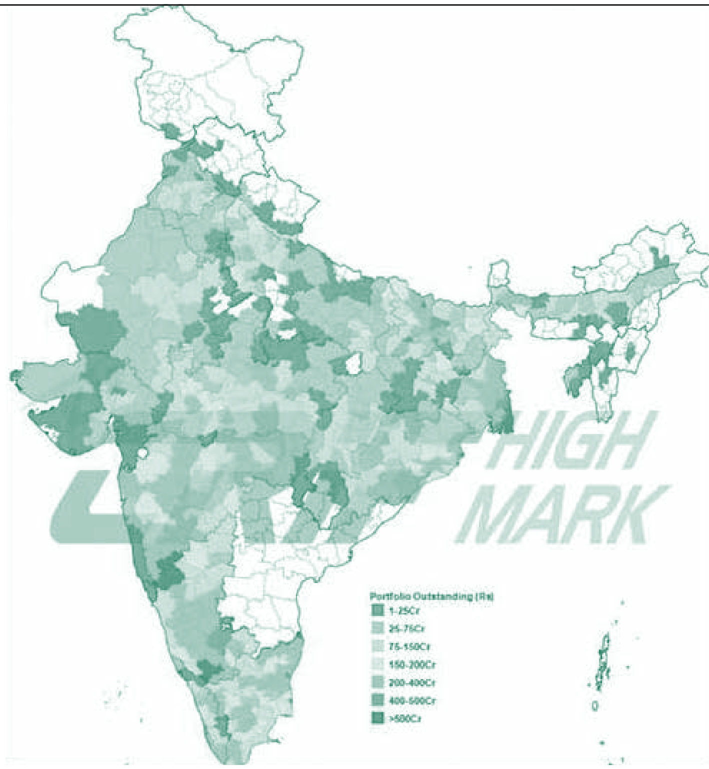
Source: Data provided by CRIF High Mark.



Portfolio (in Rs crore)	No. of districts
>500	75
400–500	29
200–400	126
150–200	41
75–150	105
25–75	93
1–25	85

Figure 5.21: Micro-Lending Heat Map as of March 2018

Source: Data provided by CRIF High Mark.



Portfolio (in Rs crore)	No. of districts
>500	02
400–500	04
200–400	62
150–200	36
75–150	127
25–75	162
1–25	133

Figure 5.22: NBFC-MFI Heat Map as of March 2018

Source: Data provided by CRIF High Mark

NBFC-MFIs also show a geographically similar concentration (Figure 5.22), but considering that their portfolio is around 40 per cent of the total micro-lending portfolio, the saturation is not so prominent.

Mysore, the district with the highest portfolio of NBFC-MFIs, pales at Rs 580 crore in comparison to North 24 Parganas at Rs 1,900 crore. However, this cannot be seen as a comforting factor, as the other lenders and NBFC-MFIs share the same products and clients—most other lending comes from banks and SFBs, which were earlier NBFC-MFIs. To add to it, this analysis excludes SHG lending. While in the case of NBFC-MFIs, the margin cap can be said to be acting as a deterrent to spreading out in thinly populated and remote areas, the same is not true of banks, SFBs and NBFCs. NBFC-MFIs with assets more than Rs 100 crore have to keep their margin within 10 per cent, and this permissible margin includes transaction cost, risk cost and profit margin. Transaction cost in the sector has already come down to around 5 per cent, almost touching the formal banking level, and risk cost and profitability are not in the hands of MFIs but driven by external events and investors. Smaller MFIs have an additional problem, as due to higher cost of funds they are not able to operate even with the permissible margin of 10 and 12 per cent. Due to the higher cost of funds they hit the ceiling of the RBI regulation in a falling base rate regime. The rush to lower transaction cost is one of the prime factors for the concentration of NBFC-MFI operations and shows the negative side of a pricing cap. However, other lenders that do not have to abide by these interest rate regulations also focusing on high saturation areas is a matter of serious concern. This is coupled by the fact that the interest rate charged by banks on microfinance loans is no less than NBFC-MFIs despite having a much lower cost of funds.

> While MFIs are constrained by pricing regulations to spread thin, banks and SFBs have no such constraint and yet focus on high concentration markets

Does Concentration Lead to Increased Multiple Lending and Portfolio Quality Issues? The Answer Is Yes

Often when the market saturation picture is presented, the response from lenders is that portfolio

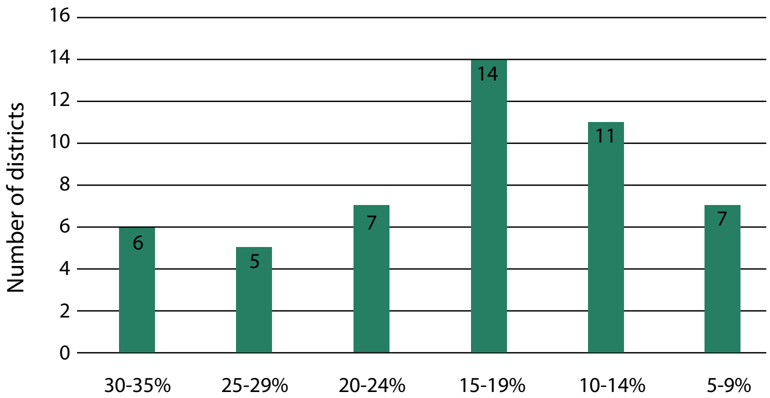


Figure 5.23: Frequency Distribution of Clients with More than Two Lenders in the Top 50 Districts (in per cent)

Source: Data provided by CRIF High Mark

concentration is a wrong yardstick even at the district level, as there can be more economic potential in these areas leading to a higher number of clients. To analyse this, data from the credit bureau for the top 50 districts was examined from the perspective of (i) the percentage of clients having loans from multiple lenders and (ii) the portfolio quality range in these districts. The answer from data sets points to increased multiple lending in the top 50 districts, as also credit quality concerns.

Figure 5.23 shows that in 18 districts, 20 per cent or more clients have more than two lender relationships. It is to be noted that number of lenders does not equal number of loans as a client can have more than one loan from a single lender, which means that if measured in terms of number of loans, the percentage will be even higher. There is not a single district in which less than 5 per cent clients have more than two lender relationships.

Though it can be argued that loan sizes of each lender are small and not sufficient to meet the genuine requirements of the client, and hence the need for multiple lenders. This argument shows that lenders are keeping loan sizes low to minimise risk but forcing clients to borrow from multiple sources—not a client-centric practice. But the argument of low loan size versus higher client requirement does not hold good when portfolio quality in these districts is examined. Figure 5.24 reflects the higher portfolio at risk figure in these districts even from a lenient measure of 31–180 days. Typically, the sector has claimed less than 1–1.5 per cent PAR, but 37 districts out of 50 have much higher PAR than the normal range. The average loan exposure per client in the top 50 districts ranges from Rs 91,524 to Rs 48,362—this is the average in the district and actual figures might be even higher. The sector needs to acknowledge that concentration risk is a real thing and will harm both clients and institutions.

CONCLUDING OBSERVATIONS

The microfinance sector (NBFC-MFIs) has demonstrated its resilience time and again, and the year 2018 witnessed another testimony to this. MFIs weathered the pile up of defaults post-demonetisation, cleaned up their balance sheets and got back to business with 50 per cent portfolio growth. The MFI industry now caters to nearly 25 million low-income clients and has been the prime source of small-value loans in the economy. Banks and NBFCs have joined the bandwagon after seeing its success. The reach of MFIs is enviable and that

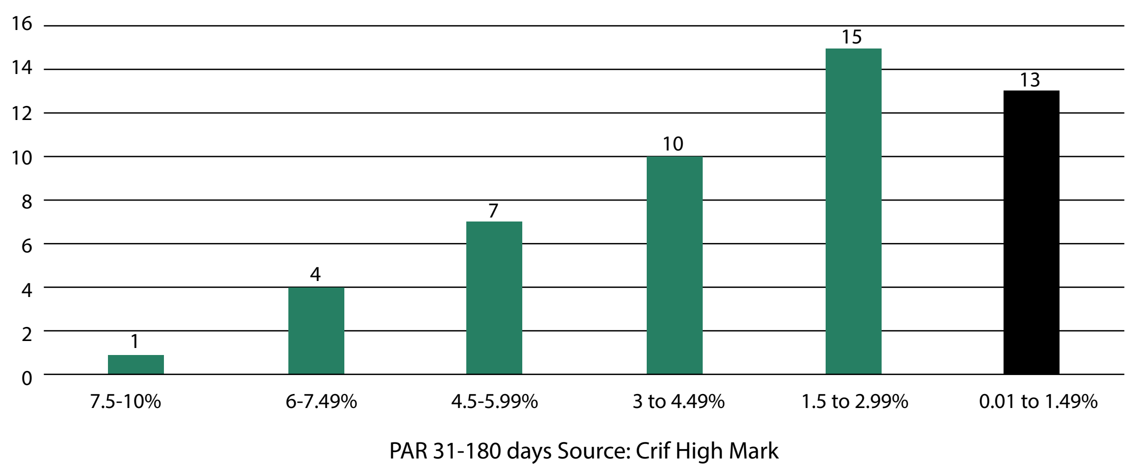


Figure 5.24: Frequency Distribution of the Top 50 Districts with PAR 31–180 Days

Source: Data provided by CRIF High Mark is proven by the long line of consumer goods, insurance and now even capital market-based savings companies wooing MFIs to leverage the latter's extensive branch network and customer base. The merger of the biggest NBFC-MFI, the BFIL, with IndusInd Bank during the year has opened another dimension to the sector wherein banks are no longer content doing wholesale lending to MFIs or building part of their portfolio through the BC route but want to acquire the entire business for on-book growth.

This is a crucial juncture and in fact an inflection point for the MFI sector, where along with immense possibilities it appears that the foundational principles of microfinance are losing their sheen. Negligible product innovation, venturing into non-core areas like selling of third-party products, lack of traction for mobilising savings as BC due to commercial considerations, and weakening of client relationship at the altar of productivity and digital come to the fore as prime examples. It must be reiterated that micro-regulation NBFC-MFIs' business as well as regulatory arbitrage available to other micro-lenders are also contributing to this situation, where MFIs are not sure of their future business model and have hence got into a stage of experimentation with new business strategies. Three possibilities are seen for MFI players in the sector: (i) becoming a BC with the bank and not doing business on its book; (ii) using the client base to get into new business lines to the extent permissible for the diversification of the income stream and to ensure readiness for the future; and (iii) continuing to stick to the core and improving the service quality to create a wow factor for clients, which will act as its differentiator from other players.

It is not clear as to how the model of becoming a full BC of the bank will pan out and will depend on the appetite of banks for low-income market and client centricity. The option of using the client base to do other business seems to be a recipe for being neither here nor there. The sector needs to realise that its client reach and operational best practices have stood the test of time and further investment in those will provide it the comparative advantage in the years to come. Client-centric products; a deeper understanding of clients' needs by strengthening client relationships instead of reducing them to being only transactional in nature; offering other financial services like savings as BC, even at a lower margin; and spreading into unsaturated areas are some of the key things which will give MFIs the comparative margin. It needs to be underscored that MFIs have a vital role in the financial inclusion of the excluded and that role will get further enhanced by investing in understanding the client and not by using the client as captive market.

However, it must be reiterated that this journey cannot be undertaken by MFIs on their own—it has to be facilitated by regulatory support. Key areas of regulatory support required relate to levelling the playing field across micro-lenders, considering relaxations in pricing cap for enabling MFIs to expand operations into unsaturated areas, and continuing with the policy of wholesale lending by banks to MFIs, albeit at a lower rate, justified by the inclusion of the last-mile customer. Last but not the least, since concentration risk remains alive and kicking, MFIs and other players must acknowledge it and take corrective steps, even if it means going against the grain of the bottom line. This is because MFIs have demonstrated their ability to provide last-mile financial services and the ecosystem should facilitate it further, while at the same time ensuring that microfinance operations remain client-centric.

ANNEXURE 5.1:
State and Region-wise Portfolio Outstanding of NBFC-MFIs (in Rs. Crore)

CENTRAL	March, 2015	March, 2016	March, 2017	March, 2018
Chhattisgarh	363	582	811	1,111
Madhya Pradesh	1,406	2,314	2,492	3,898
	1,770	2,896	3,303	5,009
EAST AND NORTHEAST	**March, 2015**	**March, 2016**	**March, 2017**	**March, 2018**
Arunachal Pradesh		0.23	0.69	1.64
Assam	62	171	364	852
Bihar	1,119	1,956	3,101	4,677
Jharkhand	251	545	814	1,397
Manipur			0.46	-
Meghalaya		0.47	4.97	5.67
Mizoram		0.56	2.07	3.31
Nagaland			-	-
Odisha	1,288	2,382	3,126	5,283
Sikkim		0.08	0.89	3.78
Tripura		2.40	25	111
West Bengal	875	1,418	2,115	3,538
	3,596	6,475	9,554	15,871
NORTH	**March, 2015**	**March, 2016**	**March, 2017**	**March, 2018**
Chandigarh	0.35	7.46	2.94	4.22
Delhi	122	128	56	87
Haryana	150	387	599	856
Himachal Pradesh	1.95	7.52	12	18
Jammu and Kashmir	2.66	2.51	3.65	2.14
Punjab	249	588	797	1,247
Uttar Pradesh	2,212	3,432	3,520	4,804
Uttarakhand	218	317	292	339
	2,956	4,869	5,282	7,358
SOUTH	**March, 2015**	**March, 2016**	**March, 2017**	**March, 2018**
Andhra Pradesh	2,166.11	2,103.35	78.35	119.32
Karnataka	2,155.28	3,612.76	4,303.46	6,068.23
Kerala	328	918	1,547	2,132
Puducherry	21.88	21.63	28.99	57.55
Tamil Nadu	903	1,805	3,200	4,573
Telangana			1.90	1.30
	5,574	8,461	9,159	12,952
WEST	**March, 2015**	**March, 2016**	**March, 2017**	**March, 2018**
Goa	5	8.42	13	37
Gujarat	223	444	497	835
Maharashtra	1,332	2,504	3,102	4,516
Rajasthan	309	574	732	1,446
	1,869	3,531	4,345	6,834
Grand Total	15,765	26,233	31,643	48,025
	1,00,00,000			
All INDIA GROWTH		**66**	**21**	**51.77**

Source: MFIN Micrometer

ANNEXURE 5.2:
Top 100 Districts as per Portfolio Outstanding as of March 2018—All Lenders

STATE	DISTRICT	Rank by Portfolio Outstanding	No. of Lenders	No. of Borrowers—active (in lakh)	No. of Active Loans (in lakh)	Portfolio Outstanding-JLG (in Rs billion)
WB	NORTH TWENTY FOUR PARGANAS	1	31	5.8	8.9	19.00
WB	SOUTH TWENTY FOUR PARGANAS	2	32	5.2	6.9	15.49
WB	MURSHIDABAD	3	27	5.0	7.8	15.62
WB	JALPAIGURI	4	21	4.3	6.7	15.04
WB	NADIA	5	31	3.8	5.9	14.77
KA	BANGALORE	6	29	6.2	9.0	13.99
WB	BARDDHAMAN	7	28	4.3	7.2	14.62
WB	KOCH BIHAR	8	18	3.6	5.4	13.01
KA	MYSORE	9	26	3.5	8.1	12.59
WB	HAORA	10	20	3.6	5.4	12.53
WB	HUGLI	11	21	3.5	5.6	12.24
TN	THANJAVUR	12	39	4.0	7.7	11.86
TN	CUDDALORE	13	37	3.7	7.3	11.38
WB	KOLKATA	14	24	4.1	5.8	11.46
TN	COIMBATORE	15	43	3.9	7.0	10.96
TN	KANCHEEPURAM	16	45	4.0	7.0	11.16
TN	VILUPPURAM	17	37	3.6	6.1	9.70
MH	PUNE	18	45	3.3	5.1	9.42
TN	SALEM	19	42	3.9	6.2	9.17
KA	BELGAUM	20	38	3.0	5.5	8.58
TN	THIRUVALLUR	21	38	3.8	5.9	9.10
TN	MADURAI	22	40	3.4	6.2	8.97
BR	PATNA	23	35	3.1	5.0	8.60
TN	TIRUCHIRAPPALLI	24	45	2.9	5.2	8.22
MH	NAGPUR	25	40	3.4	5.3	8.36
BR	MUZAFFARPUR	26	36	2.9	4.9	8.17
TR	WEST TRIPURA	27	15	2.0	2.8	8.37
TN	TIRUNELVELI	28	34	2.9	5.6	8.06
AS	NAGAON	29	19	2.1	2.9	8.31
TN	VELLORE	30	43	3.4	5.5	8.07
KL	THRISSUR	31	26	2.1	4.7	7.68
BR	SAMASTIPUR	32	35	2.5	4.6	7.85
KA	TUMKUR	33	31	2.4	5.0	7.43
WB	MALDAH	34	19	2.1	3.1	7.67
BR	BEGUSARAI	35	32	2.3	4.3	7.51
OR	GANJAM	36	30	2.7	4.8	7.49
TN	DINDIGUL	37	32	2.7	5.0	7.19

STATE	DISTRICT	Rank by Portfolio Outstanding	No. of Lenders	No. of Borrowers—active (in lakh)	No. of Active Loans (in lakh)	Portfolio Outstanding-JLG (in Rs billion)
KL	PALAKKAD	38	27	2.0	4.2	7.02
KL	KOLLAM	39	21	2.2	4.8	7.25
MH	KOLHAPUR	40	43	2.2	4.2	6.84
TN	THIRUVARUR	41	32	2.3	4.5	6.95
MP	INDORE	42	50	2.5	4.2	6.80
WB	PURBA MEDINIPUR	43	17	1.9	2.9	6.97
TN	CHENNAI	44	38	3.3	4.6	6.84
TN	NAGAPATTINAM	45	31	2.3	4.5	6.86
MH	SOLAPUR	46	37	2.3	4.3	6.65
KL	ALAPPUZHA	47	19	2.0	4.5	6.60
KL	THIRUVANANTHAPURAM	48	17	1.9	4.0	6.78
WB	UTTAR DINAJPUR	49	22	2.2	3.2	6.48
TN	TIRUPPUR	50	38	2.3	4.3	6.34
KA	MANDYA	51	25	1.7	3.9	6.44
MH	JALGAON	52	31	2.2	4.1	6.58
BR	PURBA CHAMPARAN	53	28	2.2	3.8	6.41
TN	ERODE	54	41	2.3	4.0	6.13
OR	KHORDHA	55	37	2.5	4.2	6.44
AS	KAMRUP	56	28	1.8	2.6	6.44
MH	THANE	57	30	2.4	3.6	6.24
BR	SARAN	58	29	2.1	3.1	5.91
OR	CUTTACK	59	31	2.1	3.9	6.09
KA	HASSAN	60	28	1.7	3.5	5.88
BR	VAISHALI	61	32	2.0	3.5	5.88
WB	PASCHIM MEDINIPUR	62	23	1.9	2.8	5.68
WB	BIRBHUM	63	20	2.0	3.0	5.77
AS	SONITPUR	64	17	1.5	2.0	5.51
TN	TIRUVANNAMALAI	65	36	2.0	3.5	5.64
UP	GORAKHPUR	66	25	2.3	3.4	5.59
MH	AHMADNAGAR	67	40	2.0	3.4	5.33
TN	PUDUKKOTTAI	68	37	1.9	3.4	5.45
MH	AMRAVATI	69	30	2.3	3.6	5.40
WB	DARJILING	70	20	1.5	2.2	5.32
UP	SAHARANPUR	71	24	2.3	3.0	4.87
MH	AURANGABAD	72	33	1.8	3.1	5.13
KA	DAVANAGERE	73	30	1.7	3.2	4.91
TN	KANNIYAKUMARI	74	26	1.6	3.1	4.99
KA	BELLARY	75	29	1.8	3.1	4.94
TN	THENI	76	26	1.7	3.3	4.81

STATE	DISTRICT	Rank by Portfolio Outstanding	No. of Lenders	No. of Borrowers—active (in lakh)	No. of Active Loans (in lakh)	Portfolio Outstanding-JLG (in Rs billion)
UP	VARANASI	77	35	1.9	3.0	4.82
MH	NASHIK	78	35	1.9	3.2	4.62
MH	YAVATMAL	79	29	2.2	3.3	4.70
MP	JABALPUR	80	43	1.9	3.2	4.73
KA	CHAMARAJANAGAR	81	25	1.2	2.9	4.63
RJ	JAIPUR	82	40	1.8	2.6	4.34
AS	KAMRUP METROPOLITAN	83	26	1.3	1.9	4.39
GJ	AHMADABAD	84	33	1.9	2.7	4.49
MH	MUMBAI	85	29	1.8	2.7	4.51
AS	CACHAR	86	8	1.1	1.3	4.66
TN	VIRUDHUNAGAR	87	33	1.8	3.3	4.45
GJ	VADODARA	88	33	1.6	2.5	4.25
MH	SANGLI	89	40	1.4	2.7	4.32
AS	GOLAGHAT	90	13	1.1	1.6	4.23
WB	DAKSHIN DINAJPUR	91	16	1.4	2.1	4.27
MP	UJJAIN	92	48	1.6	2.7	4.28
OR	PURI	93	29	1.5	2.7	4.33
UP	ALLAHABAD	94	27	1.8	2.8	4.19
TN	NAMAKKAL	95	38	1.6	2.8	4.05
KL	ERNAKULAM	96	23	1.3	2.5	4.10
OR	BHADRAK	97	29	1.4	2.4	4.22
OR	BALANGIR	98	26	1.4	2.6	4.14
BR	BHAGALPUR	99	25	1.2	2.1	4.11
BR	PURNIA	100	28	1.3	2.1	4.07

Source: http://mfinindia.org/resource-center/mfin-publications/.

ANNEXURE 5.3:
Top 100 Districts in NBFC-MFI operations

State Code	District	No. of NBFC-MFIs	No. of Loans (Lakhs)	Portfolio Outstanding (Rs Bn)
KA	MYSORE	16	4.3	5.84
KA	BELGAUM	21	3.6	5.28
WB	KOLKATA	19	3.3	4.80
KA	TUMKUR	15	3.5	4.66
BR	SAMASTIPUR	27	2.8	4.11
WB	NORTH TWENTY FOUR PARGANAS	21	3.3	4.06
WB	MURSHIDABAD	19	3.2	3.98
BR	BEGUSARAI	23	2.6	3.95
BR	MUZAFFARPUR	28	2.7	3.95
WB	BARDDHAMAN	22	2.9	3.88
KA	HASSAN	18	2.5	3.83
WB	NADIA	31	2.7	3.58
OR	GANJAM	20	2.5	3.53
WB	SOUTH TWENTY FOUR PARGANAS	40	2.8	3.44
TN	KANCHEEPURAM	21	2.0	3.43
MH	KOLHAPUR	24	2.3	3.38
BR	PATNA	27	2.3	3.30
OR	KHORDHA	19	2.3	3.19
TN	CUDDALORE	20	2.1	3.16
KA	BANGALORE	27	2.6	3.14
BR	VAISHALI	28	2.1	3.10
MH	SOLAPUR	28	2.3	3.10
KA	DAVANAGERE	17	2.1	3.04
KA	MANDYA	12	2.1	3.02
KL	KOLLAM	12	2.2	3.02
TN	MADURAI	20	2.2	3.00
TN	TIRUNELVELI	23	2.2	3.00
TN	THIRUVALLUR	21	1.9	2.99
BR	PURBA CHAMPARAN	22	2.1	2.98
OR	CUTTACK	20	2.1	2.90
TN	VILUPPURAM	17	1.9	2.85
WB	HAORA	16	2.0	2.76
TN	VELLORE	22	2.0	2.66
WB	HUGLI	22	1.9	2.66
KL	ALAPPUZHA	10	2.0	2.59
MH	AMRAVATI	22	1.6	2.56
KA	SHIMOGA	19	1.7	2.53
MP	JABALPUR	21	1.7	2.53
OR	BARGARH	16	1.7	2.47

State Code	District	No. of NBFC-MFIs	No. of Loans (Lakhs)	Portfolio Outstanding (Rs Bn)
MH	JALGAON	24	1.8	2.47
KA	CHITRADURGA	15	1.7	2.47
KL	PALAKKAD	14	1.5	2.40
MH	AHMADNAGAR	29	1.7	2.39
MH	SANGLI	23	1.6	2.34
KL	THIRUVANANTHAPURAM	12	1.4	2.34
UP	GORAKHPUR	20	1.5	2.34
KA	HAVERI	19	1.5	2.32
OR	SUNDARGARH	17	1.6	2.32
WB	JALPAIGURI	18	2.2	2.30
MP	INDORE	25	1.6	2.27
MP	CHHINDWARA	19	1.4	2.27
OR	BALANGIR	17	1.5	2.25
MH	YAVATMAL	23	1.5	2.22
KA	BELLARY	16	1.5	2.21
TN	SALEM	23	1.9	2.19
OR	BALESHWAR	18	1.6	2.11
OR	BHADRAK	19	1.4	2.11
KA	CHAMARAJANAGAR	16	1.4	2.11
UP	BULANDSHAHR	17	1.0	2.10
MH	AURANGABAD	25	1.4	2.06
KA	CHIKMAGALUR	16	1.4	2.05
MH	NAGPUR	24	1.4	2.05
TN	COIMBATORE	22	1.4	2.04
MP	SAGAR	25	1.4	2.02
KA	DHARWAD	18	1.4	2.00
TN	DINDIGUL	18	1.5	2.00
MH	THANE	35	1.2	2.00
UP	ALLAHABAD	21	1.3	2.00
TN	THIRUVARUR	18	1.4	1.98
TN	TIRUVANNAMALAI	20	1.2	1.96
BR	SARAN	26	1.3	1.89
KA	DAKSHINA KANNADA	17	1.3	1.89
TN	THANJAVUR	20	1.4	1.89
TN	TIRUPPUR	19	1.4	1.88
TN	SIVAGANGA	22	1.3	1.88
OR	PURI	21	1.3	1.86
BR	PASHCHIM CHAMPARAN	20	1.3	1.85
MH	NASHIK	30	1.3	1.85
KL	THRISSUR	12	1.3	1.84
KA	RAMANAGARA	16	1.4	1.83

State Code	District	No. of NBFC-MFIs	No. of Loans (Lakhs)	Portfolio Outstanding (Rs Bn)
TN	CHENNAI	23	1.2	1.80
TN	NAGAPATTINAM	20	1.3	1.79
OR	JAJAPUR	19	1.2	1.71
UP	BIJNOR	15	1.0	1.71
MH	BULDANA	26	1.3	1.70
TN	TIRUCHIRAPPALLI	21	1.1	1.70
AS	SONITPUR	16	0.8	1.69
BR	PURNIA	18	1.1	1.67
JH	GIRIDIH	14	1.2	1.67
AS	NAGAON	19	0.9	1.67
MH	NANDED	22	1.2	1.66
OR	KALAHANDI	16	1.2	1.65
OR	DHENKANAL	14	1.2	1.65
MH	PUNE	37	1.2	1.65
UP	KUSHINAGAR	16	1.1	1.65
UP	VARANASI	23	1.1	1.64
UP	SAHARANPUR	18	1.1	1.63
TN	VIRUDHUNAGAR	22	1.2	1.58
BR	KATIHAR	23	1.1	1.57
WB	KOCH BIHAR	14	1.8	1.56

Source: http://mfinindia.org/resource-center/mfin-publications/.

REFERENCES

1 The financial and operational data is from MFIN and CRIF High Mark. In some places adjustments have been made by the author to avoid errors and double counting.

2 'MFI sector' is used to signify NBFC-MFI members of MFIN as data for other NBFC-MFIs is not available and they constitute a smaller segment of the market. The data reported in Figure 5.1 for NBFC-MFIs is for the universe, while the analysis in the chapter is for MFIN members, hence the two figures are different.

3 https://www.livemint.com/Opinion/9ZWgRWMtD11ts6xe7ygAmJ/The-untold-story-behind-IndusInd-BankBharat-Financial-merge.html. Accessed on 12 August 2018.

4 RBI. DNBS.(PD) CC No. 395/03.10.38/2014-15. Dated 1 July 2014.

5 RBI/2017-18/35 DBR.CID.BC.No.79/20.16.042/2017-18. Dated 2 August 2017.

6 Arrived at by dividing the total gross loan portfolio by the total number of clients.

7 RBI/2015-16/20 DNBR (PD) CC.No.047/03.10.119/2015-16.

8 Field visits in Muzaffarpur and Vaishali districts on 22 and 23 June 2018.

9 The MFIN declined to reveal the names of signatories to MACC citing privacy issues.

10 Data for this section provided by CRIF High Mark.

11 According to the regulation, interest rates can either be (i) cost of funds plus 10 or 12 per cent margin or (ii) 2.75 times the base rate of five commercial banks, whichever is lower. In July 2018 the applicable base rate was 8.92 per cent, which implies that the interest rate based on this formula cannot be more than 24.53 per cent. If a small MFI has 14.5 per cent cost of funds, it cannot add 12 per cent to this and charge 26.5 per cent as 2.75 multiples of the base rate is lower and that has to be followed.

SHG Banking and the NRLM Factor in Financial Inclusion

6

TWENTY FIVE YEARS OF THE SHG-BANK LINKAGE PROGRAMME: A STOCKTAKING

There are multiple narratives around the role and development of SHGs. As the number of SHGs has multiplied in the past 25 years and more, so have the types of activities and innovations that have been designed around them. As a result, the SHG 'movement' represents a rich diversity of interventions and outcomes difficult to classify and analyse. However, within the larger SHG movement, the programme for linking SHGs with banks has been the core innovation that has been the mainstay of SHG development during this period.

By a series of circulars in 1991–92, the Reserve Bank of India (RBI) and NABARD set out the framework for linking SHGs to banks—the SHG-bank linkage programme (SBLP). There were three important policy decisions governing this innovation:

- Banks could lend to SHGs without ascertaining the purpose for which the loan was being taken by the eventual borrower.
- Banks could undertake lending to groups without physical collateral.
- Banks could be allowed to lend to unregistered groups.

The SHG model thus promoted was essentially a savings-led and savings-linked credit model, with a minimum savings period of six months prior to the availability of bank credit. It was positioned as a 'supplementary channel' for the provision of credit, not as an alternative to mainstream banking. The rationale for the interest of bankers was primarily the possibility of externalisation of transaction costs of small loans and ensured recoveries through the operation of peer pressure among group members.

SHGs and SHG-based community institutions have emerged as an important part of the development infrastructure in India as also an arena for the empowerment of women. Indeed, SHGs have been strongly associated with the assertion of the agency of women in development processes, but often increasingly also as instruments in the delivery mechanism of the state. While in the initial stages NABARD, along with some leading NGOs, was the main proponent of SHG-bank linkage with a target-driven approach to the promotion of SHGs, the initiative for SHG development has since been ceded by NABARD to state governments.

On account of the relatively small average loan size to groups and the reluctance of NGOs to act as financial intermediaries between banks and SHGs, both NGOs and government self-help promoting agencies (SHPAs) started promoting community organisations in the form of SHG federations. This was done in order to strengthen the quality of groups, to facilitate bank linkage, as also to act as microfinance institutions (MFIs) on-lending to SHGs with borrowed funds. According to estimates made by the Andhra Pradesh Mahila Abhivruddhi Samiti (APMAS), as of March 2013 there were 1,78,664 federations of SHGs in the country. These included 1,71,511 primary-level federations, 7,087 secondary-level federations, and 66 tertiary-level financial and non-financial federations. However, detailed data regarding the functions of federations, legal forms and funds managed by them were not available. The state governments of Andhra Pradesh, Tamil Nadu and Kerala were prominent in promoting SHG federations.[1]

Only some of the above federations were engaged in financial intermediation. Over the years the role of the financial federation has continued to be a contested one. On the one hand a federation facilitates aggregation of SHG demand for credit, mobilisation of savings and provision of support services; on the other it undermines the role of the SHG in financial intermediation and cuts into SHG margins by adding another layer (or a set of layers) in the intermediation chain. Also, federations are seen as being organisationally weak and liable to elite capture as in the case of cooperatives. Despite much debate and arguments in favour and against, NABARD and the bankers did not take kindly to the idea of federations as financial intermediaries. More recently, it is the National Rural Livelihoods Mission (NRLM) that is determined to see through the project of federations as financial intermediaries between banks and other financing agencies, and the SHGs.

Within NABARD, following the launch of the SBLP, great stress was laid on SHG formation and the motivation and capacity building of bankers to engaged with SHGs. However, there had been relatively little by way of innovation. SHG-bank linkage has also until recently been characterised by a relatively straightforward product design in the form of a term loan from the bank which was a multiple of the savings of the SHGs.

After the initial enthusiasm and a target-oriented effort to promote a million groups by 2004 (which was easily achieved by 2001), the initiative for SHG development appears to have been ceded to state governments. It was only in 2012, after 20 years of bank linkage, that a new set of guidelines were put out in SHG 2.

1. Voluntary savings facility at the SHG level for SHG members.
2. Cash credit/overdraft system of lending for SHGs towards flexibility in borrowing.
3. Facility of formation of JLGs within SHGs for economically active members.
4. Risk-mitigation systems (such as self-rating tools and SHG-level audits) to strengthen bankers' confidence in SHGs.
5. Engagement of well functioning SHGs and NGOs by banks as BFs.
6. Strengthening of monitoring and training mechanisms.

SHG 2 evoked a mixed response. The overall impression has been that it was too little too late. It has also been argued that several of the proposals, including savings mobilisation, could better be dealt with by SHG federation structures that have evolved over the years and are now being supported by the NRLM.

The cash credit facility for SHGs was generally welcomed by banks and SHPIs. However, it is also suggested that it has been a measure of doubtful utility which may have led to evergreening of loans and concealing the true recovery position. Voluntary savings at the SHG level has been seen as a belated attempt at boosting the savings component but as being undertaken without pilot testing on the ground and which would require a deposit guarantee to support it. Initiatives for financial literacy, financial counselling and the involvement of SHG members (not SHGs, which are not eligible) as bank agents have since been undertaken and are documented elsewhere.

At present it is the NRLM and its state chapters that have become the custodians of the promotion and nurturing of women SHGs and their federations with the objective of inclusive finance and broader livelihood development. This includes harnessing the potential of the SHG sector for convergence between Government of India's mission for financial inclusion and the pre-existing financial and social infrastructure represented by SHGs, their promoters and associations.

The SBLP, as it has evolved, has been mainly about providing loans rather than savings and a wider range of financial services, even though the volume of savings mobilised has been very impressive. Beyond this there have been many notable initiatives for promoting income-generation activities, group enterprise, trading and marketing channels, apart from important contributions to the social and political participation by SHG women on a large scale. Despite many regional variations and contexts, it can be said that over the years several issues related to the SBLP have emerged. These include, among others, concentration in selected regions, concerns about the quality of groups and institutional and banker support, small average loan size, multiple memberships of SHGs and MFIs, and the practice of equal sharing of loans by SHG members. Besides, as the digitisation process takes place under the NRLM and banks, it is emerging that perhaps only about 60–70 per cent of groups that were ever given a loan are still active.

Reports also suggest that the failure in capacity building has resulted in an absence of a sense of ownership among SHG members, and that SHG meetings are often routinely held for savings collection rather than with a wider development concern. The belated government recognition and mainstreaming of SHGs has also meant that they have become vulnerable to government management patterns, namely target orientation, and channels for the provision of subsidy in the implementation of state-sponsored programmes; and SHG members are also being mobilised for political purposes. Overall, the function of SHGs in financial services provision and management has been diminished as also possibly their role in the empowerment of the poor and marginalised. It remains to be seen whether the NRLM can breathe fresh life into SHGs by mainstreaming them into digital banking towards a more holistic livelihood agenda.

SHG-BANK LINKAGE: PROGRESS AND PERFORMANCE

Starting with a small number of 620 SHGs linked to banks during the first two years (1992–93 and 1993), the number of credit-linked SHGs had grown to 2,63,825 by 31 March 2001 and to nearly 1.08 million by 31 March 2004. By 31 March 2008, when savings data was also being generated for the programme, the number of savings-linked SHGs reached over 5 million with more than 3.6 million SHGs having outstanding loans from banks. This exponential growth pattern in SHG performance continued until 2010, after which the growth tapered off[2] before witnessing a revival with the advent of the NRLM.

Review of the Progress of the SBLP during 2017–18

The progress of the SBLP from the period 2014–15 to 2017–18 is given in Table 6.1. Despite some hiccups in recent years, the SHG programme has been growing steadily over the years. As seen in the table, over 8.74 million SHGs, with a membership of about 105 million,[3] have been savings-linked with banks as of 31 March 2018. The SBLP boasts of group savings with banks of Rs 195.92 billion (or SHG savings at group and bank level of Rs 653 billion[4]) with credit outstanding of Rs 755.98 billion to 5.02 million SHGs or to over 57 per cent of the total savings-linked groups. At 7.39 million, nearly 85 per cent of the SHGs are exclusively women's groups which represent a big contribution to the participation in linkage and to women's empowerment.[5]

Table 6.1: Overall Progress under SHG-Bank Linkage for the Last Four Years

		2014–15		2015–16		2016–17		2017–18	
		No. of SHGs (in million)	Amount (in Rs billion)	No. of SHGs (in million)	Amount (in Rs billion)	No. of SHGs (in million)	Amount (in Rs billion)	No. of SHGs (in million)	Amount (in Rs billion)
SHG savings in banks	Total SHGs	7.70	110.60	7.90	136.91	8.58	161.14	8.74	195.92
		3.59%	11.74%	2.68%	23.79%	8.53%	17.69%	1.91%	21.58%
	NRLM/SGSY	3.05	44.24	3.46	62.45	3.74	75.53	4.18	104.34
		34.92%	78.56%	13.27%	41.16%	8.30%	20.94%	11.87%	38.14%
	% NRLM/SGSY	39.65	40.00	43.70	45.61	43.65	46.87	47.85	53.26
	NULM/SJSRY	0.43	10.72	0.45	10.06	0.55	11.27	0.43	13.51
				3.00%	6.12%	22.42%	11.99%	-22.73%	19.86%
	% NULM/SJSRY	5.63	9.69	5.64	7.35	6.36	6.99	4.86	6.89
	All women SHGs	6.65	92.64	6.76	120.35	7.32	142.83	7.39	174.98
		6.38%	15.61%	1.68%	29.92%	8.26%	18.67%	0.96%	22.51%
	% women groups	86.41	83.77	85.58	87.91	85.36	88.64	84.52	89.31
Loans disbursed to SHGs in the year	No. of SHGs extended loan	1.63	275.82	1.83	372.87	1.90	387.81	2.26	471.86
		19.03%	14.84%	12.67%	35.18%	3.60%	4.01%	19.00%	21.67%
	NRLM/SGSY	0.64	94.88	0.82	167.86	0.89	173.36	1.27	250.55
		28.45%	27.26%	26.91%	76.92%	8.58%	3.28%	42.81%	44.53%
	% NRLM/SGSY	39.54	34.40	44.54	45.02	46.69	44.70	56.21	53.10
	NULM/SJSRY	0.11	18.72	0.11	26.20	0.11	26.76	0.11	24.24
				5.71%	40.00%	-4.50%	2.12%	-3.64%	-9.41%
	% NULM/SJSRY	6.46	6.79	6.06	7.03	5.60	6.90	4.69	5.14
	All women SHGs	1.45	244.20	1.63	344.11	1.72	361.03	2.08	445.59
		25.69%	16.07%	12.50%	40.92%	5.34%	4.92%	20.64%	23.42%
	% women groups	89.05	83.53	88.92	92.29	90.42	93.09	91.77	94.43

SHG loan outstanding	Total SHGs	4.47	515.46	4.67	571.19	4.85	615.81	5.02	755.98
		6.46%	20.06%	4.59%	10.81%	3.74%	7.81%	3.51%	22.76%
	NRLM/SGSY	1.85	197.53	2.19	266.10	2.49	299.94	2.79	382.25
		41.24%	94.08%	18.69%	34.72%	13.69%	12.72%	12.17%	27.44%
	% NRLM SGSY	41.32	38.32	46.89	46.59	51.37	48.71	55.64	50.56
	NULM/SJSRY	0.32	34.63	0.32	39.80	0.32	41.33	0.29	53.51
				-1.57%	14.93%	1.60%	3.86%	-9.38%	29.46%
	% NULM/SJSRY	7.12	6.72	7.00	6.97	6.55	6.71	5.78	7.08
	All women SHGs	3.86	459.02	4.04	514.29	4.28	564.44	4.55	704.02
		13.27%	26.97%	4.61%	12.04%	6.14%	9.75%	6.29%	24.73%
	% women groups	86.35	89.05	86.37	90.04	88.36	91.66	90.62	93.13

Note: Highlighted figures are percentage change from the previous year.
Source: NABARD, Status of Microfinance in India 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.

According to NABARD, there are more than 100 scheduled banks, 300 DCCBs, 27 State Rural Livelihood Missions and over 5,000 NGOs engaged in the Self-Help Group Bank Linkage Programme. During 2017–18 there was a net addition of 1,60,000 SHGs to the number of SHGs savings-linked with formal financial institutions.[6] A sizeable number of these SHGs have been added during the year in priority states like Assam, Bihar, Chhattisgarh, Jharkhand, Odisha, Rajasthan and Uttar Pradesh. However, based on NABARD 2016,[7] there is probably still the potential for the formation of nearly three million additional SHGs in the country. Besides, there are still areas where the NRLM has limited presence or intervention and there exists substantial potential for the formation of SHGs. As noted in NABARD 2018 there is a need to map those pockets which lack in good SHPAs. A large nodal NGO could train smaller local NGOs to orient them for SHG promotion in these areas.

Savings

Reviewing the performance for the year 2017–18, it is observed that despite a significant growth (21.6 per cent) in the amount of savings of SHGs in banks to nearly Rs 196 billion at the end of March 2018, as compared to end-March 2017, the number of savings-linked groups increased only marginally by less than 2 per cent from the number a year earlier. The small net increase in the number of SHGs could partly be explained by better reporting standards adopted by banks by including only operative SHG accounts. The consequence of this has been a substantial increase in average savings per SHG, which reached over Rs 22,405 at the end of March 2018 as against Rs 18,780 a year earlier. By way of comparison, the number of NRLM SHGs with savings in banks increased by nearly 12 per cent during this period and the amount of bank savings by over 38 per cent. The average savings of NRLM SHGs was Rs 24,960 at the end of March 2018.

Loan disbursement

The volume of fresh loans issued by banks to SHGs during 2017–18 showed a significant growth of nearly 22 per cent to reach almost Rs 472 billion. This was matched by the increase in the number of SHGs receiving loans during the year, which rose by 19 per cent. This represented a substantial increase in the growth rate over that of the previous year, which was only about 4 per cent higher than for 2015–16 both in the number of SHGs receiving loans and the loan amount disbursed. Again it was the loan disbursement to NRLM SHGs that was principally responsible for the increase during 2017–18, with the growth of both the number of SHGs receiving loans during the year and the loan amount increasing in excess of 40 per cent each. With more and more SHGs being brought under the NRLM, there was a virtual stagnation during 2017–18 in the number of non-NRLM SHGs receiving loans and the total loan amount. A disquieting feature of the data is that only about 26 per cent of the total number of SHGs saving with banks received loans during the year. The figure was slightly higher at 30 per cent for NRLM SHGs. The average loan size during 2017–18 was about Rs 2 lakh in the case of both NRLM and non-NRLM SHGs.

Table 6.2: Progress of SHGs: Physical (Compound Annual Growth Rate)

Physical performance of SHGs	CAGR 2014–18	CAGR 2010–14	CAGR 2006–10
Number of SHGs having savings accounts with banks	4.2	1.7	27.5
Number of SHGs under NRLM/govt programmes	19.5		
Number of SHGs receiving loans during the year	13.3	–3.7	26.4
Number of SHGs receiving loans during the year under NRLM/ other govt programmes	56.4	–4.1	12.8
Number of SHGs with loan outstanding	4.6	–3.6	18.7*
Number of SHGs with loan outstanding under NRLM/govt programmes	23.9	1.2	21.9*

Note: *from 2007 to 2010
Source: NABARD, Status of Microfinance in India 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.
Tara Nair and Ajay Tankha, Inclusive Finance India Report 2014 (New Delhi: Oxford University Press, 2015).
http://www.inclusivefinanceindia.org/uploads-inclusivefinance/publications/1002-1001-FILE.pdf. Accessed on 29 September 2018.

Loan outstanding

The number of SHGs with outstanding bank loans was 5.02 million at the end of March 2018, which was 3.5 per cent higher than the number a year earlier. This follows a similar small increase in the previous four years. The loan amount outstanding, however, increased by nearly 23 per cent for all SHGs and nearly 28 per cent for NRLM SHGs. The average loan outstanding per SHG at the end of March 2018 was over Rs 1,50,000 as against around Rs 1,27,000 a year earlier. The share of NRLM SHGs in the number of SHGs with total outstanding at the end of March 2018 was nearly 56 per cent and in the case of amount outstanding it was a little over 50 per cent.

Overall SHG Growth Performance

Tables 6.2 and 6.3 provide a snapshot of the growth performance of the SBLP in terms of the important physical and financial indicators over the past 12 years since 2006.

Physical performance

For the four-year period 2006–10 the major indicators of physical progress of the SBLP (Table 6.2) show a massive increase in the compound annual growth rate (CAGR). The number of SHGs having savings accounts with banks increased at more than 25 per cent per year, and the number of SHGs with loans outstanding by nearly 19 per cent per year. However, in the subsequent four-year period since 2010, the year of the Andhra Pradesh crisis, there is an impression of stagnation and decline, with the number of SHGs having savings accounts with banks increasing by only 1.7 per cent and the number of SHGs receiving loans during the year and those with loans outstanding registering an annual decline of nearly 4 per cent each per year during this period. This period also corresponds to the interregnum covering the phase-out of the government's Swarnajyoti Gram Swarozgar Yojana (SGSY) and the initial stages of its revamped successor, the NRLM, as also the rationalisation of SHG numbers by several major banks as they took stock of their active SHGs.[8] This period also coincided with the implementation of financial inclusion plans of banks based upon individual-centred banking through an expansion of banking outreach and outsourcing of operations to BCs. However, despite the substantial social capital embodied in them, there was no clear role or strategy for SHGs within the financial inclusion discourse until the comparatively recent, but largely independent, take-off of the NRLM.

In the most recent four-year period, 2014–2018, the annual net growth in the number of savings-linked SHGs has gone up to 4.2 per cent and the number of SHGs receiving loans to 13.3 per cent annually. Contributory to this reversal in the decline has been the expansion of the scope and coverage of the NRLM in various states as the programme has matured and attained scale. Thus, there has been a spurt in the growth of the number of SHGs covered by the NRLM at 19.5 per cent per year and the annual increase in the number of SHGs receiving bank loans at 56.4 per cent.[9]

Table 6.3: Progress of SHGs: Financial (Compound Annual Growth Rate)

Financial performance of SHGs	CAGR 2014–18	CAGR 2010–14	CAGR 2006–10
Savings of SHGs with banks	18.6	12.4	26.9
Saving of SHGs under NRLM/govt programmes	47.7		
Volume of loans disbursed to SHGs during the year	18.4	13.5	33.8
of which under NRLM/other govt programmes (in per cent)	67.6	12.2	16.3
Bank loans outstanding with SHGs (in Rs billion)	15.2	11.2	31.3*
of which under NRLM/other govt programmes (in per cent)	43.6	13.0	24.2*

Note: *from 2007 to 2010
Source: NABARD, Status of Microfinance in India 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.
Tara Nair and Ajay Tankha, Inclusive Finance India Report 2014 (New Delhi: Oxford University Press, 2015).
http://www.inclusivefinanceindia.org/uploads-inclusivefinance/publications/1002-1001-FILE.pdf. Accessed on 29 September 2018.

Financial performance

The financial performance data (Table 6.3) on the CAGR similarly replicates the V-shaped pattern observed in the case of SHGs' physical performance. Thus the CAGR of savings of SHGs with banks which had declined from 26.9 per cent during 2006–10 to 12.4 per cent during 2010–14 picked up to grow at 18.6 per cent annually during 2014–18. The volume of bank loans disbursed annually, which had declined from 33.8 per cent per year during 2016—10 to 13.5 per cent during 2010–14, rose again to 18.4 per cent per year during 2014–18. The same was the case with loan outstanding with the sharp dip in growth rates being followed by the re-establishment of a more robust growth rate during the latest period 2014–18. In each case the contribution of NRLM SHGs has been the dominant factor. Despite the rate of increase of SHGs with loans, as only 50.20 lakh SHGs have outstanding loans, with banks there is still scope for 42 per cent of the SHGs, i.e. the balance of 37.24 lakh SHGs savings-linked as of March 2018, to be credit linked. It is expected by NABARD that the digitisation of all the existing SHGs will mainstream them and pave the way for their credit linkage.

REGIONAL AND AGENCY-WISE ANALYSIS

Regional Spread

The uneven progress of SHG-bank linkage, nevertheless, cannot deflect from the substantial gains that have been made in the mobilisation of savings through SHGs as also the loan funds being made available to them for on-lending to their members. However, there are the inevitable variations across regions and states. Right from the beginning the main SBLP growth areas were the southern states, which had several favourable factors operating for the success of a collective entity like the SHG. Though the dominance of the southern states has declined a little and the eastern region has come up in recent years, the growth of the other regions, particularly the north, central and northeast, has been slow to pick up and a relatively skewed pattern continues to prevail in respect of all indicators.

Savings

The number of SHG savings with banks has gone up by over 1 million from 7.70 million as of 31 March 2015 to 8.74 million as of 31 March 2018, and the average SHG savings has gone up by over 50 per cent over this period (Table 6.1). Thus, the SHGs are not only recipients of loans but also major contributors of savings to the banking system. Indeed, the total SHG savings with banks of Rs 195.92 billion as of 31 March 2018 were more than a quarter of the loan amount outstanding to SHGs from banks, i.e. Rs 775.98 billion. This, of course, can be explained by the banks retaining SHG savings as collateral for the loans given by them.

Figure 6.1 gives the shares of the different regions in the number of SHGs saving with banks and the amount of their total savings deposits. Agency-wise state-level particulars are given in Annexure 6.1. The main contributor to this impressive savings record of SHGs continues to be the southern region which contributes nearly 3.65 million SHGs, or 41.6 per cent of the total SHGs, but as much as 62.1 per cent of the total savings by SHGs as of 31 March 2018 at Rs 121.58 billion. In fact, all other regions contribute a lower share to total savings than their share in SHG numbers.

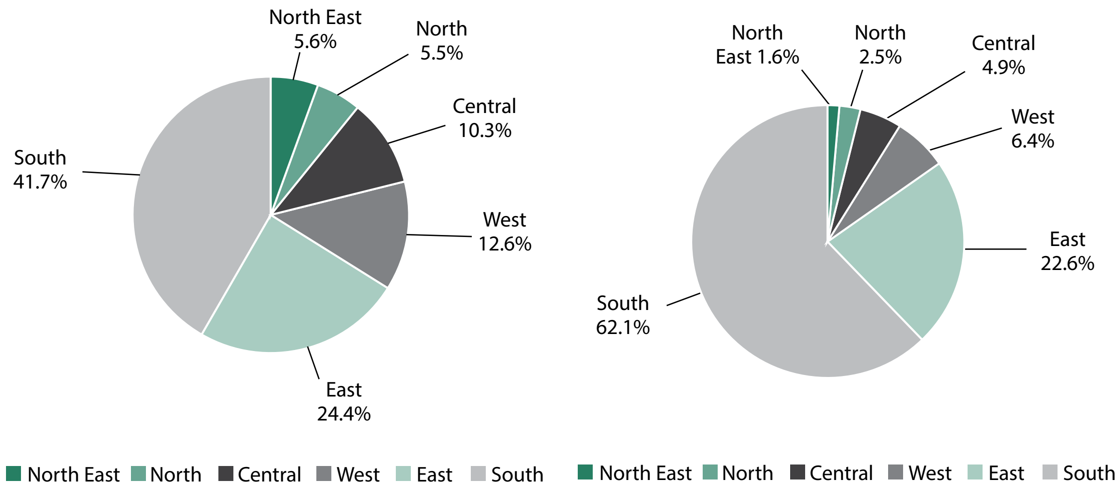


Figure 6.1: Regional Spread of SHG Savings with Banks (Accounts and Amount) as of 31 March 2018

Source: NABARD, Status of Microfinance in India 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.

With the exception of the eastern region, the average savings of all other regions would be much lower than for the SHGs as a whole. The average savings in the southern region was Rs 33,317 per SHGs as of 31 March 2018 and in the eastern region Rs 20,732, and as low as Rs 6,633 per SHG in the northeastern region. Among the states Tamil Nadu is the largest contributor to SHG numbers, followed by Andhra Pradesh and Maharashtra with West Bengal and Karnataka close behind. Total savings as of 31 March 2018 were the highest in the state of Andhra Pradesh followed by Telangana and West Bengal. The southern states have a sizeable number of matured SHGs that contribute a higher amount of monthly savings leading to a higher average savings rate, whereas in the northeastern states and other priority states, the average savings are low.

There has been virtually no change in the relative shares of the various regions in the number of SHGs with savings in banks over the years. As regards the savings amount there has been a small increase in the share of the southern region at the expense of the western and central regions.

Loan disbursement

The number of SHGs receiving loans annually has gone up from 1.63 million as of 31 March 2015 to 2.26 million as of 31 March 2018 and the average loan amount has gone up by more than 12 per cent to over Rs 2,08,000 per SHG in this period (Table 6.1). The loan amount disbursed to SHGs for India as a whole during the year 2017–18 was Rs 47,186

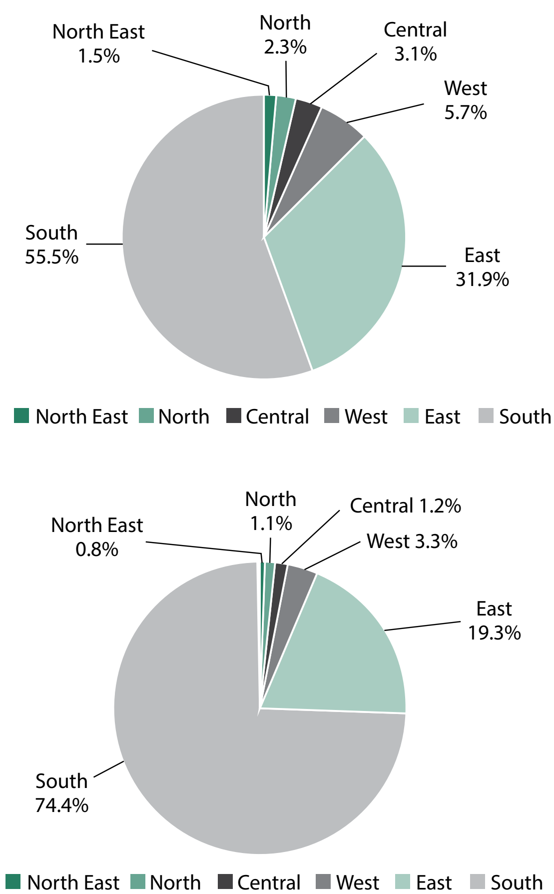


Figure 6.2: Regional Spread of Loans Disbursed to SHGs (Accounts and Amount), 2017–18

Source: NABARD, Status of Microfinance in India 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.

crore which was a substantial increase of 21.7 per cent in comparison to the previous year.

The shares of the different regions in the number of SHGs receiving loans from banks during 2017–18 and the total amount of loan received are shown in Figure 6.2. Agency-wise state-level particulars are given in Annexure 6.2. Again it is the southern region which accounts for 55.5 per cent of the total of loans to SHGs borrowing from banks during the year with the eastern region contributing an impressive 31.9 per cent of the SHGs receiving loans with the share of the other regions being quite small. The share of the southern states in total loan of Rs 471.85 billion received by SHGs during 2017–18 is still higher at 74.4 per cent. The eastern region with a share of 19.3 per cent cannot match the average loan size received by the southern states. An idea of the skewed nature of SHGs is that the remaining four regions of the country received barely 6 per cent of the loans disbursed by banks to SHGs.

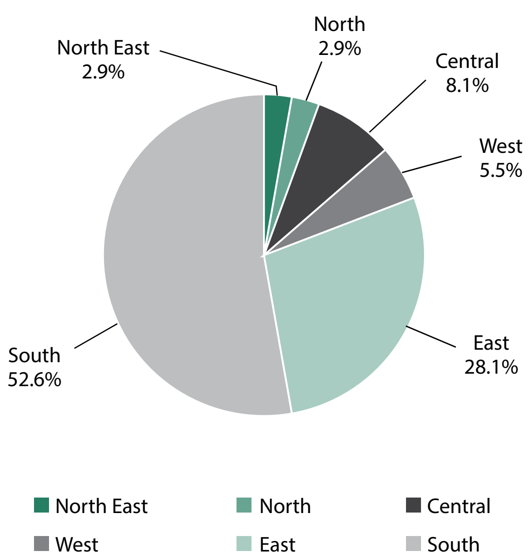
Among the states, Karnataka received nearly 4,00,000 SHG loans during the year but the loan amount was highest in the case of Andhra Pradesh, which received nearly Rs 106.5 billion in SHG loans from banks during 2017–18, followed by Karnataka and Telangana. Other states receiving a substantial number of SHG loans were West Bengal and Bihar. The number of SHGs availing bank loans was lower in the central region, which recorded a decline mainly due to a fall in the number of credit linkages of SHGs in Chhattisgarh and Madhya Pradesh. A telling statistic from NABARD statements is that apart from the southern and eastern states, Maharashtra and Jammu and Kashmir, not even one out of eight savings-linked SHGs in eighteen other states received loans during 2017–18.

There has been a small decline over the previous years in the share of the southern region both in terms of the number of loans and the share in the total loans during 2017–18. This has been the case with the emergence of the eastern region as a destination for SHG loans thereby increasing its share both in terms of the number of loans and the loan amount received. The other regions have not registered any improvement in their position.

Loan outstanding

As per Table 6.1, the number of SHGs with loans outstanding registered a comparatively small increase from 4.47 million to 5.02 million during the three-year period from 31 March 2015 to 31 March 2018. However, the total loan outstanding to SHGs went up by over 50 per cent from Rs 515.46 billion to Rs 755.98 billion while the average loan outstanding has gone up by over 30 per cent to nearly Rs 150,600 per SHG over this period.

The shares of the different regions in the number of SHGs with loans outstanding from banks as of 31 March 2018 and the total amount of loan outstanding are shown in Figure 6.3. Agency-wise state-level particulars are given in Annexure 6.3. As in the case of other parameters, the southern region



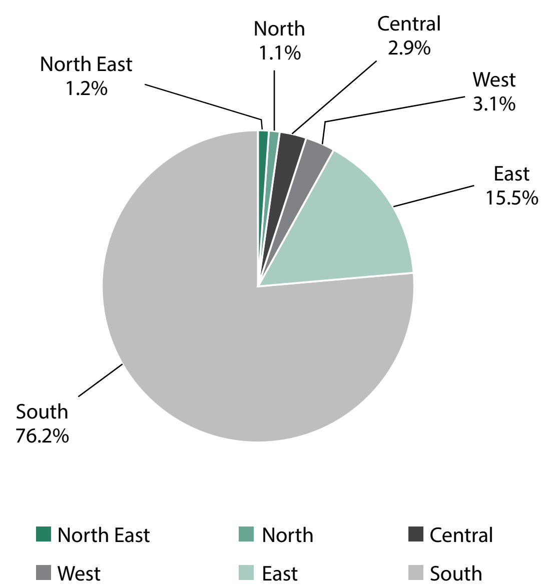


Figure 6.3: Regional Spread of Loan Outstanding to SHGs (Accounts and Amount) as of 31 March 2018

Source: NABARD, Status of *Microfinance in India* 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.

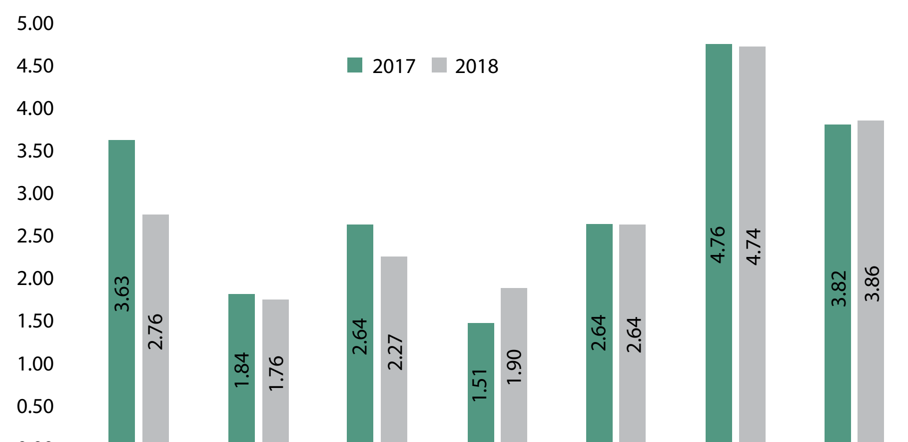
is predominant, accounting for 52.6 per cent of the SHGs with loans outstanding as of 31 March 2018, with the eastern region contributing 28.1 per cent. The share of the central region with over four lakh SHGs, or 8.1 per cent of total SHGs with loans outstanding, is rather high given its share in loans received during 2017–18. The share of the other regions is quite small with barely a quarter of the SHGs in the important western region having loans outstanding as of 31 March 2018. The share of the southern states in the total SHG loan outstanding of Rs 755.98 billion as of 31 March 2018 is still higher at 76.2 per cent. The eastern region's share of 15.5 per cent reflects in part the lower average loan received as compared to the southern states. The remaining four regions of the country, however, account for only 8.3 per cent of the bank loan outstanding to SHGs as of 31 March 2018. Among the states, Andhra Pradesh and Karnataka had over seven lakh SHGs with loans outstanding, while West Bengal had over six lakh SHGs with loans as of 31 March 2018. The loan amount outstanding was highest in the case of Andhra Pradesh at Rs 222.4 billion, followed by Telangana and Karnataka. There was no significant change in the share of loan outstanding of the different regions over the previous year, or indeed, over the past several years.

Credit multiplier

The foregoing tables also provide the overall situation in respect of the extent to which SHGs can leverage loans from the banking system. The credit multiplier, which provides the ratio between the loans outstanding of banks to their savings in the banking system, is illustrated in Figure 6.4. It represents the bankers' confidence in lending to SHGs. There has been no significant change in the credit multiplier between 2017 when it was 3.82 and its level of 3.86 in 2018 in almost all regions. However, it has declined for the country as a whole from 5.5 in 2012 to 4.66 in 2015 to 4.17 in 2016 to its present level of 3.86. The factor responsible for this may be the increased bank savings of SHGs—which was in turn boosted by savings mobilisation within SHGs complemented the resources provided to the SHGs in the form of revolving funds under the NRLM. However, it would appear that the off-take of credit has not kept up with the savings effort. It would also reflect on the inability of SHGs to leverage greater loans from the banking system on the strength of the community funds made available to them. In states where NPAs are a problem, particularly those of the central region, there would be a constraint to repeat lending, which could contribute to the phenomenon of limited off-take of credit.

Performance of Banks in the SBLP

Table 6.4 gives the performance of the various financing agen cies in respect of the SHG-bank linkage programme.



	North Eastern	Northern	Central	Western	Eastern	Southern	All India
2017	3.63	1.84	2.64	1.51	2.64	4.76	3.82
2018	2.76	1.76	2.27	1.90	2.64	4.74	3.86

Figure 6.4: Region-wise Credit Multiplier

Source: Adapted from NABARD, Status of *Microfinance in India* 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.

Table 6.4: Agency-wise Status of SHG-BLP in 2017-18

Category of Agency	Total savings of SHGs with banks as of 31 March 2018		Loans disbursed to SHGs by banks during 2017-18		Total outstanding bank loans against SHGs		NPAs of SHGs	
	No. of SHGs	Savings amount (in Rs lakh)	No. of SHGs	Loans disbursed (in Rs lakh)	No. of SHGs	Loan outstanding (in Rs lakh)	Amount of gross NPA (in Rs lakh)	NPA (in per cent)
Commercial banks	46,33,712	11,66,422	12,72,886	28,70,762	29,04,086	48,74,805	3,10,120	6.36
Share (in per cent)	52.99	59.54	56.29	60.84	57.85	64.48	66	
Regional rural banks	28,07,744	5,80,735	7,82,563	15,11,934	16,58,221	22,73,864	1,21,603	5.35
Share (in per cent)	32.11	29.64	34.61	32.04	33.03	30.08	26.1	
Cooperative banks	13,02,981	2,12,054	2,05,683	3,35,892	4,58,051	4,11,176	31,082	7.56
Share (in per cent)	14.9	10.82	9.1	7.12	9.12	5.44	7.9	
Total	87,44,437	19,59,211	22,61,132	47,18,588	50,20,358	75,59,845	4,62,805	6.12

Source: NABARD, *Status of Microfinance in India* 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.

Considering savings performance, 53 per cent of the SHGs in the country, i.e. about 4.63 million, maintain their savings account with commercial banks as of 31 March 2018. During 2017–18 the share of commercial banks in terms of SHGs with savings linkage increased marginally. Commercial banks accounted for about 60 per cent of the savings outstanding of SHGs with Rs 11,664 crore. Though the total quantum of SHG savings with commercial banks increased by 14 per cent during the year, their share has declined marginally from 63 per cent of the previous year. The number of SHGs maintaining their savings bank account with RRBs was over 2.8 million and during the year 2.2 lakh more SHGs have been savings-linked with RRBs. SHGs of RRBs have savings outstanding of Rs 5,807 crore, i.e. about 30 per cent of the total savings outstanding under SHG-BLP as of 31 March 2018. The share of cooperative banks was relatively limited with 15 per cent of the number of SHGs saving with banks and 11 per cent of savings outstanding. The State Bank of India had the largest SHG savings deposits of Rs 2,490 crore, followed by Andhra Bank of Rs 2,155 crore and Andhra Pradesh Grameena Vikas Bank, a State Bank of India-sponsored RRB, of Rs 1,454 crore.

Commercial banks had the major share in the credit flow to SHGs as well, with disbursement of Rs 28,708 crore (61 per cent of the total disbursement during 2017–18) to 12.73 lakh SHGs. As compared to 2016–17, commercial banks' disbursements were to 14 per cent more SHGs and an 18 per cent higher amount of loan disbursed. In the case of RRBs loan disbursed during the year was an impressive Rs 15,119 crore to 7.83 lakh SHGs—an increase of 40

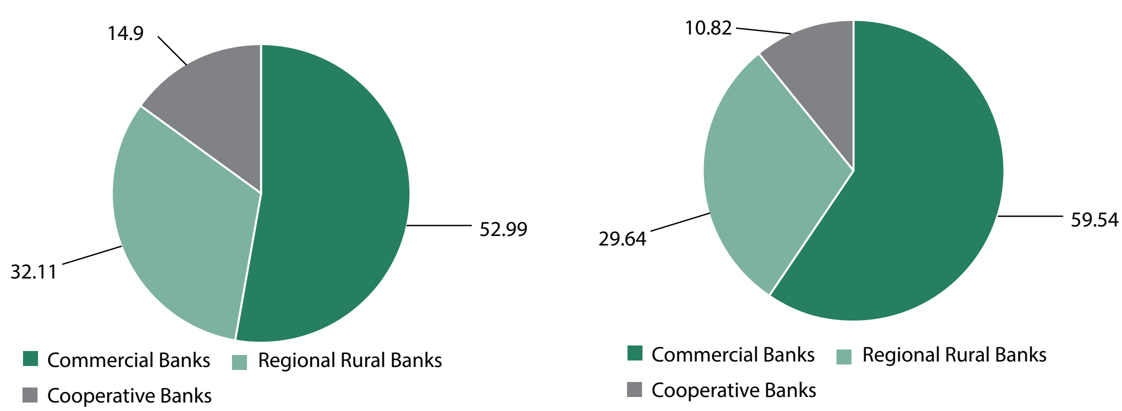
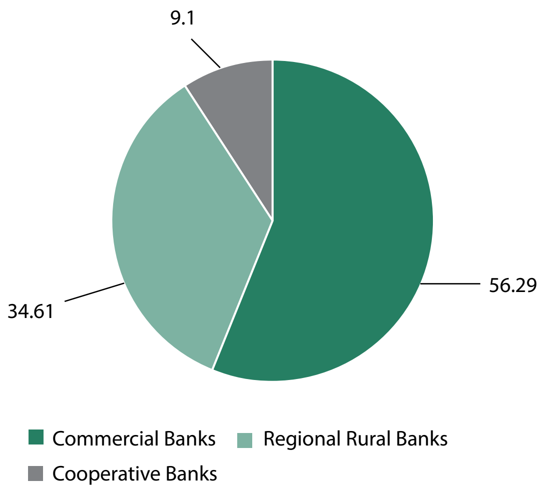


Figure 6.5: SHG Savings by Financing Agency as of 31 March 2018

Source: NABARD, Status of *Microfinance in India* 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.



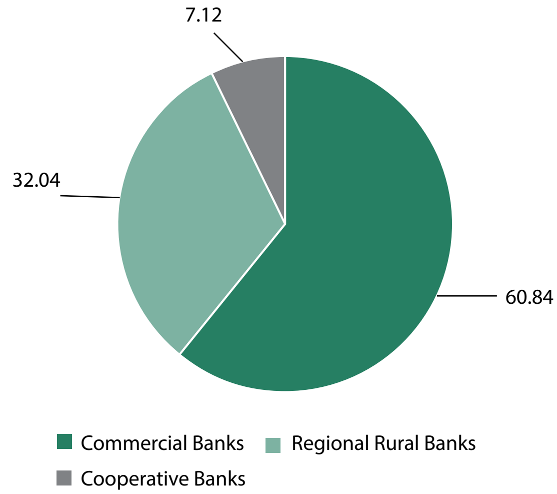


Figure 6.6: Share of Financing Agencies in Disbursement of Loans to SHGs, 2017–18

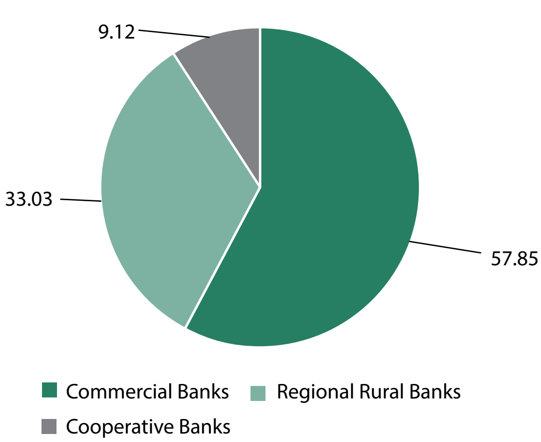
per cent in the number of SHGs and 30 per cent in the quantum of loan disbursement over the previous year. Cooperative banks extended credit of Rs 3,359 crore to 2.06 lakh SHGs, i.e. 8 per cent fewer SHGs as compared to the previous year. However, there was an increase of 17 per cent in the quantum of credit disbursed by cooperatives during the year. In loan disbursements to SHGs as well, it was the State Bank of India that led with Rs 2,490 crore, followed by Andhra Bank with Rs 2,155 crore and Andhra Pradesh Grameena Vikas Bank with Rs 3,641 crore.

Commercial banks had a share of 64.5 per cent of total bank loan outstanding by SHGs as of 31 March 2018 amounting to Rs 48,748 crore to over 2.9 million SHGs. RRBS and cooperative banks had a share of 30 per cent and 5.5 per cent, respectively. Cooperative banks, however, recorded a 34 per cent increase in the average loan outstanding over 31 March 2017 as compared to about 16 per cent in the case of commercial banks and RRBs.

Table 6.5 shows the average, saving, loan disbursement and loan outstanding data for the various agencies for 2018.

Some of the main highlights of the data are:

1. RRBs recorded a significant 47 per cent improvement in their average savings outstanding per SHG during 2017–18.
2. The average loan disbursement per SHG by commercial banks remained the highest during 2017–18, representing a small increase over the previous year. On the other hand, RRBs recorded a fall in the average credit disbursement during the year as compared to the previous year.



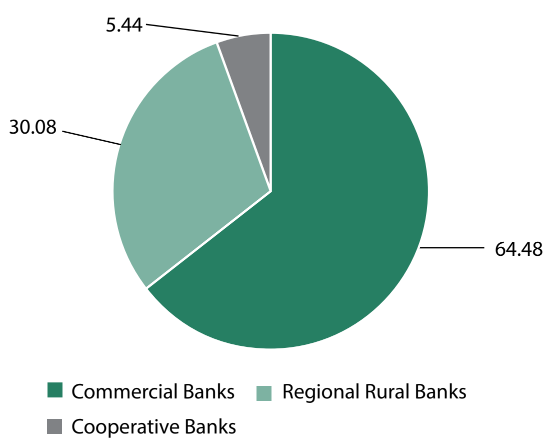


Figure 6.7: Share of Financing Agencies in Loan Outstanding to SHGs as of 31 March 2018

Source: NABARD, Status of *Microfinance in India* 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereadda-ta/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.

Table 6.5: Agency-wise Average Savings, Average Loan Disbursement during the Year and Average Loan Outstanding, 2016–17 and 2017–18

	Average savings of SHGs with banks*			Average loans disbursed to SHGs by banks			Average outstanding bank loans against SHGs*		
	2017–18 (in Rs per SHG)	2016–17 (in Rs per SHG)	Change# (in per cent)	2017–18 (in Rs per SHG)	2016–17 (in Rs per SHG)	Change# (in per cent)	2017–18 (in Rs per SHG)	2016–17 (in Rs per SHG)	Change# (in per cent)
Commercial banks	25,173	22,883	10.01	2,25,532	2,17,629	3.63	1,67,860	1,44,809	15.92
Regional rural banks	20,683	14,042	47.29	1,93,203	2,08,290	–7.24	1,37,127	1,18,621	15.6
Cooperative banks	16,275	14,956	8.81	1,63,306	1,28,097	27.49	89,766	66,996	33.99
Total	22,405	18,788	19.25	2,08,683	2,04,314	2.14	1,50,584	1,27,017	18.55

Notes: #Per cent change in 2017–18 over 2016–17.
*Savings and loan outstanding data pertains to 31 March 2017 and 31 March 2018.
Source: NABARD, Status of Microfinance in India 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.

There was a significant improvement in the average credit disbursement of loans to SHGs by cooperative banks during the year.

3. The average loan outstanding as of 31 March 2018 too remained the highest in the case of commercial banks and the least for cooperative banks, even though the latter registered a significantly greater increase in their loan outstanding than the commercial banks and the RRBs.

Regarding the portfolio quality of bank lending, as recorded in Table 6.4, NPAs of the banks stood at 6.12 per cent as of 31 March 2018, which represents a small decline from the previous year's figure of 6.5 per cent. A fuller discussion of NPAs is carried out in the following section.

NPA LEVELS IN THE SBLP: A DISCUSSION

While the level of NPAs of SHGs may not be higher than in other components of the portfolio of banks, both in terms of the gross amount of NPAs and the NPA ratios, it had contributed to some loss in enthusiasm among banks lending to SHGs. A contributory factor had the promise of loan waivers and politicisation of the SHG movement, which resulted in a decline in repayment ethics among the groups. Besides the recovery, performance under the SGSY had been a major cause for concern. With the NRLM taking a firmer control of SHG development some of these issues could be addressed. The continued policy of interest rate subvention carries with it both incentives for repayment as well as expectations of waiver of loans. It appears, however, that the mature states with larger SHG portfolios perform better than others where the SBLP has not been grounded more firmly.

A summary of the region-wise and agency-wise NPAs in bank lending to SHGs as of 31 March 2018 is provided in Table 6.6. More comprehensive state-wise and bank-type-wise data provided by NABARD is detailed in Annexure 6.4. As noted above, there has been a very slight decline in the ratio of gross NPAs to total loan outstanding when compared to the position as of 31 March 2017, i.e. from 6.5 per cent to 6.12 per cent. Though a favourable development, these numbers do conceal some variations across regions and institutions that require further analysis. The substantial increase in loan outstanding suppresses the fact that gross NPAs of SHGs, which reached Rs 4,628 crore as of 31 March 2018, have actually registered an increase of 15 per cent over the figure for the previous year and are more than 25 per cent higher than gross NPAs as of 31 March 2016.

The share of the southern region, at Rs 2,571 crore, is 56 per cent of gross NPAs of SHGs. However, this constitutes only 4.46 per cent of their outstanding loan, a creditable performance at almost the same level as the previous year. All other regions have NPA ratios in excess of the national average and in some regions the situation is quite alarming. Of the other regions, the eastern region with an NPA percentage of 7.17 per cent performs quite well, even as it has been able to bring down the percentage as compared to the previous year, largely thanks to the contribution of West Bengal. The central region has the highest NPA percentage of 24.7 per cent and represents a further decline over the previous year's figure. In fact, with the exception of Chhattisgarh, all

Table 6.6: Region and Agency-wise NPAs

	Public sector commercial banks		Private sector commercial banks		Regional rural banks		Cooperative banks		Total	
	Gross NPA (in Rs lakh)	NPA as %age of loan out-standing	Gross NPA (in Rs lakh)	NPA as %age of loan out-standing	Gross NPA (in Rs lakh)	NPA as %age of loan out-standing	Gross NPA (in Rs lakh)	NPA as %age of loan out-standing	Gross NPA (in Rs lakh)	NPA as %age of loan out-standing
Central region	22,692	23.52	840	7.09	27,678	26.96	2,183	42.30	53,393	24.70
Eastern region	42,623	9.30	16	0.08	36,450	6.02	4,663	5.54	83,752	7.17
Northeastern region	6,514	18.72	0	1.13	9,707	19.69	1,214	24.69	17,435	19.58
Northern region	9,596	36.50	572	2.60	4,976	22.23	4,072	25.17	19,216	22.12
Southern region	1,95,711	5.21	10,386	3.63	35,060	2.44	15,997	5.67	2,57,154	4.46
Western region	19,814	21.98	1,356	1.87	7,732	13.80	2,952	15.84	31,855	13.43
TOTAL	2,96,949	6.65	13,171	3.19	1,21,603	5.35	31,082	7.56	4,62,805	6.12

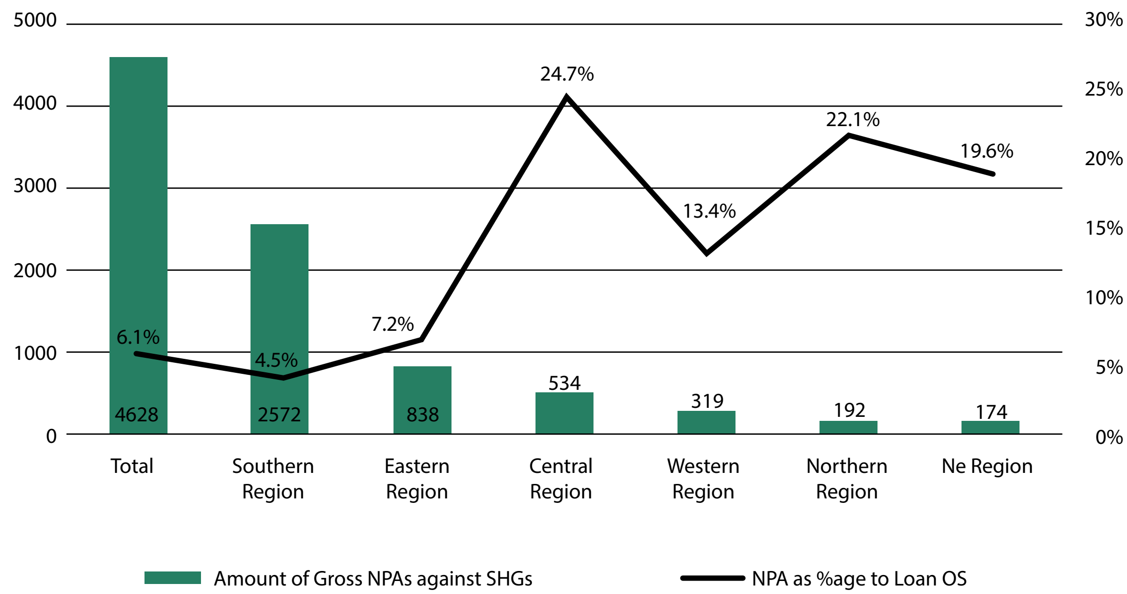


Figure 6.8: Region-wise NPAs (Gross NPAs and NPA Percentage) as of 31 March 2018 (in Rs crore**)**

Source: NABARD, *Status of Microfinance in India* 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.

the central region states have NPAs in the region of 20 per cent and over with Uttar Pradesh accounting for two-thirds of the gross NPAs of the region. Similarly, Rajasthan accounts for over 60 per cent of the NPAs of the northern region. Overall, there is virtually a clear divide between the two main regions with larger SHG portfolios and larger NPAs and the other regions with relatively lower gross NPAs but considerably higher NPA ratios.

With continued dominance of the southern region, and to an extent the eastern region, in bank lending to SHGs it would appear that overall there is a deepening of credit flow to a limited number of SHGs with repeat lending on hold in certain regions. Thus, banks lend to well-established SHGs in the leading states, while holding back in other states and regions where SHG NPAs have built up. In some states where NRLM activity has progressed, disbursements have picked up slightly. According to data put out by NABARD, there does not appear to be much variation in the NPAs of SHGs covered by the NRLM as compared to the overall SHG

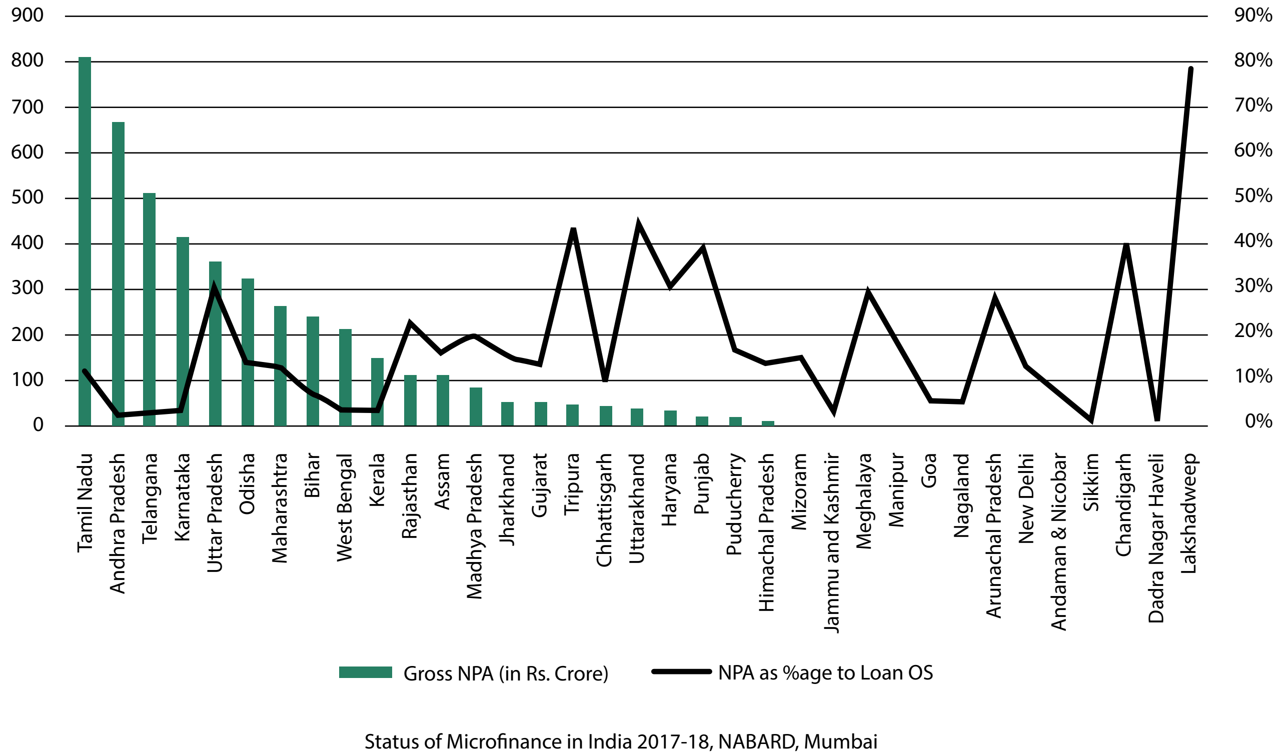


Figure 6.9: State-wise Gross NPAs (Gross and as Percentage of Loan Outstanding) as of 31 March 2018

Source: NABARD, *Status of Microfinance in India* 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.

performance as of 31 March 2018, both in respect of the region and the financing agency. It is only in the case of the small NRLM component of NPAs of private commercial banks that in almost all regions there are substantially higher NPA ratios. This merits further investigation.

The southern states enjoying substantial, even full, interest subvention also have greater incentive for timely repayment, even as they contribute the highest level of gross NPAs. Indeed, though there has been some slight improvement in SHG loan recoveries, the weak performance in the states of the north and northeast regions, which continue to be neglected, needs to be tackled on an urgent basis.

The state-wise NPA performance set against the NPA percentage is given in Figure 6.9. Tamil Nadu is seen to have the highest level of gross NPAs at over Rs 809 crore, followed by Andhra Pradesh and Telangana. Though these three states accounted for 43 per cent of the gross NPAs of the country, they are associated with comparatively much lower NPA ratios than other states with smaller SHG portfolios. Thus of the 10 states with gross NPAs of about Rs 150 crore and more, with the exception of Uttar Pradesh, all have NPA ratios less than 15 per cent, and 5 states have NPA ratios lower than the national average of 6.12 per cent. It would seem that the overall NPA ratio is held down by the states with a large portfolio in SHG-bank linkage, with the other states performing quite unsatisfactorily such as to limit the possibility of their SHGs attracting greater loans from the banking system in the future as well.

As regards the NPAs in the SHG portfolio of the financing agencies, Figure 6.10 illustrates the gross NPA levels and the NPA rates of different types of banks. The overall rate of NPAs to bank loan outstanding to SHGs was 6.12 per cent. Of course, as discussed earlier, the averages conceal the relative performance of the SHG portfolio of the banks in terms of NPAs across regions. While the public sector banks had an NPA ratio of 6.5 per cent it is the RRBs with 5.35 that have registered the best performance among the major financing agencies with the cooperative banks having a somewhat higher ratio of 7.6 per cent. Significantly all categories of banks have reduced their NPA ratios during 2017–18. Out of the total NPA amount of Rs 4,628 crore, commercial banks (public and private) with Rs 3,101 crore (Table 6.4) accounted for two-thirds of gross NPAs of SHGs as of 31 March 2018, a rise of 17 per cent over the previous year. RRBs also registered a rise of 16 per cent in their gross NPA amount of Rs 1,216 crore as of 31 March 2018. Cooperative banks however succeeded in lowering the NPA amount marginally to Rs 310 crore from Rs 316 crore during the year.

Overall, though apparently relatively contained, the national averages in NPA levels and ratios of the SHG portfolio of banks conceal great variations across regions and states. This is also reflected in the constrained growth of the SBLP in the northeastern states as also in some of the larger states of the northern and central region. The underlying issues for this phenomenon will have to be addressed by the NRLM as it expands its operations from the intensive blocks to the wider development of SHGs across the states of the country.

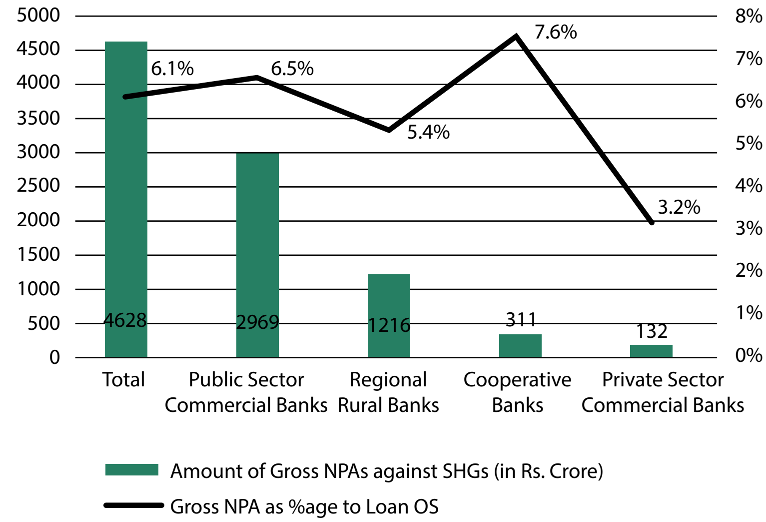


Figure 6.10: NPAs by Financing Agency (Gross NPAs and NPA Percentage) as of 31 March 2018

Source: NABARD, *Status of Microfinance in India* 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.

THE NRLM FACTOR IN INCLUSIVE FINANCE[10]

Making the poor the preferred clients of the banking system is core to the NRLM financial inclusion strategy. Mobilising bank credit is crucial for accomplishing investment goals under the NRLM. Hence, SHG development and the SHG bank linkage programme are central to the implementation of the NRLM.

Progress under the NRLM

During 2017–18, the growth rate of total NRLM SHGs according to NABARD data in Table 6.1 was nearly 12 per cent as against less than 2 per cent for SHGs as a whole, bringing the total savings-linked NRLM groups to 4.18 million. In fact, the NRLM is effectively the custodian of all women SHGs, whether they are covered by it or not. The total number of savings-linked women's groups was 7.39 million out of the total of 8.74 million SHGs as of 31 March 2018 (Table 6.1). Steady progress appears to be made across the various components of the NRLM with as many as 606 districts being covered with 4,998 intensive blocks as of July 2018. As can be seen from Table 6.7, which gives fuller details of progress of the SHG programme under the NRLM as of July 2018, there are substantial funds flowing to SHGs in the form of revolving funds (RF) and community investment funds (CIF).

Table 6.7 reveals the important fact that the cumulative number of new SHGs promoted by SRLMs as of July 2018 was 2.41 million as against 2.46 million other SHGs brought into the NRLM fold. Thus, over half the NRLM SHGs belong to the latter category. These pre-existing SHGs, also described as home-grown SHGs, would bring with them an alternative experience of promotion, processes and federation from within the ranks of NGOs. There would inevitably be significant stresses related to the co-option[11] of these SHGs as they are made to adapt to new systems and styles of functioning and even subjected to reorganisation and restructuring.

Other data shows that as many as 15.5 million SHG members had own savings accounts and about two-thirds of the total SHGs, that is, 3.2 million had been provided with RF support while 0.92 million SHGs had been provided with CIF support. The number of VOs of SHGs (or the first-level SHG federations) that had been formed was 2,67,394 with a membership of 3.37 million SHGs or about 70 per cent of SHG numbers. In addition, 23,122 cluster-level federations (CLFs or secondary-level institutions) had been formed. Hence, the federation of SHGs is still very much a work in progress.

It would appear that there continue to be differences in SHG numbers and other data between the NABARD report and the overall progress reports of the NRLM. Thus Table 6.7 shows the cumulative savings mobilisation at about Rs 164.8 billion by 4.87 million SHGs as of July 2018 (Rs 157.2 billion in respect of 4.66 million SHGs as of 31 March 2018). This compares with savings of Rs 104.3 billion for 4.18 million SHGs as of 31 March 2018 as per Table 6.1. While the difference in the number of SHGs in the two reports is relatively small, the

Table 6.7: Details of Progress of SHG Programme under NRLM, July 2018

Indicators	Annual target 2018–19	Progress till March 2018	Cumulative progress till July 2018
Progress of implementations in intensive blocks (planned/targeted vs covered)			
Number of gram panchayats in which intensive strategy initiated	12,138	1,23,675	1,28,973
Number of villages in which intensive strategy initiated	31,539	3,46,655	3,63,117
Number of new SHGs promoted by the SRLM	2,68,890	22,75,763	24,07,674
Number of other SHGs brought into the NRLM fold (after revival/strengthening)	75,382	23,86,689	24,65,693
Number of SHGs under the NRLM fold in intensive blocks	3,44,272	46,62,452	48,73,367
Number of predominantly SC SHGs (SC member >= 50%)	67,322	9,48,802	9,87,433
Number of predominantly ST SHGs (ST member >= 50%)	53,661	5,87,542	6,27,227
Number of predominantly minority SHGs (minority member >= 50%)	43,542	3,68,985	3,94,829
Number of other SHGs	1,79,747	23,46,823	24,53,578
Number of predominantly SHGs with PWD members (PWD member >= 50%)	1,263	57,585	60,676
Number of elderly SHGs promoted by the SRLM	617	21,516	21,763
Number of SHGs that have become defunct/dormant	43	1,27,855	1,60,100
Number of SHGs in which standard bookkeeping practices introduced	3,50,731	34,89,678	36,18,340
Number of SHGs following Panch Sutras	2,83,012	38,34,045	39,77,533
Number of SHG bookkeepers deployed	2,09,654	15,44,774	16,42,768
Amount of savings mobilised in all SHGs (in Rs million)	3,374	1,57,237	1,64,818
Households mobilised into all SHGs	40,85,836	5,31,76,533	5,54,74,898
Other households mobilised into all SHGs	21,28,831	2,85,48,484	2,96,76,686
Financial inclusion			
Number of SHG members having own savings account	12,34,100	1,42,95,988	1,55,40,145
Members covered under insurance schemes	11,33,423	83,64,650	97,20,131
Number of SHGs covered under financial literacy training	1,17,874	43,867	1,66,787
RF support provided to SHGs			
Number of SHGs provided with RF	3,02,157	30,97,411	31,79,539
Amount of RF provided (in Rs million)	4,420	21,960	23,174
CIF support provided to SHGs			
Number of SHGs provided with CIF	1,34,731	8,74,511	9,23,547
Amount of CIF provided (in Rs million)	8,257	43,978	46,725
Promotion and functioning of primary and secondary level federations			
Number of VOs (first-level SHG federations) formed	20,467	2,57,513	2,67,394
Number of SHGs holding membership in VOs	1,91,300	32,71,593	33,74,676
Number of VOs provided with CIF	8,968	32,729	36,068
Amount of CIF provided to VOs (in Rs million)	851	9,290	10,120
Number of CLFs (second-level SHG federations) formed	1,475	21,578	23,122
Number of CLFs provided with CIF	619	8,833	10,392
Amount of CIF provided to CLFs (in Rs million)	7,071	6,414	6,731

Source: NRLM website. https://nrlm.gov.in/KeyPerformanceIndicatorsAction.do?methodName=showDetail&reqtrack=L1969DuZuLcKJb3CEyRtmxHaj. Accessed on 31 August 2018.

figures for the amount is savings mobilised clearly do not match. This is probably explained by the fact that the NRLM data could pertain to total savings at the SHG level, which would also include grant funds received by them in the form of RF and CIF, while the NABARD data pertains only to SHG savings in the banking system.

A similar situation prevails in respect of the data on credit linkage though the gap appears to be narrowing. According to SHG-bank linkage data provided by the NRLM for this report in August 2018, 2.67 million SHGs had an amount of Rs 440 billion outstanding for 2017–18. The NABARD data from Table 6.1 for loan outstanding to NRLM SHGs as of 31 March 2018 is Rs 382 billion to 2.79 million SHGs.

The NRLM is seized of the problems of data mismatch in SHG numbers and MIS as maintained by NABARD. There are differences between the parameters tracked by eShakti of NABARD and those in the MIS of SLRMs. In the case of the NRLM the data comes directly from the CBS of the bank. There is no manual interpretation. An attempt is being made to have an integrated system that permits seamless transfer of data. This is being piloted in five districts by the Bihar Livelihoods Promotion Society (BRLPS).

NRLM Initiatives in Inclusive Finance

Community-based institutions delivery model

Under the NRLM community-based institutions have to follow certain basic principles like forming federations and financial intermediation. The three-tier system (SHG, VO and CLF) is not mandatory, local customisation has taken place and a state like Mizoram has only two tiers. Odisha has VOs at the gram panchayat level as opposed to other states that have VOs at the village level.[12] Box 6.1 gives a summary of the Odisha Livelihood Mission (OLM) strategy for Financial Inclusion Hubs.

Federations generally work with a corpus of around Rs 2 crore, not just as a fund-sourcing unit but they converge with different departments and schemes. CLFs have not yet moved towards bulk borrowing and lending. This would require higher level of capacity and management. Self-sustainability of these community-based institutions is still a work in progress. There is a systematic approach to tackle three main areas. The first is bookkeeping and accounting at the federation level. The second is management systems. National resource persons have been attached to SRLMs for better guidance

Box 6.1: Financial Inclusion Hubs under Odisha Livelihoods Mission

Under the NRLP (National Rural Livelihoods Promotion Society) funded by World Bank, a dedicated fund has been set up to promote innovations and models under financial inclusion (FI) that can be scaled up under the NRLM. In Odisha, the OLM planned to promote block-level federations (BLFs) as a Financial Inclusion Hub with the support of the above special fund/project. The project is being implemented in all three blocks of Deogarh district covering all the Gram Panchayat Level Federations (GPLFs). The key objective is 'to Facilitate Promotion of Block Level Federation (BLF) as Comprehensive Financial Inclusion Hub'.

The FI hub will work on both demand and supply side actors of the financial inclusion space and fill the gaps to achieve last-mile financial inclusion in the district. It will also function as a financial inclusion resource centre and would gather update information on financial inclusion, government schemes, products, services, etc. and disseminate that to the GPLFs and SHGs. The FI hub will also facilitate customised, integrated result-oriented financial literacy inputs for SHG members, leaders and stakeholders within their operational areas.

The FI hub is designed to be a member-driven organisation of all the GPLFs formed in the block. Operating as an apex-level entity of GPLFs, the FI hub will be owned, managed and governed by the members and that would give it a sustainable institutional footing, mandate and legitimacy to work in the block. All GPLFs functioning in different GPs are members of the FI hub. It is expected that all three FI hubs will get registered soon under the Societies Registration Act, 1860 and would start operating each as an independent legal entity in the block.

Source: As per information provided by Access-Assist Odisha, Bhubaneswar, September 2018.

and handholding support. The third is the human resource at the federation. Managers, accountants and coordinators are being given regular help to develop capacity to run the federation.

There is a focus on revenue generating business for the federation like the Custom Hiring Centre (CHC). The main aim of the CHC is to provide farm equipment to poor or marginal farmers at relatively cheaper rates. There are about 20,000 women involved in CHCs all over the country.

Different federations have taken up work on various social and development issues like women's rights, health and enterprises. SHG women along with the panchayat samiti have been actively involved in the Swachch Bharat Mission (SBM) in Chhattisgarh, Jharkhand, Bihar and Rajasthan. Federations have also taken up new initiatives, like the Gender Justice Centre for gender equality.

SRLMs are directly dealing with different banks for higher SHG lending. Specialised institutions for lending to SHGs and federations is still an idea, even as the requirements of SHG members are changing in terms of the size and purpose of loans. Different products with different terms and conditions have to be identified especially given the absence of a transaction history. In view of this, an expert committee has been set up under G.C. Chaturvedi, former finance secretary, on a special bank for SHGs. The committee will recommend on the relevance and future of these institutions. Four states, namely Rajasthan, Bihar, West Bengal and Tamil Nadu, have had feasibility studies conducted and submitted proposals for similar state-level banks patterned upon the Stree Nidhi of Andhra Pradesh and Telangana. There are a host of considerations before these would be implemented not least the legal form of the proposed bank and the political atmosphere for such an initiative.

Innovations and new directions

The World Bank National Rural Livelihoods Project, a component of the NRLM devoted to developing pilots and proof-of-concept ended in June 2018. It has been cleared for a further period of five years with fortunately 250 million dollars contribution from the World Bank. In the next phase, it is understood the project will be going beyond SHG mobilisation to next generation activities in the financial inclusion space, e.g. digital financial inclusion—how to digitize the transactions of the community between the SHG and SHG members and federations. The project will also focus on microenterprises, by facilitating the graduation to individual enterprise of SHG members who have taken two or three cycles of loans and have a running livelihood activity. The NRLP is looking at partnerships with SIDBI, under MUDRA, on bringing the SHG cohort to that side.

As part of the digitisation initiative, this involves expanding and enabling Bank Sakhis technologically through a fund similar to NABARD's FIF. Also the development of new protocols covering joint accounts of SHGs and federations towards cashless transactions. A module of online loan application-marketplace has been prepared. SHGs supported by a grassroots level facilitation system would be able to put up a loan application on a portal and any bank can download it for lending. This portal is likely to be launched soon.

The next phase of World Bank funding is also likely to focus on SHG federations. This could cover grants, grading of federations, and though bulk financing of federations may not become popular with banks, SHG federations could become sub-BCs of banks and under risk-sharing arrangements. This is considered a useful way of improving access to finance for SHGs, and pilots for these types of partnerships would be undertaken in the upcoming phase. PSBs and RRBs, which have thus far not entered into these types of arrangements, could be involved. One of the SRLMs actively promoting financial federations is BRLPS. Details of its financial inclusion initiatives are given in Box 6.2.

Box 6.2 Financial Inclusion Initiatives of Bihar Livelihoods Promotion Society

The BRLPS operates through a World Bank loan to the state government under the BRLP, now the Bihar Targeted Development Programme (BTDP), and a central government programme, the NRLM. All 38 districts and 534 blocks of the state are now covered. The design of the project targets the poorest of the poor. Major initiatives are on individual savings bank account opening of members, and significant work has also been done on insurance solicitation for subsidised government insurance schemes (i.e. PMJJY and PMJSY). As a result, a market is being created for different kinds of financial services through a certain amount of subsidy. By July 2018, 7,00,000 SHG members will be covered by these schemes. Around 1.96 lakh SHGs have been credit-linked with loans outstanding of approximately Rs 2,500 crore.

The response of most banks to SHG-bank linkage is largely positive.

Around 1.8 lakh groups have received RF and 13,000 VOs CIF of Rs 30,000 to Rs 50,000. The target is to have 10 lakh SHGs and around 8.2 lakh SHGs have already been formed. Civil society involvement in the project is limited to technical partnerships for federations and producer cooperatives. There is no representation of BRLPS on the board of SHG federations promoted by it. It only provides technical support. The BRLPS too is working towards federations as financial intermediaries. The older CLFs that are 5–6 years old have transacted Rs 100 crore thus far. (The operations of an active CLF in Muzaffarpur district are documented in Annexure 6.5.) Rating tools are being developed for federation capacity, management of CIF, etc. It is felt that loans can be a conduit not only for entrepreneurship, but also for housing, education and a range of other purposes. The SRLM strongly believes in financial intermediation through CLFs. The question is how to formalise it, what loan products, etc., should be available at each level.

SHGs are serving to strengthen the social infrastructure and they have contributed in a major way towards prohibition, sanitation and have had a major impact on the flood situation. The State Women's Development Corporation is collaborating under the Priyadarshini project, which is working on social issues. SHGs have also been at the forefront in the implementation of the PMJDY and the APY. SHGs are the only institution in rural areas that can be used as a development channel, after many other development channels have failed. Through the NRLM, SHGs, PRIs, MGNREGA and other programmes are beginning to function in an integrated manner. The Government of Jharkhand under the MGNREGS-NRLM Cluster Facilitation Team (CFT) strategy issued a state directive to appoint 100 per cent SHG mates in CFT blocks—wherein MGNREGS mates (worksite supervisors) were to be selected from among SHG members.

Source: Mukesh Chandra Sharan, Project Manager, Finance, BRLPS, discussions with author, Patna, June 2018.

Issues and Challenges for the NRLM Model

The NRLM has mushroomed into a mega programme with many verticals and activities. The many accomplishments in each sector are impossible to document and concerns remain about the basic building block, namely SHGs. One of the main questions is whether the quality of SHGs is being maintained and their capacity for undertaking such a wide range of activities has been adequately developed.[13] At one level ground reports about SHG functioning are not always encouraging. Are timely meetings, high degree of participation and discussion, collective functioning, solidarity and integration of activities ensuring continuity and sustainability of the groups? Have the SRLM been able to enthuse both the co-opted SHGs and the newly formed ones with what is essentially a top-down approach driven by targets and procedure and regimented functions?[14] Does the project management unit offer an effective alternative to experienced SHPI processes? Are capacities for financial intermediation being adequately developed, or are energies being widely dissipated on a large number of state-mandated target-driven activities?

While financial inclusion is taking place under the NRLM, some of the old issues continue to persist, e.g., problems in the opening of SHG accounts. One view suggests that there is supply-driven lending to SHGs in states like Andhra Pradesh and Telangana with interest subvention under the NRLM which has sent up the budgetary requirement for interest subvention into thousands of crores. NPAs are mounting in certain states as PSUs are given targets for lending by the NRLM which is being monitored through the CBS.

Another perspective suggests that the NRLM provides a very costly framework to work with, especially as the SRLM staff in certain states seeks to be regularised. This highlights problems of running a long-term programme in project mode. Others point to the return of malpractices of an earlier generation of subsidy-based lending.

An alternative critique sees the NRLM as an elephant in the room that is not adequately responsive to community needs and that serves to crowd out NGO initiatives and the space for civil society. There is an assertion that the narrative has changed from women taking charge to the government pushing the women to take up the developmental agenda. The SHG programme is now a top-driven programme regulated entirely by the state and the NRLM. Existing SHGs have been co-opted such that their original promoters cannot carry out activities of their choice in these SHGs.[15] Some of the SRLMs have taken the services of their NGO partners. In Jharkhand the SRLM paid the HR cost of civil society organisations for four years, which has ensured smooth operations. However, in other states the facility has been systematically withdrawn.

At the group level, many practices such as weekly meetings and the introduction of 17 books for bookkeeping are found to be onerous and difficult to observe according to feedback received from the clusters and SHGs in Rajasthan and Bihar. Community resource persons (CRPs), however, have an incentive in the form of remuneration for various activities even though they are being required to restart the group federation process. The overall objective seems to be to displace NGOs and introduce new structures. While the situation varies from state to state, SHGs are generally looked at as a medium for last-mile delivery and are pressurised and burdened with facilitating the smooth operation of markets.[16]

In conclusion, the various activities of the NRLM and their convergence with other programmes[17] have meant that members of women's SHGs and SHG-based community organisations have received opportunities to both assume community leadership roles and in some cases access paid, semi-skilled, local work opportunities or to undertake land development works. However, there remain aspects that need further examination—whether outsourcing responsibility of implementation of government programmes to women SHG collectives enables community ownership or whether it instrumentalises women's labour, holding them accountable for 'delivering' entitlements in exchange for task or performance-based remuneration; and what have been the repercussions on women's time and work burden with these increased responsibilities, adding to unpaid work that remains disproportionately conducted by women.[18]

NABARD SUPPORT FOR THE PROMOTION OF SHGs AND RELATED INITIATIVES[19]

NABARD provided refinance to banks to the extent of Rs 698 crore during 2017–18. Cumulative refinance over the years has amounted to Rs 50,275 crore. Apart from this, NABARD's Financial Inclusion Fund and Women Self-Help Group Development Fund were utilised during the year 2017–18 for various microfinance related activities such as formation and linkage of SHGs/JLGs through SHPIs/JLGPIs, training and capacity building of stakeholders, livelihood promotion, studies, documentation, awareness and innovations. A sum of Rs 72.10 crore was expended during 2017–18 from these funds for the above purposes, representing an increase of 15.01 per cent over the previous year.

Grant Support to Partner Agencies for SHG Promotion

NABARD extended grant support to NGOs, federations of SHGs, RRBs, NGO-MFIs, DCCBs, PACS, Farmers' Clubs and Individual Rural Volunteers (IRVs) for promotion, nurturing and credit linkage of SHGs with banks. A sum of Rs 27.37 crore was sanctioned for this purpose for promoting 28,745 SHGs to various SHPIs during 2017–18. However, releases for this purpose during the year were only Rs 16.21 crore with 39,232 SHGs savings-linked. The cumulative sanctions up to 31 March 2018 have been 387.95 crore covering 8,38,918 SHGs. Out of this, the releases or utilisation has been only Rs 143.2 crore with 60,10,920 SHGs savings-linked. Notwithstanding the leading role of NABARD in SHG promotion and bank linkage, and its many other contributions towards financial inclusion, this represents a very modest contribution. Thus NABARD support has been provided for less than 7 per cent of the 8.74 million SHGs savings-linked as of 31 March 2018.

Women SHG (WSHG) Scheme in Left-Wing Extremism (LWE) Affected and Backward Districts

Under this scheme, which is being implemented in association with the central government in 150 districts of 28 states, anchor NGOs received Rs 20.72 crore during 2017–18 with 3,930 SHGs savings-linked to banks and a cumulative amount of Rs 91.7 crore covering 2,04,628 SHGs savings-linked to banks. As of 31 March 2018, 2.05 lakh WSHGs had been savings-linked and 1.20 lakh WSHGs credit-linked.

Village-Level Programmes (VLPs)

With a view to foster better understanding of mutual requirements between banks, SHGs and SHPIs, and to sort out issues like credit linkage, repayment etc. at the ground level, VLPs are being conducted with the support of banks and the NRLM. NABARD-sponsored VLPs led to increased credit flow and appreciation of each other's needs by the various parties. During 2017–18, NABARD supported more than 30,011 VLPs with a sum of more than Rs 4.64 crore covering 8,55,713 beneficiaries.

Joint Liability Groups (JLGs)

An offshoot of the SBLP, the JLG scheme of financing, targeted at mid-segment clients among the poor, leverages on social collateral offered by the members. This counterpart to the SBLP is not mainly aimed at women groups but to groups that do not have easy access to credit, e.g. tenant farmers. The scheme has also recorded an impressive growth during 2017–18 with 10.19 lakh JLGs receiving loans of Rs 13,955 crore from various banks as against 7.02 lakh JLGs and receiving loans of Rs 9,511 crore a year earlier. Since RRBs have a huge rural network, NABARD has encouraged them to finance JLGs in a big way and has entered into MOUs with 36 RRBs and the State Bank of India in 19 states during 2017–18. Under this scheme, NABARD provides grant assistance to banks for using a corporate BC/NGO as a JLG Promoting Institution (JLGPI) and for capacity building to create a pool of trainers out of bank staff for the formation, nurturing and financing of new JLGs. Promotion of JLGs by RRBs through the BC network is another intervention which would give momentum to the Joint Liability Group Bank Linkage Programme. NABARD has provided over Rs 170 crore of assistance to JLGPIs for the promotion of JLGs. The progress and challenges to the business model involving financial inclusion of JLGs through RRBs in Odisha are given in Annexure 6.6.

Livelihood Interventions for SHGs

NABARD continued with its Microenterprise Development Programme (MEDP) to nurture the entrepreneurial talents of members of mature SHGs to set up and run microenterprises. Around 16,406 skill upgradation training programmes have been conducted under this initiative covering about 4.68 lakh members of matured SHGs up to 31 March 2018. NABARD mainstreamed the Livelihood and Enterprise Development Programme (LEDP) with a view to creating sustainable livelihoods among SHG members through skill upgradation. The LEDP targets SHG clusters in contiguous villages involved in farm and off-farm activities and supports intensive skill building, refresher training, backward-forward linkages, value chain management, end-to-end solutions, handholding and escort services over two credit cycles. During 2017–18, 2,620 SHG members were provided skill and entrepreneurship training for setting up livelihood units through 185 LEDP programmes. Cumulatively, 15,382 SHG members have been supported through 324 LEDP programmes with a grant sanction of Rs 1,507 lakh from NABARD up to 31 March 2018.

Finally, NABARD has called for redefining the priorities and strategy for underserved states with particular emphasis on central, eastern and northeastern regions of India by mapping the potential for SHG promotion. Potential SHGs could be encouraged to graduate as members of producers' organisations for farm and non-farm activities. NABARD has also called for scaling up alternative delivery channels such as that of NABFINS (discussed in Chapter 3) for timely credit to SHGs at a reasonable cost.

MAINSTREAMING SHGs: DIGITISATION AND MIS ISSUES

Following the report of the Aditya Puri Committee to recommend the data format for furnishing of credit information to credit information companies, the Reserve Bank of India in 2016 set out the structure of the credit information in respect of SHG members to be collected and reported by banks to Credit Information Companies (CICs).[20] CICs were required to share credit information relating to SHGs or SHG members on an aggregate basis with government agencies, NABARD, banks and MFIs for the purpose of credit planning and research and also with other parties for the purpose of undertaking research that could potentially benefit the SHG segment. Aggregate information is to be shared in a manner that is non-discriminatory and respects the confidentiality of individual SHG groups and SHG members as per the relevant laws of the country.

It is at present not clear how many banks are complying with these requirements and the future course of action of the RBI. It is understood that the International Finance Corporation has done a gap analysis study for the NRLM to ascertain the data points required by the RBI vis-à-vis what banks are able to collect to see where the gaps are. The exercise has been done for a commercial bank and an RRB. The challenge is how to get this data from the field for banks, and to what extent this will be used and applied and how many banks are interested in this since for them this is additional work. While the NRLM should be able to take this forward, a challenge is that the members taking loans from bank linkages do not know where the money has come from, especially in view of the other external funds also being provided by the NRLM. Under the NRLM about 80 per cent of the SHG members have individual JDY accounts seeded with Aadhaar and individual KYC information, which can contribute to digitisation and a transaction trail. So they are well placed to meet the RBI's individual member information requirements.

In March 2015 NABARD launched a pilot project for digitising the social and financial data of SHGs titled eShakti to bring SHGs to the technology platform, facilitate wider access to financial services and enable online monitoring of SHGs. Owing to the enthusiasm and interest generated amongst all the stakeholders in its subsequent implementation, the project now covers 100 districts in 22 states and 1 union territory of India and is expected to digitise 4.5 lakh SHGs benefiting around 5.4 million rural poor. NABARD is in the process of gradually expanding the coverage of eShakti. The project is expected to increase credit linkage as well as credit deepening for deserving SHGs in rural areas as also help banks in building up their SHG business portfolio. The 'one-click availability of social and financial related information' of tens of millions of rural families across India on a single platform will help to make available financial and public welfare schemes to the rural poor, owing to its pan-rural India reach and impact. Scaling up the project to cover the remaining districts, however, remains a challenge. Many banks are also sceptical and not using the eShakti software.

According to NABARD, the convergence of the SHG-BLP with financial inclusion initiatives of the government and the RBI in the form of the JAM trinity is seen as an imperative for which the credit history of all SHG members needs to be created. This will ensure credit discipline and facilitate banks to achieve higher off-take of credit to SHGs. Details of eShakti are given in Table 6.8. As of 15 June 2018 3,88,925 SHGs had been digitised covering 4,391,847 members in 58,006 villages. Over 79 per cent of the SHG members have been provided with individual accounts. While a good start it still only covers less than 5 per cent of SHGs saving with banks and less than 10 per cent of the villages in the country.

It is expected that the scale of SBLP operations will double upon the completion of the eShakti project. For banks the cost of maintenance and monitoring of SHG loan accounts will decrease and with increased SHG savings, the volume and quality of SHG loans will also increase. The only concern is that it is limited to SHG transactions, and not looking at federations as a sustainable entity in the long run.

While the initial funding of the pilot was being met by NABARD, there will be a huge fund requirement for scaling this pilot from the present level to the 87 lakh SHGs across the country. Since banks would be the major beneficiaries of eShakti by accessing quality data for sanctioning loans, disbursement and monitoring, appropriate cost sharing mechanism with bankers is another way of sustaining the eShakti project. Other government

Table 6.8: Progress of Digitisation in the Identified 100 Districts under NABARD's eShakti as of 15 June 2018

		Amount (Rs crore.)	
Partner SHPIs	306	Cumulative savings by SHGs	1635.17
SHG digitised	38,8925	O/S member loan (from savings)	923.65
Villages covered	58,006		
Total SHG members	43,91,847	Bank loan availed	4,220.41
Total BPL members	22,33,906	Bank loan outstanding	3,371.47
Number of literate members	31,79,588	Other loan availed	267.74
Individuals having SB account	34,73,957	Other loan outstanding	216.43
Bank branch involved	10,642	Cash in hand	376.58
Commercial bank	6,667	Bank balance	688.55
RRBs	2,174	No. of SHGs credit-linked	2,06,785
SCBs	171		
DCCBs	1,630		

Source: NABARD, *Status of Microfinance in India* 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.

and private players can also be charged for sharing the valuable data available on the platform for making policy and business-related decisions. SRLMs have also been involved as implementing agencies for eShakti in several states and they are supporting the digitisation project in many states. The sustainability of the project depends on the SHGs realising the importance of this software platform for maintaining their books of accounts, obtaining financial support from the banking system and other social benefits. It is felt that if banks owning the software make it available to SHGs and their federation for management and monitoring, then it would be the ideal situation for credit discipline.

An alternative view from the field notes that in the emerging scenario private banks are coming through to show that SHGs are bankable. However, they want individual-level documentation, which goes against the spirit of SHGs and empowering the poor, and is more of a business proposition. Similarly, the credit bureaus are intended essentially to make credit available and promote business; but the need is to educate borrowers and to bring about greater financial literacy towards proper use of credit. Thus the proposed MIS is not empowering to the community, but directed at reporting to the promoters. It does not help SHGs to analyse the performance of their own institutions but is tied to the performance appraisal requirement of lenders.

The MIS of the NRLM is not aligned to the eShakti framework. There is a transaction MIS sheet through which the NRLM monitors all the data. The infrastructure for this is being created in the villages, with a desktop and internet connection at the federations and with trained data entry operators. The NRLM vouches for the data of all its SHGs. However, information asymmetry is a big challenge. There is a big discrepancy in the information given by bankers and the NRLM staff/SHG women. There is still work to be done on the MIS at the NRLM. Based on an initiative first undertaken by the Society for the Elimination of Rural Poverty (SERP) the NRLM developed a website for retrieving this data directly from banks and has made it mandatory

Box 6.3: Brief Findings of the IFMR-LEAD Study on Technology and Digitisation of SHGs

IFMR recently conducted a study on digitization and the use of technology in SHGs in India.[21] The study undertook a rapid landscaping of the current use of digital technology in groups and federations. The study looked across self-help promoter agencies, technology solution providers and policy-making bodies. In terms of MIS management, out of a total of 10 programs, only 2 programs incorporate digital data collection at the ground level, and innovations across MIS features is extremely limited. A majority of these 10 programs have taken nascent steps toward developing various innovations for application within their program; these innovations include efforts such as digitising the payment ecosystem, leveraging SHG members as business correspondent agents, accessing member entitlement and benefits information through an online platform, and incorporating WhatsApp for information dissemination. However, current scale and penetration of these initiatives remains low and there is tremendous scope for growth.

The findings suggest a number of nascent areas in which further digitization can help in achieving the goals of financial support and social mobilization, set at the outset of the SHG movement.

Whilst assessing the benefits of digitization, the study found program level efficiency gains in data load, bandwidth and time taken for approvals/ sanctions, increased data accuracy and reliability and better allocations of human and financial resources. Looking toward larger gains, programs are using the digitised data generated toward performance grading, facilitating resource allocation, assessing financial health of SHGs and building feedback loops and planning. Programs currently place a great deal of focus on building operational efficiencies through digitisation of MIS management and facilitating credit linkages, whilst end-users are yet to reap the benefits at an individual-level. Overall, the study concludes that advocacy and discussions are required around the sustainability and viability of current approaches to digitization; there is low community level ownership, approaches to partnerships depend on vision and capacity and financial sustainability beyond grant-funding is uncertain.

Source: 'Technology for and with SHGs in India Today: A Rapid Landscaping', a study conducted by the financial inclusion team at the IFMR-LEAD (Institute for Financial Management and Research-Leveraging Evidence for Access and Development.)

for all banks to update their bank linkages on the NRLM bank linkage portal. There are also plans for loan applications to be moved online completely for error-free applications and easy tracking of the application. This would decrease the discrepancy in information as well. These applications can also be made available in the market for other banks to lend money to any SHG in the country. Bankers also have a problem with the authenticity of the data of SHGs promoted through other agencies. It is felt that it is essential to have a single point data collection with interface and a two-way exchange between the NRLM and NABARD data. It is also desirable that for the confidence of bankers the NRLM and NABARD join hands and synergise their operations. In this connection, the findings of a study by the Institute for Financial Management and Research (IFMR), summarised in Box 6.3, would also point to areas requiring attention.

NEW CHANNELS OF SHG-BANK LINKAGE AND THE 'DISINTERMEDIATION' OF SHGs[22]

While there are a variety of group formations like SHGs having varied objectives, the defining feature of the SBLP was a role for SHGs in financial intermediation. When the SBLP was still in its infancy, Harper et al. (1998) described, even celebrated, 'the new middlewomen' of Indian SHGs as profitable on-lending groups which collect their own equity capital, and savings deposits, from their owners, who are also the members and the customers, they lend out their money to the members, at interest rates which they decide, and they accumulate profits which they choose either to distribute to the owners, or to add to the fund at their joint disposal.[23] SHGs were thus effectively a micro-bank that would raise equity and deposits, as well as external funds, and on-lend them. It is instructive to examine how the SBLP has moved in the last 25 years, particularly the role of SHGs in respect of its financial intermediation function.

SHG Intermediation Models

The SBLP began with two forms of SHG linkage: (i) direct with bank and (ii) indirect linkage, or bulk lending, through an NGO intermediary. The latter soon became unpopular in view of the NGO's reluctance and lack of an appropriate legal form to involve itself in financial functions that concerned, among things, coercion in the recovery of SHG loans. In view of the challenges faced in directly linking SHGs to banks, leading NGOs promoted non-profit companies and for-profit companies as MFIs to ensure the flow of credit to SHGs promoted by them.

Further, to draw upon the strengths of the network of SHGs as well as provide the numbers and bulk necessary for engagement in financial and non-financial markets the SHG federation became central to the SHG model, particularly when state involvement in SHG promotion came about. The unbifurcated Andhra Pradesh implemented the three-tier federation structure, namely SHG–VO–Mandal Samakhya. With CIFs being moved to Stree Nidhi, the apex institution sponsored by the state government, the VO became the main point of loan disbursement, with the Mandal Samakhya only a routing entity. Similar federation structures have come up all over the country. However, they have been able to attract bulk borrowing from banks and other wholesalers only to a limited extent.

In the latest round of innovation around intermediation in the SHG channel, banks have deployed NGOs, MFIs or federations as BC and BF intermediaries through outsourcing certain functions. The main channels for the flow of financial resources to SHGs that have emerged from the original bank linkage model are briefly set out in Table 6.9.

Diminished Role and Viability of SHGs

An outcome of these varied lending channels, along with applicable interest subsidies and subventions, is that loans to SHGs are available in different contexts at interest rates that range from nil to more than 26 per cent. The institutional innovations and concomitant structure of intermediation margins has had important implications for the financial roles and margins of the SHGs in on-lending to their members and indeed their own internal dynamics. Without placing a value judgment on it, the range of interventions have almost invariably resulted in the diminishing of the role or margin available to SHGs or their effective 'disintermediation.'

Direct bank linkage

The SHG-bank linkage model provides the cheapest and most direct source of funds to SHGs where available. It also allows SHGs a reasonable margin towards profitable functioning. However, not all SHGs are able to access funds from banks to the desired extent.

Further, in certain states and under the NRLM where interest subvention make available loans effectively at low or zero interest through subsidised

Table 6.9: Financial Intermediaries in Lending to SHGs by Banks

Model of financial intermediation	Method of provision of loans to SHG	Example/remarks
1. Direct linkage of SHPA-promoted SHGs with banks through the SBLP	(a) Term loan or credit limit from branches of PSBs, RRBs, cooperative banks and private banks (b) Direct linkage with the SHG by bank with fee-based incentives to the SHPA	Standard bank linkage: SHGs (Low cost but no support from bank for NGO/SHPA promoter) (a) ICICI Bank NGO partners*
2. SHG lending through SHPA-promoted MFIs	Retailing of loans from banks and other financial institutions by in-house MFI of NGOs	(a) Not-for-profit (b) NBFC-MFI
3. BC/BF models	(a) NGO/SHPA acts as agent for bank's loans through the NBFC (b) Govt-promoted institution with the SHG federation as shareholder acts as CBC (c) NGO/SHG federation as BF (d) NGO-MFI acts as BC of bank for SHG/JLG lending (e) NGO acts as BC/BF for PSBs	NABFINS B&D C model (no guarantees or margin money requirement as with MFI as BC) Stree Nidhi (high-tech low-cost model with VOs as CSPs) (a) ICICI Bank-CMRC fee-based lending model (MAVIM) (b) WSHG programme in LWE districts (grants and service charges to anchor NGOs) Private bank partners sharing risk through First Loss Default Guarantee (FLDG) SKDRDP (range of financial services offered)
Financial federations as MFIs	(a) Bank loan on-lent by federations to SHGs (b) Multi-tier SHG structure with state-level cooperative financial federation	Chaitanya/GMSS federation (SHPA acts as guarantor) Stree Nidhi–(Mandal Samakhya)– VO–SHGs

* While ICICI Bank refers to the SBLP, this could also be described as a BF relationship similar to the case of MAVIM-CMRC (Also discussed in Chapter 3).

funds the SHGs' own savings and internal rotation of funds at higher rates of interest are affected. SHGs are understood to have limited the build-up of their savings for intermediation and are inclined to distribute their accumulated corpus at frequent intervals. This brings into question the fundamental role of SHGs as micro-banks, intermediating own and borrowed funds on a long-term and sustainable basis. Instead, their position becomes one of user groups, essentially in existence for channelling government loans and other development services from government agencies. An outcome of this phenomenon is the equal sharing of bank loans by all SHG members. Loans thus become entitlements with members with smaller loan requirements on-lending either to other members or outside the SHG.

Under the direct bank linkage model, there is no margin available to SHGs. A study of 2,000 SHGs done by APMAS in Karimnagar district[24] showed that 31 per cent of SHGs were operating at a loss. With interest subvention and the back-ended subsidy, the loan instalment fixed by the bank is repaid through respective individual contributions or SHG funds. The interest subvention that is subsequently received is adjusted by the bank against future instalments that are payable. As a result, there is no margin for SHGs, except on the limited savings with their own funds—which are being rotated internally—since banks too are demanding deposits from SHGs. Banks insist on deposits of Rs 50,000 to Rs 75,000 from SHGs for loans greater than Rs 3 lakh.

The ICICI Bank provides an example of a modified form of bank-SHPI partnership wherein the SHPI is provided with a fee as incentive for its role in loan origination and assistance with recovery. SHG funding is seven years old now. New group formation is through SHPIs. SHPIs promote and introduce the SHG to the bank and thereafter the bank staff takes over the appraisal functions. Tablet-based services are provided—a feature of which is quick time sanction and access to a larger range of services. This ensures sustainability of SHGs by contributing to the SHPI's maintenance expenses, unlike the original SBLP where SHPIs were not remunerated for these functions. Besides, a dedicated team from the bank for SHGs is responsible for this channel. Though the banks' lending rate to the SHGs is a little higher than under the original bank model, this has the potential to be a more viable and efficient model than linkage through bank branch where the manager attends to the SHG channel along with her other functions and portfolios. Details are provided in Box 6.4.

Box 6.4: ICICI Bank-SHG Bank Linkage Model

The ICICI Bank lending to SHGs is at a mean rate of 15.1 per cent with an incentive to SHPIs of 1.5 per cent of collections facilitated by them. This is effectively a business facilitator model. In the case of MAVIM, CMRCs act like SHPIs and for Tamil Nadu Women Development Corporation SHGs, the Panchayat-level Federations (PLFs) are like SHPIs. Similar arrangements are undertaken with PLFs, Rajeevika in Rajasthan and Maharashtra State Rural Livelihoods Mission (MSRLM). The SHG portfolio is Rs 2,000 crore. The ICICI Bank portfolio in the eastern states is expanding. SHGs will remain an important part of the ICICI Bank strategy. However, there are concerns about the quality of the SHG portfolio in category I districts where lending is to be undertaken at 7 per cent per annum with an interest subvention element. This vitiates the recovery climate. Also, with the insistence of cash credit limits, groups are only paying interest and extending the loan.

Source: Chattanathan Devarajan and Anjali Mahajan, interview by author, June 2018.

In-house NGO-MFI intermediary

A common feature in all these models and innovations involving NGO-MFI or in-house 'not-for-profit' or 'for-profit' entities is that the role of the SHG as financial intermediary is effectively eliminated. Loans to SHGs financed from borrowed funds leave little or no margin for SHGs and are invariably passed on to members at the same rate. This creates a dependency relationship with the promoting NGO for SHGs. Besides, in view of the relatively high cost of borrowing of the MFI and its operating expenses, loans to SHGs may be made at high rates going up to the maximum permissible 24–26 per cent per annum. SHGs, however, may continue to intermediate own funds and funds directly borrowed from local banks under the SBLP unless such access is specifically disallowed or discouraged by the promoters. However, in some cases SHGs are not allowed to withdraw savings from banks. The savings deposit of SHGs in banks acts as some sort of security to obtain loans from the MFI. In some instances JLGS have been formed out of SHGs for delivery of doorstep services. The overall effect of such developments and practices was that though SHGs continued to function their role in financial intermediation was seriously curtailed and undermined.

8.2.3 Federation models

While the federation provides a much-needed supplementary source of loans for SHGs in addition to the SBLP, the margin of SHGs is similarly reduced because of the additional layer of financial intermediaries. Where federations of SHGs have been formed, the role of the SHG as a micro-bank is taken over by the VO or Mutually Aided Cooperative Society (MACS). The SHG becomes a facilitating institution rather than a fund manager, which is potentially disempowering. Second, MACS does not overcome the SHG weakness of low degree of capitalisation and low mobilisation of external funds, while at the same time it does not generally have the required capacity apart from being susceptible to political influences. For some experts, these are sufficient grounds to reject the financial federation model. As such MACS cannot be considered a substitute for direct bank linkage but only a supplementary source of loans for the SHGs. The role of federations continues to be a contested one that places the NRLM and NABARD in different camps.

Chaitanya-Grameen Mahila Swayamsiddha Sangh (GMSS) is an old and rare case of a federation successfully operating as a BC and providing financial services to its constituent SHGs. However, even in this case the role of GMSS in financial intermediation is made possible by Chaitanya acting as the guarantor.

BC models

The BC model wherein an MFI partners with a bank can also be used to lend to SHGs. It is mainly the private banks that have employed this model with Yes Bank's YES LEAP being the prominent one but also favoured by IndusInd Bank and Axis Bank. The partner NGO/MFI is invariably required to participate in risk sharing through the First Loss Default Guarantee. A generous spread of 6 to 10 per cent can be made available to the partner by the bank since the lending rate to the SHG can go up to the maximum stipulated by the Malegaon Committee. This could be 24 per cent or so. This has obvious implications for the SHG, which again finds its own intermediation margin squeezed. In any event, it is understood that for this channel, as in the case of NABFINS and some MFIs, lending to JLGs is emerging as the preferred option. Despite the potential of the risk-sharing model and the available spread, PSBs have thus far not entered this space, though the SBI has recently advertised for BC partners.

In the case of Sri Kshetra Dharmasthala Rural Development Project (SKDRDP), the SHGs it caters to are understood not to have an intermediation role. They are also obliged to save with banks. Decisions on any matter related to loans including rate of interest are taken in consultation with federations. Thus even in the case of the more credible of institutions, there is a dependency situation rather than empowered SHGs operating with much freedom.

Specialised institutions

NABFINS and Stree Nidhi are specialised institutions created to facilitate additional needs-based lending to SHGs. Working on thin margins they have been able to lend at a reasonable rate of interest to SHGs. The latter by using IVR technology in both Andhra Pradesh and Telangana is able to ensure recoveries and prevent misuse of funds. While rates of interest to SHGs are moderate, in the case of NABFINS it is a high-risk model, without savings deposits or the FLDG, in which several B&C partner SHPIs have defaulted and absconded. It finds that the JLG methodology is more disciplined and is moving away from mainly lending to and through SHGs. While Stree Nidhi is free of this problem, since it is a government promoted entity there is the risk of political interference in its operations.

For an NGO-SHPI not having its own in-house MFI, with the decline in donor funds for SHG development, the various revenue models reflecting options available for facilitating lending from banks to its SHGs and federations with varying risk exposure. These included: (i) an interest spread of 6 to 9 per cent with a 10 per cent default risk from a bank; (ii) a 5 per cent monthly average loan outstanding as service charge (adjustable against default) as BF under NABARD'S Women's SHG Fund programme; (iii) risk-free service fees of 2 per cent of loan outstanding (ICICI or NABFINS); and (iv) zero fee in the case of direct bank linkage of the SHGs promoted.

For SHGs, on the other hand, the terms of their engagement in financial intermediation are largely decided by their promoters and the financing agencies—a far cry from the 'new middlewomen' managing a micro-bank of and for their SHG members envisaged 20 years ago, who have in most contexts effectively become mere facilitators in the delivery chain. This dilution of the financial intermediation role of SHGs appears to have been carried over to the financial inclusion model. In some respects it is SHGs themselves that have the best qualifications to act as BCs or subagents. However, they still do not figure on the list of eligible entities. Undoubtedly, the determining factor in such a scenario is going to be the massive NRLM project that is committed to the SHG model and has been co-opting SHGs promoted by other SHPIs. It is critical how it supports SHGs and draws upon the proposed infrastructure of SHG federations and other livelihood organisations of the poor towards a genuine demand-driven strategy and arranges the financial resources for their needs.

CONCLUDING OBSERVATIONS

The SHG movement that showed exponential rates of growth for about 20 years has now settled to a low rate of expansion. The NRLM has arrogated to itself the leadership of women SHGs that constitute over 80 per cent of SHGs in the country even as NABARD's involvement in promotion withers away. The mission is actively furthering a role for SHG federations in financial intermediation and in BC channels for SHG member-agents and other means of their engagement with digital technology. As such the future development of SHGs rests mainly in the hands of the NRLM which, despite its impressive performance through a multi-pronged top-down strategy, appears to be also crowding out the space for civil society initiatives. A major initiative of NABARD, with the NRLM implementing a similar system, is the eShakti member-based MIS that now covers nearly 4 lakh SHGs. This could strengthen appraisal systems and lead to greater flow of credit to them. While major PSBs and RRBs retain their appetite for SHG lending though only in certain regions, some private banks, through dedicated verticals, appear to have been able to develop a more focused and viable approach to SHG lending. MFI and BC involvement in lending to SHGs, though supplementing channels of flow of financial services through SHGs, however, has served to diminish their role in financial intermediation.

ANNEXURE 6.1:
Savings of SHGs with Banks—Region-wise/State-wise/Agency-wise Position as of 31 March 2018 (in Rs million)

	Commercial banks		Regional rural banks		Cooperative banks		Total	
	No. of SHGs	Savings amount (in Rs million)	No. of SHGs	Savings amount (in Rs million)	No. of SHGs	Savings amount (in Rs million)	No. of SHGs	Savings amount (in Rs million)
Central Region								
Chhattisgarh	68,494	1,103	1,00,646	990	21,373	161	1,90,513	2,254
Madhya Pradesh	1,39,596	1,779	1,09,703	1,168	6,879	60	2,56,178	3,007
Uttarakhand	18,185	230	20,500	307	9,456	262	48,141	799
Uttar Pradesh	1,41,399	1,845	2,55,950	1,566	10,041	67	4,07,390	3,479
Total	**3,67,674**	**4,957**	**4,86,799**	**4,031**	**47,749**	**550**	**9,02,222**	**9,539**
Eastern Region								
Andaman & Nicobar	534	7	0	0	4,723	95	5,257	102
Bihar	2,46,594	4,588	3,48,168	5,249	28	0	5,94,790	9,838
Jharkhand	92,889	3,828	58,771	656	1,532	4	1,53,192	4,487
Odisha	3,02,581	4,424	1,76,387	4,127	51,521	696	5,30,489	9,248
West Bengal	3,99,990	6,569	2,53,123	8,983	1,94,156	4,952	8,47,269	20,505
Total	**10,42,588**	**19,416**	**8,36,449**	**19,015**	**2,51,960**	**5,748**	**21,30,997**	**44,180**
Northeastern Region								
Arunachal Pradesh	2,101	38	2,073	23	1,826	30	6,000	90
Assam	92,271	585	2,57,671	1,333	26,044	29	3,75,986	1,947
Manipur	4,938	20	9,378	19	2,644	2	16,960	41
Meghalaya	2,271	14	5,269	64	3,887	40	11,427	118
Mizoram	356	2	8,578	66	0	0	8,934	68
Nagaland	4,184	34	1,027	9	1,322	10	6,533	53
Sikkim	4,836	186	0	0	1,241	22	6,077	208
Tripura	11,547	162	31,688	477	10,439	57	53,674	695
Total	**1,22,504**	**1,041**	**3,15,684**	**1,990**	**47,403**	**189**	**4,85,591**	**3,221**
Northern Region								
Chandigarh	315	2	0	0	42	0	357	2
Haryana	16,362	140	18,208	147	3,646	36	38,216	323
Himachal Pradesh	0	193	11,274	267	20,809	207	49,353	668
Jammu and Kashmir	0	95	4,457	192	1,305	3	17,980	291
New Delhi	0	122	0	0	302	7	4,331	129
Punjab	21,049	155	10,343	86	6,342	81	37,734	322
Rajasthan	1,42,709	1,487	1,06,138	1,205	82,065	502	3,30,912	3,194
Total	**2,13,952**	**2,195**	**1,50,420**	**1,898**	**1,14,511**	**837**	**4,78,883**	**4,929**
Southern Region								
Andhra Pradesh	7,21,771	56,935	1,92,665	8,945	13,120	944	9,27,556	66,824
Karnataka	3,64,901	4,601	2,27,993	1,510	2,42,749	5,360	8,35,643	11,470
Kerala	1,91,995	3,648	61,021	1,194	43,273	781	2,96,289	5,623

	Commercial banks		Regional rural banks		Cooperative banks		Total	
	No. of SHGs	Savings amount (in Rs million)	No. of SHGs	Savings amount (in Rs million)	No. of SHGs	Savings amount (in Rs million)	No. of SHGs	Savings amount (in Rs million)
Lakshadweep	166	1	0	0	0	0	166	1
Puducherry	19,088	171	4,781	59	853	189	24,722	419
Tamil Nadu	7,86,646	7,723	84,703	789	1,75,754	2,266	10,47,103	10,779
Telangana	2,31,814	9,386	2,75,549	16,937	10,454	143	5,17,817	26,467
Total	**23,16,381**	**82,465**	**8,46,712**	**29,434**	**4,86,203**	**9,683**	**36,49,296**	**1,21,583**
Western Region								
Daman & Diu	43	1	0	0	0	0	43	1
Dadra and Nagar Haveli	599	17	0	0	0	0	599	17
Goa	4,438	108	0	0	3,780	111	8,218	219
Gujarat	1,55,776	1,844	55,536	651	28,985	240	2,40,297	2,735
Maharashtra	4,09,757	4,598	1,16,144	1,054	3,22,390	3,846	8,48,291	9,498
Total	**5,70,613**	**6,568**	**1,71,680**	**1,704**	**3,55,155**	**4,197**	**10,97,448**	**12,469**
Grand total	46,33,712	1,16,642	28,07,744	58,074	13,02,981	21,205	87,44,437	1,95,921

Source: NABARD, *Status of Microfinance in India 2017–18* (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.

ANNEXURE 6.2:
Progress under SHG-Bank Linkage Programme—Bank Loans Disbursed during the Year 2017–18 by State/Region and Financing Agency

	Commercial banks		Regional rural banks		Cooperative banks		Total	
	No. of SHGs	Disbursed amount (in Rs million)	No. of SHGs	Disbursed amount (in Rs million)	No. of SHGs	Disbursed amount (in Rs million)	No. of SHGs	Disbursed amount (in Rs million
Central Region								
Chhattisgarh	15,434	1,546	4,964	612	1,288	149	21,686	2,308
Madhya Pradesh	17,013	1,231	8,833	562	141	5	25,987	1,798
Uttarakhand	1,395	114	2,440	96	580	48	4,415	259
Uttar Pradesh	10,849	805	6,132	418	226	6	17,207	1,229
Total	**44,691**	**3,697**	**22,369**	**1,688**	**2,235**	**209**	**69,295**	**5,594**
Eastern Region								
Andaman & Nicobar	63	23	0	0	246	44	309	67
Bihar	1,08,870	9,532	1,17,747	13,904	28	0	2,26,645	23,436
Jharkhand	24,728	1,682	10,587	1,681	151	25	35,466	3,388
Odisha	43,048	8,085	63,136	6,441	5,227	641	1,11,411	15,167
West Bengal	1,22,431	15,454	1,55,638	26,988	68,544	6,395	3,46,613	48,837
Total	**2,99,140**	**34,775**	**3,47,108**	**49,014**	**74,196**	**7,106**	**7,20,444**	**90,895**
Northeastern Region								
Arunachal Pradesh	27	1	73	10	19	1	119	12

	Commercial banks		Regional rural banks		Cooperative banks		Total	
	No. of SHGs	Disbursed amount (in Rs million)	No. of SHGs	Disbursed amount (in Rs million)	No. of SHGs	Disbursed amount (in Rs million)	No. of SHGs	Disbursed amount (in Rs million
Assam	9,542	1,132	21,175	1,940	312	21	31,029	3,094
Manipur	89	6	267	27	74	4	430	37
Meghalaya	20	2	329	24	38	2	387	28
Mizoram	5	1	588	100	0	0	593	101
Nagaland	225	34	20	6	482	100	727	140
Sikkim	710	65	0	0	2	0	712	65
Tripura	375	30	278	30	367	36	1,020	96
Total	**10,993**	**1,271**	**22,730**	**2,137**	**1,294**	**164**	**35,017**	**3,572**
Northern Region								
Chandigarh	21	1	0	0	0	0	21	1
Haryana	2,998	199	1,694	169	56	3	4,748	371
Himachal Pradesh	1,960	255	385	50	1,183	197	3,528	502
Jammu and Kashmir	8,764	933	908	120	4	1	9,676	1,054
New Delhi	128	20	0	0	1	0	129	20
Punjab	2,106	124	869	61	561	11	3,536	197
Rajasthan	19,086	2,293	9,790	824	1,286	143	30,162	3,259
Total	**35,063**	**3,825**	**13,646**	**1,223**	**3,091**	**356**	**51,800**	**5,404**
Southern Region								
Andhra Pradesh	2,36,456	78,069	72,839	26,748	5,171	1,703	3,14,466	106,520
Karnataka	2,81,672	60,200	81,561	11,070	36,062	10,698	3,99,295	81,968
Kerala	72,356	22,001	8,872	2,943	9,540	2,342	90,768	27,286
Lakshadweep	0	0	0	0	0	0	0	0
Puducherry	1,566	486	722	230	179	76	2,467	793
Tamil Nadu	1,18,585	40,905	15,866	5,414	29,578	7,288	1,64,029	53,606
Telangana	1,01,358	31,593	1,80,856	48,218	2,364	900	2,84,578	80,711
Total	**8,11,993**	**2,33,254**	**3,60,716**	**94,623**	**82,894**	**23,007**	**12,55,603**	**3,50,883**
Western Region								
Dadra and Nagar Haveli	60	2	0	0	0	0	60	2
Goa	585	129	0	0	107	40	692	168
Gujarat	10,264	873	4,793	496	1,121	155	16,178	1,524
Maharashtra	60,097	9,250	11,201	2,013	40,745	2,553	1,12,043	13,815
Total	**71,006**	**10,254**	**15,994**	**2,509**	**41,973**	**2,748**	**1,28,973**	**15,510**
Grand total	12,72,886	2,87,076	7,82,563	1,51,193	2,05,683	33,589	22,61,132	4,71,859

Source: NABARD, *Status of Microfinance in India* 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.

ANNEXURE 6.3:
Progress under SHG-Bank Linkage Programme: Bank Loans Outstanding by State/ Region and Financing Agency as of 31 March 2018

	Commercial banks		Regional rural banks		Cooperative banks		Total	
	No. of SHGs	Amount outstanding (in Rs million)	No. of SHGs	Amount outstanding (in Rs million)	No. of SHGs	Amount outstanding (in Rs million)	No. of SHGs	Amount outstanding (in Rs million)
Central Region								
Chhattisgarh	29,366	218	74,374	2,287	3,012	137	1,06,752	4,601
Madhya Pradesh	51,103	286	37,272	1,531	323	11	88,698	4,403
Uttarakhand	8,340	51	5,443	153	3,410	234	17,193	901
Uttar Pradesh	59,590	528	1,28,723	6,298	3,422	135	1,91,735	11,712
Total	1,48,399	1,083	2,45,812	10,268	10,167	516	4,04,378	21,617
Eastern Region								
Andaman & Nicobar	139	24	0	0	838	79	977	103
Bihar	1,85,756	13,467	2,89,129	18,268	28	0	4,74,913	31,735
Jharkhand	49,085	2,342	31,152	1,254	245	49	80,482	3,645
Odisha	1,19,916	10,964	94,027	10,531	19,002	1,125	2,32,945	22,621
West Bengal	2,71,937	21,020	2,22,340	30,516	1,28,559	7,166	6,22,836	58,703
Total	6,26,833	47,817	6,36,648	60,569	1,48,672	8,420	14,12,153	1,16,806
Northeastern Region								
Arunachal Pradesh	411	17	73	8	42	8	526	32
Assam	35,379	2,695	62,061	4,008	3,015	74	1,00,455	6,777
Manipur	235	22	1,186	63	74	4	1,495	89
Meghalaya	159	11	774	61	759	22	1,692	94
Mizoram	96	8	1,728	246	0	0	1,824	254
Nagaland	696	60	107	30	482	95	1,285	185
Sikkim	3,431	281	0	0	4	0	3,435	281
Tripura	5,985	389	20,844	516	6,107	289	32,936	1,193
Total	46,392	3,482	86,773	4,931	10,483	492	1,43,648	8,905
Northern Region								
Chandigarh	71	5	0	0	1	0	72	5
Haryana	7,222	459	7,152	717	799	59	15,173	1,235
Himachal Pradesh	0	384	1,640	171	4,546	443	10,420	998
Jammu and Kashmir	0	706	1,475	123	230	7	8,971	836
New Delhi	0	62	0	0	7	0	320	62
Punjab	5,664	357	2,825	147	1,697	78	10,186	582
Rajasthan	43,200	2,858	20,221	1,081	35,865	1,030	99,286	4,969
Total	67,970	4,830	33,313	2,238	43,145	1,618	1,44,428	8,686

	Commercial banks		Regional rural banks		Cooperative banks		Total	
	No. of SHGs	Amount outstanding (in Rs million)	No. of SHGs	Amount outstanding (in Rs million)	No. of SHGs	Amount outstanding (in Rs million)	No. of SHGs	Amount outstanding (in Rs million)
Southern Region								
Andhra Pradesh	5,90,445	1,75,976	1,72,919	44,222	10,751	2,219	7,74,115	2,22,417
Karnataka	5,54,950	80,855	1,11,868	18,578	77,661	11,827	7,44,479	1,11,261
Kerala	1,44,555	31,088	16,347	3,234	12,930	2,912	1,73,832	37,234
Lakshadweep	2	0	0	0	0	0	2	0
Puducherry	4,474	725	1,969	348	841	165	7,284	1,238
Tamil Nadu	2,72,207	51,703	27,580	5,249	77,209	9,526	3,76,996	66,479
Telangana	2,85,823	63,916	2,68,229	72,145	8,655	1,560	5,62,707	1,37,621
Total	18,52,456	4,04,265	5,98,912	1,43,776	1,88,047	28,209	26,39,415	5,76,249
Western Region								
Dadra Nagar Haveli	219	7	0	0	0	0	219	7
Goa	1,027	201	0	0	445	78	1,472	279
Gujarat	31,584	1,695	28,523	1,955	5,819	144	65,926	3,794
Maharashtra	1,29,206	14,349	28,240	3,649	51,273	1,642	2,08,719	19,641
Total	1,62,036	16,253	56,763	5,605	57,537	1,864	2,76,336	23,721
Grand total	29,04,086	4,87,481	16,58,221	2,27,386	4,58,051	41,118	50,20,358	7,55,985

Source: NABARD, *Status of Microfinance in India* 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.

ANNEXURE 6.4:
NPA Levels of SHGs by State/Region and Financing Agency as of 31 March 2018

	Public sector commercial banks		Private sector commercial banks		Regional rural banks		Cooperative banks		Total	
	Amt of GNPA against SHGs (in Rs million)	NPA as %age to loan outstanding	Amt of GNPA against SHGs (in Rs million)	NPA as %age to loan outstanding	Amt of GNPA against SHGs (in Rs million)	NPA as %age to loan outstanding	Amt of GNPA against SHGs (in Rs million)	NPA as %age to loan outstanding	Amt of GNPA against SHGs (in Rs million)	NPA as %age to loan outstanding
Central Region										
Chhattisgarh	224	13.18	0	0.07	209	9.13	21	15.54	455	9.88
Madhya Pradesh	614	25.38	17	3.77	233	15.24	5	44.51	869	19.74
Uttarakhand	275	60.94	6	9.10	32	20.74	85	36.43	397	44.07
Uttar Pradesh	1,156	22.78	61	30.06	2,294	36.43	107	79.47	3,618	30.90
Total	2,269	23.52	84	7.09	2,768	26.96	218	42.30	5,339	24.70
Eastern Region										
Andaman & Nicobar	1	2.96	0	0.00	0	0.00	7	9.37	8	7.85
Bihar	1,096	8.14	0	0.58	1,316	7.21	0	0.00	2,412	7.60
Jharkhand	394	16.84	0	58.81	157	12.50	0	0.00	551	15.13
Odisha	1,999	22.25	1	0.06	1,146	10.89	100	8.90	3,247	14.35
West Bengal	772	3.68	0	0.00	1,025	3.36	359	5.01	2,157	3.67
Total	4,262	9.30	2	0.08	3,645	6.02	466	5.54	8,375	7.17
Northeastern Region										
Arunachal Pradesh	7	39.98	0	0.00	2	29.53	0	0.00	9	27.85
Assam	525	19.51	0	0.00	550	13.73	48	64.37	1,123	16.57
Manipur	2	8.35	0	0.00	14	22.42	0	0.00	16	17.85
Meghalaya	5	46.60	0	0.00	9	14.16	14	62.82	28	29.25
Mizoram	3	44.55	0	0.00	36	14.47	0	0.00	39	15.37
Nagaland	6	10.43	0	100.00	2	7.49	1	1.05	10	5.15
Sikkim	6	2.18	0	0.00	0	0.00	0	0.00	6	2.18
Tripura	97	24.82	0	0.00	358	69.35	59	20.45	513	43.02
Total	651	18.72	0	1.13	971	19.69	121	24.69	1,744	19.58

	Public sector commercial banks		Private sector commercial banks		Regional rural banks		Cooperative banks		Total	
	Amt of GNPA against SHGs (in Rs million)	NPA as %age to loan outstanding	Amt of GNPA against SHGs (in Rs million)	NPA as %age to loan outstanding	Amt of GNPA against SHGs (in Rs million)	NPA as %age to loan outstanding	Amt of GNPA against SHGs (in Rs million)	NPA as %age to loan outstanding	Amt of GNPA against SHGs (in Rs million)	NPA as %age to loan outstanding
Northern Region										
Chandigarh	2	40.03	0	0.00	0	0.00	0	0.00	2	40.00
Haryana	215	48.57	2	9.54	114	15.92	48	80.48	378	30.62
Himachal Pradesh	49	12.84	0	0.00	27	15.73	63	14.27	139	13.96
Jammu and Kashmir	10	12.47	1	0.23	12	9.65	5	71.40	28	3.36
New Delhi	8	14.86	0	0.00	0	0.00	0	0.00	8	13.63
Punjab	173	50.09	7	57.58	18	12.48	26	33.75	224	38.54
Rajasthan	503	38.09	48	3.09	326	30.21	265	25.72	1,141	22.97
Total	**960**	**36.50**	**57**	**2.60**	**498**	**22.23**	**407**	**25.17**	**1,922**	**22.12**
Southern Region										
Andhra Pradesh	5,558	3.16	28	16.96	971	2.19	102	4.59	6,659	2.99
Karnataka	2,510	3.32	378	7.05	965	5.20	296	2.50	4,149	3.73
Kerala	1,152	5.30	69	0.74	88	2.72	184	6.32	1,493	4.01
Lakshadweep	0	78.26	0	0.00	0	0.00	0	0.00	0	78.26
Puducherry	156	23.44	0	0.23	20	5.89	35	21.37	212	17.13
Tamil Nadu	6,219	16.30	558	4.12	391	7.45	926	9.72	8,094	12.18
Telangana	3,975	6.23	6	3.79	1,071	1.48	57	3.65	5,108	3.71
Total	**19,571**	**5.21**	**1,039**	**3.63**	**3,506**	**2.44**	**1,600**	**5.67**	**25,715**	**4.46**
Western Region										
Dadra and Nagar Haveli	0	1.47	0	0.00	0	0.00	0	0.00	0	1.47
Goa	10	6.75	0	0.04	0	0.00	5	6.92	16	5.65
Gujarat	154	12.23	45	10.28	281	14.35	47	32.74	526	13.87
Maharashtra	1,817	23.93	91	1.35	493	13.50	243	14.79	2,643	13.46
Total	1,981	21.98	136	1.87	773	13.80	295	15.84	3,185	13.43
Grand total	29,695	6.65	1,317	3.19	12,160	5.35	3,108	7.56	46,281	6.12

Source: NABARD, *Status of Microfinance in India* 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.

ANNEXURE 6.5:
Sangam Jeevika Cluster Level Federation—Musahari, Muzaffarpur District, Village Khabra Gadchi Tola

The SHG of this village was promoted 10 years ago. There are 22 tolas in the village, each tola comprising about 100 households. A cluster consists of 19 revenue villages (5 gram panchayats) with 44 VOs and 549 SHGs. There are 10–20 SHGs per VO and a total of 6,900 households. The cluster has a master bookkeeper, 2 cluster facilitators, a treasurer, 3 Bank Mitras, and 7 VO bookkeepers covering 5–7 VOs each. In addition, there are community mobilisers who receive Rs 3,300 and cover 13–14 SHGs each. The VO bookkeepers receive a fee of about Rs 4,000 or Rs 400–700 per VO. The Bank Mitra facilitates SHGs and is drawn from the Jeevika staff. In each block, there are 3–4 CLFs.

Among the banks, the response of the SBI and the CBI for bank linkage has been good. The linkage committee looks into the matter of NPAs, which are over three months overdue. The Bank Mitra is provided with a list of overdue accounts. There are 530 SHGs that have credit linkage with an average of Rs 3 lakh per SHG. SHGs are given an RF of Rs 5,000 and an additional CIF is given to the extent of Rs 30,000 per SHG (this was earlier Rs 50,000). Along with SHG savings and surpluses, this amounts to a corpus of about Rs 2 lakh per SHG. SHGs are given loans at 11.5 per cent per annum, which they pass on to members at 12 per cent, as per instructions of Jeevika (at 10 per cent, that is 1 per cent per month). The MIS of SHGs and VOs is maintained at the block level. Handwritten records are maintained for transactions, which are then consolidated for the several clusters at the block level. SHGs save Rs 10–20 per week and hold weekly meetings. While KCC loans have high NPAs, SHG loans have a good repayment record. SHG accounts are not computerised. Seven books are maintained at the SHG level—three ledgers and four types of passbooks. SHG members are active on social issues such as prohibition, child marriage, and in the Open Defecation Free campaign, in which SHG members have taken loans to build 267 toilets. They have received loans for toilet construction under the Bihar Rural Sanitation Programme. The completion of the toilet is monitored by geotagging.

A loan of Rs 12,000 is given for toilet construction under the campaign. The construction of a toilet when reported by a member makes her eligible for a subsidy of the same amount under the scheme. However, no subsidy has been received so far.

The CLF has received Rs 1.64 crore by way of the CIF. The fund has grown in value to Rs 2.50 crore. The CIF is paid in 60 instalments to the VO, which returns it in 100–120 instalments to the CLF. VOs are graded periodically and loans are given by CLFs to members only in VOs that are in Grade 1 and Grade 2 categories; loans are not given to VOs that are rated as Grade 3. There is also a health risk fund or emergency fund of Rs 1 lakh; now reduced to Rs 50,000. SHG members also contribute Rs 10 per month to the health risk fund, which is used as a fund to give emergency loans for health-related needs.

SHG members do not have access to MFI loans, though Bandhan and some other MFIs/banks are understood to be active in the area. Besides, MFI loans are very strict in their repayment requirement, whereas SHGs are flexible. While a few members have a demand for loans and almost all have applied for Mudra loans, the largely landless members of the group prefer to have salaried employment rather than loans. Members also contribute Rs 1 per month as per a CLF decision for an education fund. 6,200 members have contributed and 11 children have been provided means for education. The idea was derived from a similar programme in Andhra Pradesh. Livelihood initiatives that are planned include milk society and chilling centre and producer organisations for vegetable growers. In addition, the CLF arranges for the sale of paddy through multi-service PACS, to realise better prices than the Rs 12–14 per kg available at the village level. There is also a fortified food plant set up by NIDAN and GAIN India, which supplies vitamin-enriched meals under the ICDS.

There are various types of CRPs: SHG CRPs for (i) formation (ii) PRA and (iii) training. At the VO level, there are two CRPs, one for formation of VOs, and one for training. There are two CRPs at the CLF. In addition there are two CRPs under the WASH (water sanitation and health programme) for the ODF campaign. There are also five CRPS responsible for financial inclusion, which is a new concept to facilitate bank-linkage. Bank Sakhis are not operational in the area.

The CLF operates a Whatsapp group as well. It facilitated 425 Mudra loan applications to the SBI four months ago for Shishu loans of up to Rs 50,000. However, these attract bank charges of Rs 1,200 and Rs 1,000 stamp duty plus other charges. For loans over Rs 50,000 (Kishor loans), the total charges are Rs 7,500 (Rs 6,000 as stamp duty and Rs 1,500 in bank and other charges). Notably it is only in Bihar that such a high stamp duty is payable on Mudra loans. The matter has been taken up with banks and the government to be resolved before the off-take of Mudra loans can pick up.

ANNEXURE 6.6: Promotion of Joint Liability Groups through RRBs—An Update from Odisha[1]

Background of JLGs in India

The Joint Liability Group has been considered as one of the popular methodologies, especially to extend credit support to small, marginal and tenant farmers as well as entrepreneurs for taking up livelihood-based activities, both individually as well as collectively in a group. The RBI through an official notification dated 13 November 2014 advised all banks to form and on-lend through JLGs in their respective service areas based on its prescribed guidelines.[2]

Along with implementing the budget (2014–15) announcement for financing of joint farming groups of 'Bhoomi Heen Kisan' of the Government of India, the RBI's consideration was that a few members of SHGs may graduate faster to start or expand economic activities requiring much higher levels of loans than other SHG members. In such cases, other members may not like to stand mutual guarantee for large-sized loans for these members. In such cases, a JLG may be created consisting of such members of one or more SHGs. As noted in the RBI circular, one of the key objectives for promoting JLGs has been 'to augment flow of credit to landless farmers cultivating land as tenant farmers, oral lessees or share croppers and small/marginal farmers as well as other poor individuals taking up farm activities, off-farm activities and non-farm activities.' NABARD extends grant support for the formation and nurturing of JLGs to banks and other JLG promoting agencies. Apart from providing 100 per cent refinance support to banks it also extends financial support for awareness creation and capacity building of all stakeholders of this programme. NABARD has been arranging training programmes and exposure visits to successful JLGs, to the functionaries of these institutions including financing banks.

NABARD Initiative for the Promotion of JLGs through RRBs

As RRBs have a huge rural network, NABARD encouraged RRBs to finance JLGs in a big way and accordingly entered into MoUs with 36 RRBs and the SBI in 19 states during 2017–18. Under this scheme, NABARD provides grant assistance to banks for using CBC/NGO as JLGPI and for capacity building to create a pool of trainers out of bank staff for the formation, nurturing and financing of new JLGs.

Encouraged by NABARD's 100 per cent refinance support to banks, the scheme has also recorded an impressive growth in the country. According to NABARD's annual report, Status of Microfinance in India, 2017–18, as against 7.02 lakh JLGs promoted during 2016–17, those promoted during 2017–18 were 10.19 lakh, taking the cumulative number of JLGs promoted and financed by banks to 34.73 lakh as at the end of March 2018. The southern states top the list with over 11.03 lakh JLGs organised cumulatively, and the eastern region follows closely with 10.72 lakh JLGs. In terms of loans disbursed, however, southern states account for nearly 41 per cent of the total loans disbursed cumulatively.[3]

Progress Updates on JLGs from Odisha

The concept of the JLG could attract reasonable responses from banks and promoting organisations in the state. In order to give a push to the model,

JLG Promotion in Odisha: 2017–18 (Status as of 31 March 2018)

	Banks	Physical target	Applications sanctioned		Applications disbursed		Balance of outstanding	
			Accounts	Amount (in Rs crore)	Accounts	Amount (in Rs crore)	Accounts	Amount (in Rs crore)
1	PSB	28,958	2,222	45.53	2,226	45.5	3,969	29.3
2	Private sector bank	5,191	4,22,314	1,609.04	2,59,691	1,597.54	2,88,838	1,429.18
3	RRBs	11,809	964	1.95	964	1.95	15,377	81.04
4	OSCB	14,042	15,054	85.38	15,054	85.38	48,260	195.66
	Total	**60,000**	**4,40,554**	**1,741.9**	**2,77,935**	**1,730.37**	**3,56,444**	**1,735.18**

Source: Odisha State Level Bankers Committee Report (151st SLBC Meeting), July 2018.

[1] Note prepared by Narendra Nayak and Access-Assist Odisha team.
[2] RBI/2014-15/304, FIDD.CO.FSD.BC 42/05.02.02/2014-15. Dated 13 November 2014.
[3] NABARD, *Status of Microfinance in India*, 2017–18 (Mumbai: NABARD, 2018).

NABARD signed tripartite/bipartite MoUs with two RRBs in the state. The SBI and the Odisha State Cooperative Bank (OSCB) have also signed MoUs for implementing the model in the states of West Bengal and Odisha, respectively. Four Trainers of Trainees (ToT) programmes have been conducted at BIRD centres for master trainers of each of the participating banks on the JLG business model, for popularising the programme. Along with assigning the tasks to all banks in the state, the State-Level Bankers Coordination (SLBC) has been monitoring the progress in close coordination with the RBI and NABARD regional offices. As per the SLBC report of July 2018, the total amount disbursed for the period 1 April 2017 to 31 March 2018 to JLGs is Rs 1,730.37 crore in 2,77,935 accounts and balance outstanding as of 31 March 2018 is Rs 1,735.18 crore in 3,56,444 accounts. The progress updates of JLGs as on 31 March 2018 in Odisha is given in the following table.

Challenges for the Model

Most of the banks such as PSUs, private, RRBs and cooperative banks have been involved in promoting JLGs in the state of Odisha. The accomplishments of the private banks, especially Axis, HDFC and Bandhan banks have been quite impressive. So also the progress made by the OSCB. While some of the banks form and link JLGs through their branch staff, others take the support of local NGOs/BCAs to promote the groups and extend loans to members, both women and men. Coming out of the erstwhile group mechanism through SHGs, it is understood that women members also take a keen interest in joining JLGs as they can quickly get a bigger dose of loans to start or expand their business activities. Male JLGs are provided loans mainly for agro-based activities. Repayment of loans to banks from JLGs is found to be quite good so far. However, the JLG programme has also faced a few challenges. Lack of orientation for members towards enterprise promotion and productive use of bigger loans, inadequate linkages from banks (in apprehension that the loan might go bad), increased workload and limited staff in bank branches, low level of promotional incentives for NGOs/BCs, and relatively poor peer pressure among a few male JLGs have been some of the key challenges faced in the process of JLG promotion.

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1 Not all federations were financial federations. Also, the NRLM has undertaken the reorganisation of the existing federations in several areas. A recent estimate of the NRLM for July 2018 reports 2,67,394 village organisations (VOs) or primary-level federations of SHGs under the NRLM and related programmes.

2 Ajay Tankha, *Banking on Self-Help Groups: Twenty Years On* (New Delhi: Sage Publications, 2012).

3 On the basis of an average of 12 members per SHG.

4 Internal SHG savings have been assumed by NABARD over the years to be 70 per cent of the total SHG savings (i.e. total of SHG corpus held within the group and in bank accounts). SHG savings retained and rotated with the groups as of 31 March 2018 would thus be estimated to be Rs 457.15 billion.

5 These and other data below are from NABARD, *Status of Microfinance in India* 2017–18 (Mumbai: NABARD, 2018). https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%202017-18.pdf. Accessed on 29 September 2018.

6 The banks have reported an addition of 6.3 lakh savings-linked SHGs in 25 states and UTs, while there was a decline of 4.63 lakh savings bank accounts in the other 9 states and UTs during 2017–18. Bihar, Odisha, Tamil Nadu and Andhra Pradesh together have put 4.69 lakh fresh savings-linked SHGs during the year. On the other hand, Karnataka, Kerala, West Bengal and Maharashtra together have reported 4.46 lakh lesser number of SHGs as compared to the previous year (NABARD, *Status of Microfinance in India* 2017–18 [Mumbai: NABARD, 2018]. https://www.nabard.org/auth/writereaddata/tender/1907183104SMFI%20 2017-18.pdf. Accessed on 29 September 2018.).

7 According to the *Status of Microfinance in India, 2015–16,* (Mumbai: NABARD, 2016) there was potential for the formation of a further 3.7 million SHGs in the country as of March 2016 when there were 7.9 million savings-linked SHGs.

8 Other reasons for the slow down in the addition to SHG numbers suggested by NABARD have been the saturation in potential areas for the formation of new SHGs and restricted operations by SHPAs forming SHGs.

9 SHG numbers reported by the NRLM cover both SHGs promoted under the programme as well as 'home-grown' SHGs promoted earlier by NGOs and other SHPAs that have subsequently been 'co-opted' into the programme. There is thus an inevitable increase in the share of NRLM SHGs in total SHGs. Also, the discontinuity resulting from the break in the SGSY-NRLM channel possibly serves to distort the relative growth rates of this programme.

[10] The author is grateful to G.R. Chintala, D. Narendranath and Amit Arora for their valuable inputs.

[11] Co-opting an SHG into the NRLM fold entitles the SHG to receive funds from the NRLM, and in turn they have to comply with the five principles of good SHGs or the Panch Sutra (namely regular meetings, regular savings, regular inter-loaning, timely repayment and up-to-date books of accounts) and follow the NRLM's bookkeeping norms.

[12] Similarly, in Rajasthan the gram panchayat level entities comprising of 15–20 SHGs were earlier ordinarily called cluster federations—and are akin to VOs of the new dispensation. The erstwhile cluster federations were generally federated further into block-level federations composed of 15–20 VOs. Under the NRLM, a similar number of VOs are federated into the new CLF. However, in view of the larger SHG numbers over the years, there can be several CLFs in a development block.

[13] Indeed, there are also reports of the continued hijacking of groups by certain SRLMs of successful ongoing projects of other promoters.

[14] A telling example of this was the recent fixing of the SHG's internal lending rate by the SRLM in Bihar at 12 per cent p.a. suggestive of little or no agency on the part of the group to manage its own affairs.

[15] A particularly glaring instance of this was the case of a letter being sent from the SRLM to an NGO promoter with long years of experience in the state informing them that they were not to visit or interact with the co-opted SHGs and CLFs that they had promoted and with whom they were still engaged in other development activity.

[16] Under the Kudumbashree programme of Kerala, panchayats are independent and politicised, as are the SHGs which have a different dynamic as the narrative is dominated by the polity. The panchayats have the power to implement projects rather than the state.

[17] For example: (i) Local-level planning exercises such as the Intensive Participatory Planning Exercise (IPPE) of the Ministry of Rural Development and the Gram Panchayat Development Plan (of the Ministry of Panchayati Raj); (ii) pilot initiative in Jharkhand where SHG members were selected as mates under the Mahatma Gandhi National Rural Employment Guarantee Scheme (MGNREGS); (iii) pilot initiative in Rajasthan where the Women's CLFs served as the MGNREGS Project Implementation Agency (PIA) for individual works on the lands of SHG members with priority given to SC/ ST/ BPL households; (iv) role of SHGs in implementation and management of MGNREGS works in convergence with other construction programmes—such as individual household latrine (IHHL) under Swachch Bharat Mission, Pradhan Mantri Awas Yojana–Gramin (PMAY-G) and construction of anganwadi centres (AWCs) under Integrated Child Development Services (ICDS).

[18] Rukmini Tankha, *Convergent Planning for Rural Development: A Gendered Review of the Intensive Participatory Planning Exercise (IPPE)* (New Delhi: UN Women, forthcoming).

[19] This section draws largely from NABARD, *Status of Microfinance in India, 2017–18* (Mumbai: NABARD, 2018).

[20] Vide RB Circular no. RBI/2015-16/291DBR.CID. BC.No.73/20.16.56/2015-16. Dated 14 January 2016. https://rbi.org.in/Scripts/NotificationUser.aspx?Id=10227&Mode=0. Accessed on 29 September 2018.

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Small Finance Banks and Payments Banks: Struggle for Differentiation and Business Model Continues

7

BACKGROUND OF SMALL FINANCE BANKS AND PAYMENTS BANKS

The Indian financial sector policy's quest for financial inclusion and directing flow of credit to priority sectors has often taken the route of establishing a new institution. Setting up of NABARD, SIDBI, local area banks (LABs) and RRBs are examples from 1979 to the 1990s, while MUDRA, SFBs and PBs came up post-2014. The experience with the earlier set of institutions has been mixed; while NABARD and SIDBI have emerged as apex banks for rural finance and MSME finance respectively, LABs as a concept did not take off, and in the case of RRBs there have been so many changes ranging from opening up of lending to consolidation that present-day RRBs have hardly any trace of the original concept. It is important to recollect that RRBs are the earlier version of SFBs. They were established in the late 1970s at the district level and the RRB Act, 1976 defined their business as:

> Developing the rural economy by providing, for the purpose of development of agriculture, trade, commerce, industry and other productive activities in the rural areas, credit and other facilities, particularly to the small and marginal farmers, agricultural labourers, artisans and small entrepreneurs, and for matters connected therewith and incidental thereto.[1]

Basically these were small-value enterprise loans to poorer sections of society. Over a period of time, business limitations were gradually eased and the area of operation expanded, both measures were taken keeping in view the viability aspect. As a result, the number of RRBs has shrunk to 56 as of 31 March 2018 from a peak of 196, and a newspaper report suggests that there is a move for further consolidation.[2] The discussion in chapter 2 shows that despite these moves, areas of concern continue to persist in the form of 11 RRBs running at a loss, the drift towards larger loan sizes, a high concentration of the portfolio in agriculture and a larger share of savings deposit in overall deposits.

The history of RRBs has informed the concept of SFBs. The first mention of this idea came in the report of the committee on financial sector reforms headed by Raghuram Rajan in 2009. The committee was set up by Planning Commission to outline the next generation of reforms for the Indian financial sector. The committee recommended: 'Allow more entry to well-governed deposit taking small finance banks offsetting their higher risk from being geographically focused by requiring higher capital adequacy norms, a strict prohibition on related party transactions and lower allowable concentration norms'.[3] As part of the recommendations, the committee very critically noted that inclusion is best served by institutions who see the target segment as business worthy rather than by a public sector-led, mandate-ridden inclusion strategy. Failures of past similar initiatives in the form of LAB and RRB were attributed by the committee to weak governance, interference of the government and delay by the regulator in taking prompt corrective action. This implied that the idea of SFBs has merit provided the causes of failures are addressed. While the geographical risk aspect was dealt by not proposing any area limitation, the committee defined small not by loan size but 'small—because the centre of decision making is close to the loan officer', and added that such banks have to be low cost based on technology. Thus, the proposed SFBs were to be private sector-led, have no geographical limitation, have decentralised decision-making, be low cost and able to offer a full suite of asset and liability products. A model quite suited for the graduation of MFIs, and importantly, these recommendations were made a year in advance of the Andhra Pradesh crisis of 2010 that badly affected MFIs. Later in the report, the committee drops a clear signal that this can be the future of MFIs by saying: 'With the creation of a small bank category, current institutions that operate at a local level—MFIs, community-based lending organisations, etc.—would have the choice of deciding their institutional structures'.

Nothing much happened on these recommendations till 2014 when these ideas resurfaced in the report of the committee on comprehensive financial services for small businesses and low-income households[4] set up by the RBI. Interestingly, Raghuram Rajan who headed the 2009 committee was the governor of the RBI in 2014. While the idea of SFBs as they exist now was not mentioned in the report, the idea of PBs was introduced under the Vertically Differentiated Banking System (VDBS). Both these concepts were covered under the new framework of Differentiated Banking[5] introduced by the committee. As SFBs have no area limitation or service limitation (except on loan sizes) in their current avatar, they logically fit into the Horizontally Differentiated Banking System (HDBS). The report only mentioned the following as part of the HDBS:

- National bank with branches
- National bank with agents
- Regional bank
- National consumer bank
- National wholesale bank
- National infrastructure bank

However, while discussing the concept of regional banks, which as per the committee should have a regional/sectoral focus and not access capital markets for resources, the phrase 'small bank' was used. The rationale for such banks given by the committee was similar to the 2009 committee and it said, 'Regional Banks are likely to process "soft" information for lending better than National banks. However, their local nature also makes them more prone to "capture". To avoid the 'capture', the committee suggested a higher order of regulatory supervision for regional banks. Thus, both committees discussing the idea of SFBs/ regional banks agreed on a few critical things like geographical focus and decentralised decision-making. However, there are also differences. The 2014 committee interestingly noted that regional banks unable to undertake credit function should be turned into PBs.

Finally, when the RBI issued guidelines inviting applications for SFBs in November 2014, the operational framework changed the concept as outlined by the earlier committees in terms of not requiring any geographical focus. The guidelines clearly hinted that the category of SFBs provides NBFC-MFIs an option to graduate to a bank, albeit with some limitations by stating: 'Existing Non-Banking Finance Companies (NBFCs), Micro Finance Institutions (MFIs), and Local Area Banks (LABs) that are owned and controlled by residents can also opt for conversion into small finance banks'.[6] The key business metrics outlined in the guidelines, which remain unchanged are given in Box 7.1.

Box 7.1: Key Features of SFBs as per RBI Guidelines

Minimum Paid up capital of Rs 100 crore.
Prudential norms including SLR and CRR as applicable to Commercial Banks
Extend 75 per cent of its Adjusted Net Bank Credit (ANBC) to the sectors eligible for classification as priority sector lending (PSL) by the Reserve Bank.
At least 50 per cent of its loan portfolio should constitute loans and advances of up to Rs. 25 lakh.
Branch expansion in initial five years to require RBI approval.
Objectives- shall primarily undertake basic banking activities of acceptance of deposits and lending to unserved and underserved sections including small business units, small and marginal farmers, micro and small industries and unorganised sector entities.

Source: https://rbi.org.in/Scripts/bs_viewcontent.aspx?Id=2901. Accessed on 26 September 2018.

The guidelines clearly mentioned two things: (i) though there is no geographical limitation on operational area, preference will be given to those applicants who in the initial phase set up the bank in a cluster of underbanked states/districts, such as in the northeast, east and central regions of the country; and (ii) there is a need for SFBs to be responsive to local needs. The focus on small amount of loans is evident from the fact that 50 per cent of lending has to be below Rs 25 lakh, as also is the focus on priority sector by prescribing a higher requirement of 75 per cent as against 40 per cent for commercial banks. It is inferred by reading through the objectives in the guidelines and lending restrictions that the policy intent was to have SFBs as more of micro- and small-enterprise (MSE) lenders in relatively financially excluded parts of the country—moving up from microfinance lending. The list of ten entities granted in-principle approval showed the tilt towards NBFC-MFIs, as eight entities were NBFC-MFIs.

While introducing the concept of PB, the 2014 committee's suggestions, unlike SFBs, mirror the structure of PBs as they operate now. The committee observed that PBs should provide payments and deposit services but not credit and should hold some combination of SLR (statutory liquidity ratio) and CRR (cash reserve ratio) with the RBI. The idea of PBs was mooted as part of moving away from prepaid instrument (PPI) providers and shortcomings like the inability to provide cash-out services and interest on deposits of PPIs. On the question of viability of this business model, which as per the committee is only existent in Brazil, it cryptically noted that 'the discussions of the Committee with existing providers suggest that with adequate regulation, the market will be extremely competitive with participation from big and small players'. The licensing guidelines, which remain unchanged outlined the scope of business (Box 7.2).

Box 7.2: Key Features of PBs as per RBI Guidelines

Minimum Paid up capital of Rs 100 crore.
Business – a) acceptance of demand deposits up to Rs 1 lakh per customer b) issue of ATM & debit cards c) payments and remittance services d) can become Business Correspondent of another bank and d) distribution of no risk sharing simple financial products like mutual funds and insurance

Besides CRR, hold 75% of its 'demand deposit balances' in SLR eligible Government securities/ treasury bills with maturity up to 1 year and hold maximum 25% on time/fixed deposits of other scheduled commercial banks

Source: https://rbi.org.in/Scripts/BSs_PressReleaseDisplay.aspx?prid=3261501. Accessed on 20 September 2018.

Eleven entities were granted in-principle licences, which comprised of mobile phone operators, the Department of Post and NBFCs.

How Has Differentiated Banking Evolved Since In-Principle Approval?

Since September 2015, when in-principle licences were awarded to both SFBs and PBs, the evolution has been different across these entities. While as of September 2018 all ten SFBs have commenced operations, in the case of PBs only six have started functioning. The operating landscape for PBs has also changed in these years with the spread of BCs (as reported in chapter 3, there are nearly 6.4 lakh BCs on a conservative count), the ubiquitous coverage of bank accounts under the PMJDY and the spread of the UPI and the AEPS. More importantly, the recent regulatory move to allow PPIs interoperability is likely to impact PBs. These measures put together have solved the payments side of financial inclusion and in the process dented the business case of PBs. The later part of this chapter details as to what has been the key strategy adopted by PBs which are operational, but it remains to be seen as to how they will cope with the PPI interoperability challenge. Broadly speaking, while deposit mobilisation has not been a key priority—with a recent newspaper report indicating that the total deposits collected by Airtel PB, Fino, Paytm and IPPB is a mere Rs 540 crore[7] —the focus has been on payments and third-party products either on a fee basis or as a BC of a bank. The viability aspect cannot be commented upon as financial statements of PBs are not available in the public domain and the RBI report on trends and progress in banking for 2017–18 as well as banking statistical returns for 2017–18 are due in December 2018. In view of this, coupled with the reluctance of PBs to provide operational and financial data, the discussion on PBs is based on information gathered through personal interaction, discussion with industry, secondary sources—website and media reports as well from the roundtable of PBs organised by Access Assist in April 2018. Overall, PBs continue to struggle for a viable business model, and more importantly, their contribution to financial inclusion of the excluded remains to be seen.

In contrast, all SFBs already had a business model and have continued without major changes to business. While North East SFB (erstwhile RGVN) and Janalakshmi SFB commenced operations in June and July of 2018 respectively, the other eight SFBs have now a vintage ranging from 2 years to 1 and 1½ years. Capital LAB was the first to commence operations in April 2016 followed by Equitas SFB in September 2016. The remaining six started operations in 2017 ranging from January 2017 (Utkarsh) to September 2017 (FINCARE). As such, SFBs are also more of a work in progress, but because of their earlier established business there has not been much of an issue in transition as a SFB. Though issues like deposit mobilisation, cost implications of investment in technology, HR issues and questions on ability to change the business model to enterprise financing have emerged following their transition into a bank.

While SFBs being of recent origin need time to establish themselves, a review of their business operations brings out three major patterns, while the issues mentioned above are common. In terms of business, there are three distinct patterns. Among the six erstwhile NBFC-MFIs which transitioned into SFBs (leaving North East and Janalakshmi SFBs aside as they are in their first six months), Utkarsh, Ujjivan, Suryoday, ESAF and FINCARE continue to be focused on microfinance with the microfinance portfolio making up for nearly 85 per cent of their loan book. Efforts to diversify are visible but yet to fructify, and to be fair it is too early for them to demonstrate a changed loan book. Diversification has also been constrained by the impact of demonetisation as NBFC-MFIs which transitioned into SFBs continued to bear its adverse effect in 2017–18. The period 2018–19 should be different and they should be able to more clearly demonstrate their intent. This group of SFBs also exhibits a similar strategy on deposit mobilisation, that is, having exclusive liability branches while erstwhile microfinance branches continue to be primarily asset branches. Considering the need to replace earlier bank borrowings by deposits within a timeline, the strategy makes sense. It seems to have been realised that microfinance borrowers will not be able to fund the replacement leaving aside growth. The model of Equitas differs, as even as an MFI it had started diversification through its other companies—Equitas Finance for vehicle finance and housing finance. As a result of aggressive diversification, its microfinance business now comprises only 28 per cent of the total loans and advances as of 31 March 2018.[8] However, on the deposits side, it follows the other five SFBs by having liability-focused branches. Finally, Capital SFB and AU SFB—the non-MFI entities—have continued to build on their previous business model. The difference is that Capital SFB being a LAB before has experience of deposit mobilisation, while AU has ventured into deposit mobilisation post-SFB.

The second pattern that emerges among SFBs who transitioned from NBFC-MFIs is that the impact of demonetisation did impact operations in 2017–18. Ujjivan's loan book grew from Rs 6,379 crore as of 31 March 2017 to Rs 7,560 crore as of 31 March 2018, but its net profit fell from Rs 208 crore to Rs 7 crore in 2017–18 mainly on account of higher provisioning and write off.[9] Similarly, Utkarsh's loan book grew almost 50 per cent to reach Rs 3,082 crore as of 31 March 2018 but it recorded a loss of Rs 63 crore on account of provisioning and write-off totalling Rs 170 crore.[10] Now that the impact on credit quality is behind these SFBs and they also have gained experience of banking operations and their concomitant challenges, the year 2018–19 will be an interesting one.

As the data available from the RBI for SFBs as of September 2018 is of March 2017, the discussion of SFBs in the chapter is based on data and information collected from SFBs by the author, annual reports wherever available, the roundtable for SFBs organised by Access Assist and Mint, and interaction with key personnel of SFBs. The focus is on describing the three distinct models seen as of now through a few institutional stories, and in the end discussing the challenges going forward rather than a detailed description of each SFB.

Urban Cooperative Banks as SFBs: Possible New Entrants

Before SFBs could stabilise and demonstrate the usefulness of their banking status, the RBI has opened up a window for urban cooperative banks (UCBs) to voluntarily apply for licensing as SFBs, vide its circular dated 27 September 2018.[11] The scheme is in pursuance of the recommendations of the high powered committee on UCBs chaired in 2015 by R. Gandhi, the then deputy governor of the RBI, which had recommended the voluntary conversion of large multistate UCBs into joint stock companies and other UCBs which meet certain criteria into SFBs. As per the scheme, the following basic criteria has been mentioned for UCBs to be eligible for conversion:

1. UCBs with a good track record shall be eligible to voluntarily transit into an SFB. Promoters shall incorporate a public limited company under the Companies Act, 2013 having the word 'bank' in its name after receiving the in-principle approval from the RBI.
2. The board of directors of the company shall have required experience and shall meet the RBI's 'fit and proper' criteria. The above company shall enter into an agreement with a UCB for transfer of assets and liabilities to be executed at a future date (after issuance of the SFB licence).
3. The SFB commences operations with a minimum net worth of Rs 1 billion and minimum promoters' contribution of 26 per cent of the paid-up equity capital.
4. The UCB will surrender its banking licence to the RBI. The resultant cooperative society will be wound up in due course.
5. UCBs with a minimum net worth of Rs 500 million and maintaining CRAR of 9 per cent and above are eligible to apply for voluntary transition to an SFB under this scheme.

As per the RBI, there were 54 scheduled UCBs as of 31 March 2017, of which only 4 reported losses during 2016–17. Profitability measured as net profit as percentage of total assets of 54 UCBs ranged from (–)9.6 per cent to (+) 1.5 per cent, with only 10 UCBs having a ratio more than 1 per cent.[12] Other than scheduled UCBs, there are 1,508 non-scheduled UCBs.

As can be seen in Figure 7.1, of the 54 scheduled SCBs, only 31 are multistate. Though, the RBI scheme does not mention it, it can be assumed that scheduled UCBs will be given priority for conversion into SFBs. The dominance of scheduled SCBs is apparent from the fact that despite being only 3.5 per cent of the total UCBs, their share in assets is 47 per cent.

Though in recent years operations of UCBs have improved by way of amalgamation and mergers, the RBI has not been issuing fresh UCB licences for some time and this has led some commentators to question the stance of the RBI. Over the years operations of UCBs have grown steadily (Table 7.1).

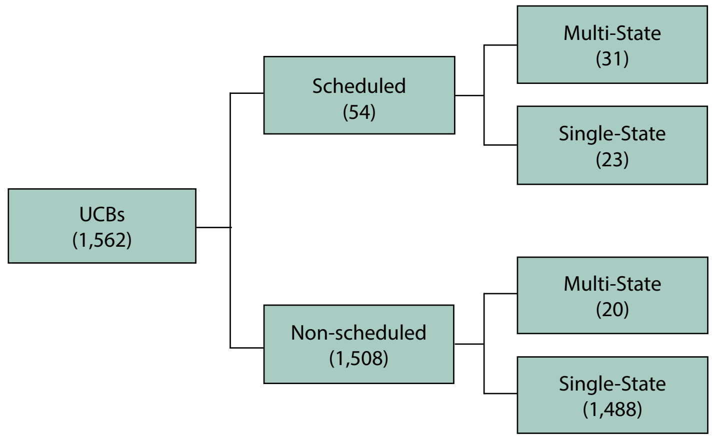

Figure 7.1: Landscape of UCBs

Source: Reserve Bank of India, Trend & Progress of Banking in India, 2016–17 (Mumbai: RBI, 2017)

By allowing the path to conversion as SFBs, the RBI has now opened up an avenue for UCBs to grow under the direct supervision of the RBI. While the scheme has come out recently and is voluntary in nature, it is worthwhile to see the performance of UCBs against the required CRAR of 9 per cent to apply for transition. The financial stability report of the RBI for June 2018 observes that 'At the system level, the CRAR of scheduled urban co-operative banks (SUCBs) remained unchanged at 13.6 per cent between September 2017 and March 2018. However, at a disaggregated level, CRAR of four banks was below the minimum required level of 9 per cent'.[13] Thus, out of 54 scheduled UCBs, 50 pass the CRAR requirement for conversion into an SFB. More detailed information covering all UCBs available for March 2017 also shows a comfortable position.

Table 7.1: UCBs in the Recent Years

Year	No. of UCBs	Deposits (in Rs billion)	Advances (in Rs billion)
2012	1,618	2,386.41	1,577.93
2013	1,606	2,768.30	1,810.31
2014	1,589	3,155.03	1,996.51
2015	1,579	3,551.35	2,251.06
2016	1,574	3,922.00	2,450.00
2017	1,562	4,434.77	2,612.30

Source: Reserve Bank of India, Primary (Urban) Co-operative Banks Outlook (Mumbai: RBI, 2018).

Table 7.2: CRAR-wise Distribution of UCBs, end-March 2017

CRAR (in per cent)	Scheduled UCBs	Non-scheduled UCBs	All UCBs
<3	4	110	114
3 <=CRAR <6	0	9	9
6<=CRAR <9	1	8	9
>9	49	1381	1,430
Total	54	1,508	

Source: Reserve Bank of India, Trend & Progress of Banking in India, 2016–17 (Mumbai: RBI, 2017)

What are the pros and cons of becoming an SFB for a UCB?

As the scheme has come out recently, there has not been much discussion on what the pros and cons will be for UCBs turning into SFBs. An analysis of the operations of UCBs vis-à-vis the regulatory guidelines for SFB show some significant pros and cons. The biggest positive under the SFB structure will be doing away with the dual regulation of the RBI and the registrar of cooperative societies at the state level. Aligned to this will be the freedom to operate without any geographical limitation as at present even among scheduled UCBs nearly 45 per cent have single state operations, and the ability to tap capital markets as against current reliance on capital from customers.

However, the SFB form also offers its set of challenges. At present, UCBs are required to have a minimum CRAR of 9 per cent, but as an SFB they will be required to have a higher CRAR of 15 per cent. As an SFB, UCBs will lose the flexibility to operate specialised branches as well as undertake foreign exchange business, which might not go down well with bigger UCBs like Cosmos, Saraswat and Shamrao Vithal Bank. In terms of business, the other challenge apparently is larger requirement of priority sector advances at 75 per cent as an SFB, while as UCBs they have to comply with 40 per cent PSL. Sector-level data for March 2017

Table 7.3: Composition of Priority Sector Credit by UCBs, March 2017

Item	Priority sector advances	
	Amount (in Rs billion)	Share in total advances (in per cent)
1	2	3
1. Agriculture credit	76	3.0
1.1. Direct agriculture credit	32	1.2
1.2. Indirect agriculture credit	44	1.7
2. Micro- and small-enterprises	732	28.0
2.1. Direct credit to SMEs	576	22.1
2.2. Indirect credit to SMEs	156	6.0
3. Micro-credit	108	4.1
4. State-sponsored organisations for SCs / STs	2	0.1
5. Education loans	22	0.8
6. Housing loans	253	9.7
7. Total (1 to 6)	1192	45.6
Of which advances to weaker sections	271	10.4

Notes:
1. Data for 2017 are provisional.
2. Percentages are with respect to total credit of UCBs.
3. Components may not add up to total due to rounding off.

Source: Reserve Bank of India, Trend & Progress of Banking in India, 2016–17 (Mumbai: RBI, 2017) shows that UCBs fall woefully short in this aspect (Table 7.3).

It is likely that there are a few institutions having higher PSL but 45.6 per cent at the sector level shows that the product focus of UCBs becoming SFBs has to undergo a drastic change. However, the silver lining is that MSEs' loans constitute 28 per cent of the UCBs' loan book and there are immense opportunities for scaling it up as an SFB without geographical limitation. In order to boost UCBs' PSL, the RBI has since April 2016 allowed 'financially sound' UCBs with a priority sector loan portfolio not less than 90 per cent of their gross loans to grant unsecured advances to the extent of 35 per cent of their total assets (beyond the extant ceiling of 10 per cent of total assets as per audited balance sheets as of 31 March of the previous financial year). UCBs' contribution to financial inclusion measured as advances to weaker sections also shows a weak performance in March 2017 at 10.4 per cent of total advances—it has remained at this level over the last five years.

The bigger UCBs might also think of the SFB structure as limiting and may want to go directly to the universal bank category; the lack of clear evidence on the performance of the first batch of SFBs might further dampen the enthusiasm. A newspaper report quoting the CEO of a large UCB and other experts mentions that the SFB route may be more appropriate for mid-sized UCBs and the need to provide more incentives for transformation.[14] Next year by this time, the import of this scheme will be visible depending on the number of applications, and within that, on those who meet the eligibility criteria. By doing this, the RBI has ended the speculation on the future roadmap of UCBs, but at the same time opened up questions on whether it is not too early to expand the SFB category.

THE THREE DIFFERENT BUSINESS STRATEGIES OF SFBS: WORK IN PROGRESS

The above section briefly mentioned three distinct business strategies among SFBs and this section details them through institutional case studies.

The Microfinance-Focused SFBs: Ujjivan and Suryoday

Ujjivan

Ujjivan started operations as an SFB in February 2017. Before that it was one of the leading NBFC-MFIs in India having an on-book portfolio of Rs 5,389 crore with operations in 24 states. As of March 2018, it has completed 14 months of operation as an SFB, and importantly, a full financial year. Ujjivan had set five challenges before itself for FY 2017–18:[15]

- Overcome the impact of demonetisation: clean up the bad book
- Build the infrastructure and the people for the future
- Build the deposit business and replace high-cost borrowings we inherited
- Recharge the engines of the existing asset business
- Contain the cost and improve the productivity to close the year in the black

Demonetisation impacted profitability and branch expansion

In short, the challenges mentioned capture strategic issues faced by all SFBs, especially those who transformed from being an NBFC-MFI. While coping with the impact of demonetisation can be seen as a temporary phenomenon, the challenge of mobilising deposits to replace borrowings, building branch network, IT infrastructure and people as well as diversifying the lending portfolio are the key challenges. Ujjivan's strategy and performance on these throw useful insights into the performance of SFBs as well as the challenges faced by them. The impact of demonetisation was felt mainly in Uttar Pradesh, Maharashtra and Karnataka by Ujjivan. As recovery efforts did not yield much due to the vitiated credit culture, Ujjivan had to resort to a write-off and incremental provisions. It did a huge write-off of Rs 176 crore and made additional provisions of Rs 135 crore. On account of this abnormal credit cost, Ujjivan ended the year 2017–18 with a marginal profit of Rs 7 crore but the PAR reduced from Rs 650 crore (10.8 per cent) in March 2017 to Rs 341.5 crore (4.1 per cent) in March 2018. The fact that it was able to ride through the crisis and the year profitably with a strong CRAR of 23 per cent against the prescribed 15 per cent is a testimony to its resilience. The other comforting factor is that its fresh loans post-demonetisation have recorded around a 99 per cent recovery rate—similar to pre-crisis levels.

Reliance on wholesale institutional deposits

Establishing banking outlets and mobilising deposits to replace borrowings was another challenge faced by Ujjivan. In addition to its existing branches, Ujjivan by the end of March 2018 set up 187 banking outlets, of which 47 are in unbanked rural centres (URCs) and it plans to take the number of banking outlets to 475 by the end of March 2019. As discussed in section 2, the deposit mobilisation strategy has centred around 187 banking outlets, while the earlier microfinance branches focus on the core business of microfinance. Deposit mobilisation efforts were backed by offering higher rates on fixed deposits like other SFBs but Ujjivan adopted a different strategy for savings deposits by keeping interest rates at 4 per cent per annum in line with bigger commercial banks. With these, Ujjivan was able to raise Rs 3,772 crore of deposits by March 2018 which enabled it to reduce legacy borrowings from Rs 5,089 crore at the start of the year to Rs 2,325 crore by March 2018. The composition of deposits shows that retail deposits—the true measure of financial inclusion—contributed a meagre 11 per cent to the deposit base, with 31 per cent coming from institutional deposits and 58 per cent from certificates of deposit (CDs). As per Ujjivan's annual report, the focus during the year was not on retail deposits as there was a slowdown in opening of branches and technology glitches in onboarding microfinance customers. Focus was on wholesale deposits for volume to reduce the grandfathered (inherited from NBFC-MFI) borrowings.

Further breakdown of the composition shows that the share of term deposits is very high at 91 per cent (per cent of retail plus institutional deposits), which resulted in a small reduction in COF to 9 per cent by March 2018 from the earlier 10.4 per cent. Data for all SFBs as of 31 March 2017 available from the RBI shows that term deposits accounted for 70.3 per cent of total deposits. On deposit-related technology, Ujjivan has developed a handheld device (Evolute), which enables its staff to open accounts, take deposits and do withdrawals at customers' doorstep, and it is claimed that the account-opening process takes less than 10 minutes. It has also developed a mobile-banking application, which has a user base of 24,000 and high user ratings. These steps are supplemented by internet banking and 146 biometric-enabled ATMs. Details of Ujjivan's IT framework and initiatives are given in Annexure 7.1. The moot point for the future from a financial inclusion perspective is whether the bank will be able to tap a significantly larger percentage of retail deposits, which will also lower its COF.

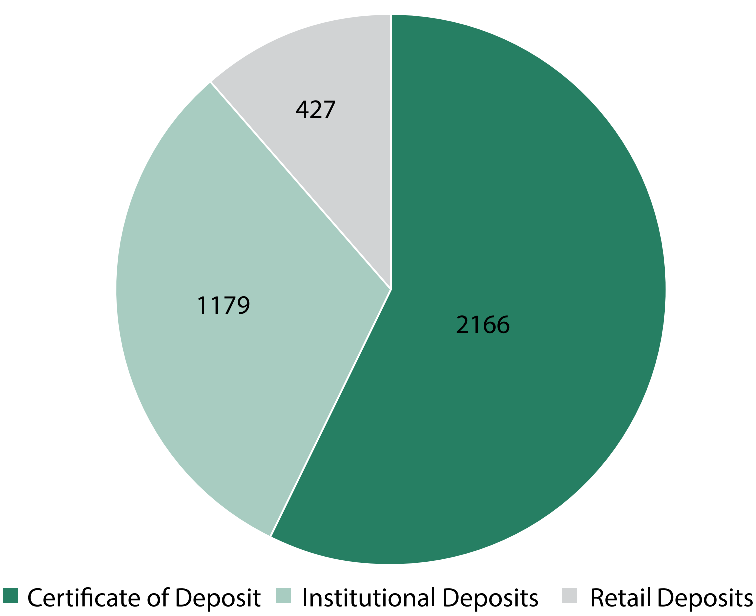

Figure 7.2: Break-Up of Ujjivan's Deposits, March 2018 (in Rs crore)

Source: Data provided by Ujjivan to author.

Lending: Diversification yet to become substantial

At present, Ujjivan broadly offers three types of loans—microfinance (group and individual), home loans and MSE loans. Other than microfinance loans, within both housing and MSE loans, there are different product types. For example, MSE has both unsecured loans (ranging from a loan amount of Rs 3 lakh to Rs 7.5 lakh) and secured loans (ranging from Rs 10 lakh to Rs 50 lakh) as well as an overdraft facility. As SFBs were expected to move up from microfinance and cater more to MSEs, referred to as the 'lost middle' between banks and MFIs in chapter 4, the performance under this is of special importance. Analysis of Ujjivan's loan book for March 2018 shows that microfinance continues to account for 84 per cent of the business. Building on microfinance, under which disbursements grew by 8.6 per cent in 2017–18, Ujjivan was able to add 7.6 lakh new customers during the year taking the total customer outreach to 35.7 lakh borrowers by March 2018. Microfinance loans below Rs 50,000 had a dominant share of 83.76 per cent in the loan portfolio.

The other verticals of MSE and housing loans recorded a much higher growth of 300 per cent and 225 per cent, respectively during the year 2017–18, showing the intent of Ujjivan. But considering their negligible base, their combined contribution to the loan book remains low at 7.25 per cent (Figure 7.3). As a strategy, Ujjivan in the coming days wants to focus on these segments, and their present low contribution is acknowledged by the MD in his note in the annual report by saying: 'Two businesses have gone through a long incubation period: Micro

& Small Business and Housing over last two years. We brought in new leadership for both businesses and built the team around them so that they start ramping up business'.[16] In the near future, Ujjivan plans to significantly expand its MSE distribution as more bank branches are launched. In operations, the focus will be on improving turnaround time for loan processing through the loan origination system (LMS) and offering a complete suite of banking solutions to MSE customers. Ujjivan sees the introduction of the GST as a temporary blip as its MSE business picked up in the second quarter of FY 2017–18. Under housing loans, Ujjivan wants to reach a customer base of 12,000 by the end of March 2019 by focusing more on the semi-formal segment over the informal segment on account of formalised income. It also has plans to build its rural business with specialised agriculture and allied agriculture products through URC banking outlets and also existing banking outlets with a large rural customer base.

Cost of credit: The MCLR continues to be high, impacting interest rates

Along with mobilisation of deposits from customer, and lending diversification, commentators had also expected that with retail deposits lowering cost of funds, lending rates would come down. This aspect like others will also take time as despite reduction in the COF

(Ujjivan's COF was 9 per cent as of March 2018), the MCLR of SFBs remains high. In the case of Ujjivan, the MCLR range is between 14.80 per cent and 16.20 per cent. Compared with ICICI Bank, whose MCLR ranges between 8.05 per cent and 8.40 per cent, it appears very high. Interaction with SFBs showed that while the COF is one factor which will

Table 7.4: Ujjivan's MCLR w.e.f. 20 September 2018

Benchmark tenor	Benchmark rate per annum (in per cent)
Overnight	14.80
One month	15.00
Three months	15.20
Six months	15.50
One year	15.80
Two years	16.20
Three years	16.20

Source: Ujjivan SFB, 2018. https://www.ujjivansfb.in/pdf/MC-LR-rate.pdf. Accessed on 24 September 2018.

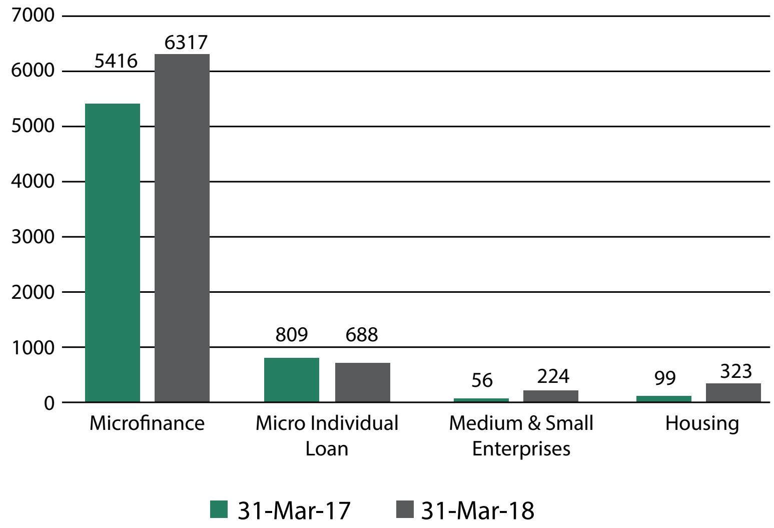

Figure 7.3: Loan Portfolio of Ujjivan (in Rs crore)

Source: Ujjivan SFB, Annual Report, 2017–2018 (Bangalore: Ujjivan SFB, 2018).

further reduce with favourable CASA, the present high MCLR is on account of high operational costs—which in turn is on account of big investments made in technology and branch expansion as an SFB.[17] At present, Ujjivan's unsecured MSE loans are priced at 21–23 per cent per annum, secured MSE loans at 14–17 per cent per annum and microfinance group loans at 21.25 per cent per annum.

In short, the experience of Ujjivan as an SFB so far can be said to be going through challenges of mobilising retail deposits, converting microfinance branches for deposit mobilisation, technology and higher regulatory compliance cost, diversification of the loan portfolio from almost 90 per cent share of microfinance, and reducing the lending rate progressively. It must be reiterated that it is still early days and the next two to three years will show the right picture. The story of Ujjivan, however, mirrors the current state of other microfinance-focused SFBs.

Suryoday SFB: A smaller but similar story with a different deposit mix

While Suryoday is much smaller in asset size compared to Ujjivan, with a loan book of Rs 1,575 crore as of March 2018, its profile as an SFB exhibits a similar model and challenges. Suryoday operates in seven contiguous states of Gujarat, Madhya Pradesh, Chhattisgarh, Odisha, Maharashtra, Karnataka and Tamil Nadu through 215 erstwhile microfinance branches, now called doorstep service centres, and 26 banking outlets. During the year 2017–18, it opened 22 bank branches, taking the total to 26 by March 2018, of which the majority (17) are in Maharashtra. The network operates similar to Ujjivan with 26 bank branches being the deposit mobilisation network as doorstep service centres have not yet started their liability business and the bank feels that for that to happen its systems have to stabilise and be strengthened for the tablet-based account opening and savings IT system.

Against a loan book of Rs 1,575 crore, Suryoday in a short span of time has been able to mobilise deposits of Rs 830 crore. Compared to Ujjivan, its deposit mix is different primarily due to a much lower share of CDs at 3.54 per cent and a larger share of retail deposits at 41 per cent.

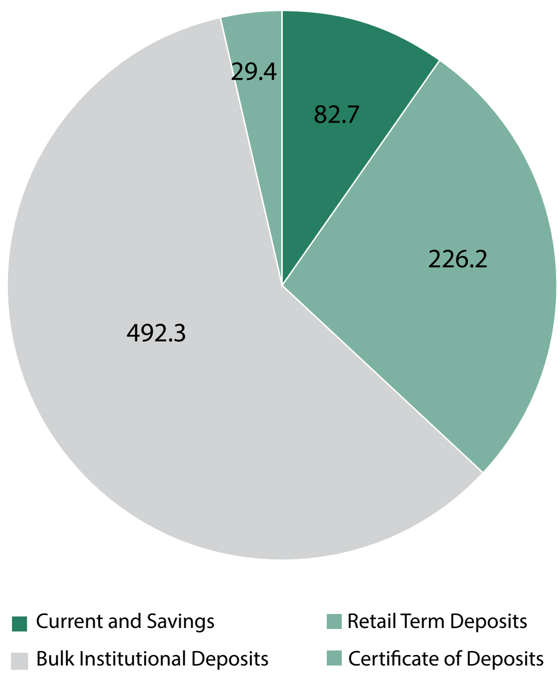

Figure 7.4: Suryoday's Deposit Break-Up, March 2018 (in Rs crore)

Source: Data provided by Suryoday to author.

Discussions with Suryoday's MD and CEO and other senior functionaries brought out the fact that as Suryoday has A1 credit rating for CDs, there were limitations in mobilising CDs and the bank had to rely on strategy building on retail and institutional bulk deposits. The balance of funding has been mainly met through capital, NCDs (Rs 311 crore) and grandfathered loans[18] (Rs 374 crore).

On the asset side, the product suite of Suryoday mirrors Ujjivan's. Besides microfinance loans, it offers MSME loans, home loans, loan against property and commercial vehicle loans. In addition to these products, Suryoday also has a Financial Intermediary Group (FIG) loan which is for wholesale lending to NBFCs as well as NBFC-MFIs. The product side is broadly divided into two segments—inclusive banking and retail assets (See Annexure 7.2 for product details). Inclusive banking includes the typical microfinance JLG loan and Vikas loan—a larger sized loan (Rs 30,000 to Rs 1 lakh) to microfinance clients who have completed two JLG loan cycles and individual loans to microfinance clients called MSME (micro). The inclusive banking segment constitutes 90 per cent of the total loans managed by the company (on-book plus off-book) as of 31 March 2018. JLG loan and Vikas loan together account for 88.5 per cent of total loans outstanding. New loan products clubbed under retail assets have a mere 10 per cent share, which points to future work for the bank.

Suryoday's MCLR ranges between 13.98 per cent (overnight tenure) and 14.22 per cent (two-year tenure), which is lower than Ujjivan but higher than commercial banks. Suryoday's rate of interest on its main loan product—microfinance—was 25.4 per cent in March 2018. This shows the impact of transformation cost on a rather small balance sheet size. Future challenge for Suryoday also lies in mobilising retail deposits especially from its traditional microfinance client base, diversification of loan portfolio to have a proper mix of secured and unsecured loans, and reduction in lending rates. R. Baskar Babu, MD and CEO of Suryoday, observed that over the next two years the share of joint liability-based microfinance loans will be around 60–70 per cent of the total AUM as the bank will grow its secured loan book under the retail assets segment.

Equitas' Diversified Business Strategy

Before converting into an SFB in 2016, Equitas was a diversified group with three companies having different operations in microfinance (Equitas Microfinance), vehicle finance/other MSME loans (Equitas Finance) and housing (Equitas Housing Finance). It started with microfinance in 2007 but added vehicle/asset finance and housing finance subsidiaries four years later in 2011. With the setting up of the SFB it was able to bring all these together, which gave it an advantage over other microfinance-focused SFBs in terms of diversification, and it has continued to push for diversification post-SFB also. The diversification strategy even before becoming an SFB is borne out of the belief that there should not be too much portfolio concentration risk as also the fact that there are various untapped business segments beyond microfinance. Equitas was one of the first SFBs to commence operations in September 2016. It also successfully did its IPO.

Deposit mobilisation: Similar strategy[19]

Before discussing its current business mix, it is useful to see Equitas' branch network and deposit mobilisation. While there are differences in the lending business from other microfinance-focused SFBs, the deposit strategy of Equitas is similar. While 597 centres or branches called 'asset branches' are spread across 12 states and 2 union territories, there are 392 bank branches across 13 states and 2 union territories that focus on liability products and also generate leads for the asset branches. Equitas plans to adopt a hub-and-spoke model for liability branches with hubs being physical upmarket branches having spokes in the form of BCs.

Since starting banking operations in September 2016 the bank has built a strong network of 392 banking outlets and 321 ATMs/cash recycler machines (CRMs) spread for deposit mobilisation. It offers a suite of digital banking services like internet banking, mobile banking, digital wallet, FASTag, UPI, Bharat Bill Payment Services (BBPS) and National Automated Clearing House (NACH). Equitas has also, in the process of replacing borrowings with deposits, focused on customers other than the ones served through asset centres, and a statement to this effect was made in its annual report for 2017–18, which said: 'Our major focus is on mass and the mass-affluent segment of the population for mobilising deposits and liability accounts.'

> Though Equitas has a deposit customer base of 2.83 lakh customers, the share of retail household deposits in total deposits continues to be low at 38 per cent as of March 2018. The challenge being faced by other SFBs in mobilising retail deposits is also present for Equitas, despite it being more successful in doing so.

Equitas has seen a healthy quarter-on-quarter growth of 28 per cent in customer deposits (defined as a total of current account, savings account and term deposit balances) reaching a total deposit base of Rs 4,764 crore. To put in context, the total asset size of Equitas SFB as of March 2018 was Rs 13,495 crore. Its CASA has improved from 18 per cent in Q4 2017 to 34 per cent in Q4 2018 and this resulted in a steady fall in the cost of customer deposits to 6.5 per cent and the overall COF to 7.6 per cent in FY 18.

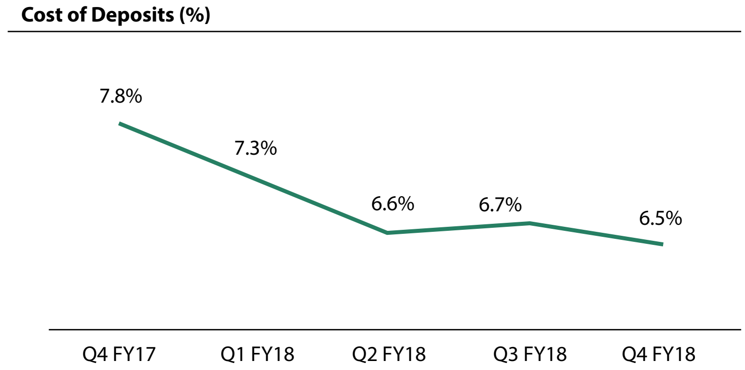

Figure 7.5: Equitas' Cost of Deposits Over the Years

Source: Investor presentation of Equitas Holdings Limited, Q4 FY18 and FY18. https://www.equitas.in/holdings-details.php?category=Cw&section=Dg. Accessed on 20 July 2018.

Retail customer deposits and institutional deposits put together make up about 45 per cent of the borrowing pool of Equitas as of end March 2018, the other coming from a mix of refinance, debentures, certificates of deposit, etc. (Figure 7.6).

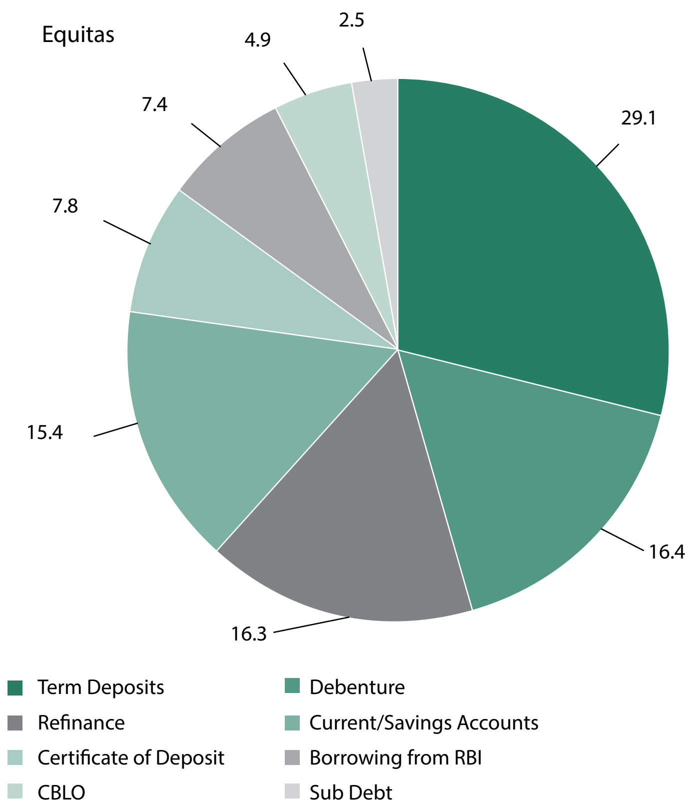

Figure 7.6: Borrowing Profile of Equitas (in per cent)

Source: Investor presentation of Equitas Holdings Limited, Q4 FY18 and FY18. https://www.equitas.in/holdings-details.php?-category=Cw&section=Dg. Accessed on 20 July 2018.

The borrowing profile of Equitas is well diversified as compared to other SFBs and seen with Ujjivan and Suryoday shows how SFBs have tried to meet their liability requirements. While each has its own mix based on its options, the common point is that deposit mobilisation is focused on new banking branches opened mainly in urban centres. It is evident that only after meeting the liability requirements and getting the technology right will these SFBs venture into deposit mobilisation through asset centres. This reflects the general perception among SFBs that their traditional low-income clients as captive customers can only contribute to a small part of their liability requirement.

Though at present Equitas feels that the profile of its asset and liability customers does not overlap much, going ahead Equitas has taken approval to undertake liability business from asset centres. It plans to start with piloting it in a few branches rolling out deposit services for asset customers through the asset branches where it believes that the cost of servicing such deposit customers would be very marginal, and if it works well it will be expanded.[20]

Loan portfolio: Diversification based on pre-SFB legacy

Equitas has 597 asset centres that do the lending and liability centres that provide business leads to them—the objective being to provide asset products to liability customers. The following business divisions handle the advances portfolio of the bank. The business divisions have been created based on the similarity of the customer profile served.

A typical asset branch has three assistant branch managers who look after different portfolios—microfinance (loans below Rs 35,000 based on group concept), micro (loans from Rs 50,000 to Rs 5 lakh) and retail (loans from Rs 5 lakh to Rs 25 lakh). Vehicle finance has different branches and CSME requirements are at present handled from the head office in Chennai.

The product-wise break-up (Figure 7.7) shows that the orange-coloured bars (representing legacy diversification) account for 87 per cent of the portfolio and recently introduced products (in blue) form 13 per cent. It is notable that Equitas started as a microfinance company but over the years its focus on diversification has reduced the share of microfinance to about 28 per cent. During 2017–18, Equitas was not only impacted by demonetisation-induced delinquency but also consciously decelerated its microfinance portfolio—microfinance constituted a 46 per cent share in March 2017. Though even at 28 per cent portfolio share Equitas services around two million clients.

Table 7.5: Equitas' Diversified Loan Products and Business Divisions

Business divisions	Product offerings
Agri, Micro Enterprise & Inclusive Banking	Micro Finance, Micro Loan against Property, Agricultural loans, Small Business Loans and Affordable Housing Micro Finance [MF] and Micro Loan against Property [M-LAP] are products on offer for the last 11 and 6 years' respectively while Agriculture loan was introduced in FY 2016-17. M-LAP is also targeted at MSEs Home loans also come under this and are targeted at Affordable housing segment. The normal loan sizes are in the range of Rs1 -5 lakh for the Economically Weaker Sections segment of borrowers while it is Rs 5 – 100 lakh for other segments.
Emerging Enterprise Banking	Commercial vehicle finance, including used vehicles Targeted at customers, who have been drivers of commercial vehicles and who desire to turn owners, by providing them with the capital required to buy their first used commercial vehicle [UCV]. UCV finance has been on offer by the bank for the past 7 years, in 2017-18 product for purchase of new vehicles was also introduced
Business Banking	Business and working capital loans to Micro and Small Enterprises Secured and unsecured working capital and term loans to MSEs. The average loan sizes range normally between Rs10 – 200 lakh. Introduced after becoming SFB
Outreach Banking	Business Correspondent Channel, offering both liabilities and advances Equitas by March, 2018 had 16 Individual BCs.
Corporate Banking	Banking solutions to emerging corporates

Source: Equitas Annual Report, 2017–18 (Chennai: Equitas, 2018).

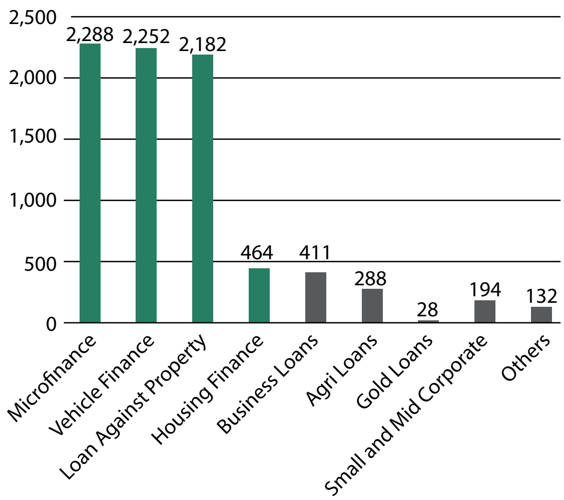

Figure 7.7: Equitas SFB: Product-wise Break-up of Loan Portfolio (On+Off Book), March 2018 (in Rs crore)

Source: Investor presentation of Equitas Holdings Limited, Q4 FY18 and FY18. https://www.equitas.in/holdings-details.php?-category=Cw&section=Dg. Accessed on 20 July 2018.

Going forward, Equitas wants to accelerate MSE loans, meaning business loans, working capital loans and term loans for MSEs. The loan sizes typically should be in the range of around Rs 10 lakh to Rs 50 lakh and maybe Rs 50 lakh to Rs 1 crore with an average loan size anywhere in the range of Rs 30 lakh, Rs 40 lakh and Rs 50 lakh.[21] It is now more or less two years since the launch of Equitas SFB and it seems well poised for diversification. The RBI guidelines stipulating 50 per cent of loan portfolio being of loans less than Rs 25 lakh will ensure that the focus remains on the lost middle. By March 2018 loans below Rs 2 lakh—typical financial inclusion loans—constituted 41 per cent of the portfolio, which implies smaller-sized loans even in segments other than microfinance.

Interest rates: Show a declining trend

Equitas prides itself on being one of the most cost-effective institution for clients even before being an SFB—its website says Equitas started the microfinance business with an interest rate of 25 per cent per annum when the rates in the industry were in the range of 35 per cent to 40 per cent.[22] The philosophy was not to burden customers with the initial higher cost of operations and in the process its acceptance of a longer break-even period. At present, its rate of interest varies as per the product: microfinance loans are priced at 18 per cent per annum, business loans at 18 per cent per annum, gold loans have a range of 12–14 per cent with gold loans for agriculture at 12 per cent, micro loan against property and agriculture loans are in the range of 12–24 per cent. As in the case of other SFBs mentioned above, Equitas' MCLR is in the range of 14.25 per cent (overnight) to 15.95 per cent (one year)[23] despite a low COF at 7.6 per cent. However, since Q4 2017 (January–March 2017) the yield on advances is gradually coming down (Figure 7.8). The overall effective interest rate would be a little higher, as in FY 18 the vehicle finance segment had a 4.9 per cent gross NPA and the mortgage segment (micro LAP) had a 2.9 per cent gross NPA.

Equitas building on its legacy provides an interesting example of product diversification and change in the business model post-SFB in full. Like others, while its business success will depend on expanding the business loan portfolio and other new products and mobilising a favourable CASA, from an inclusion perspective its success has to be seen in terms of providing savings service to its microfinance customers and sticking to the lost middle segment in lending.

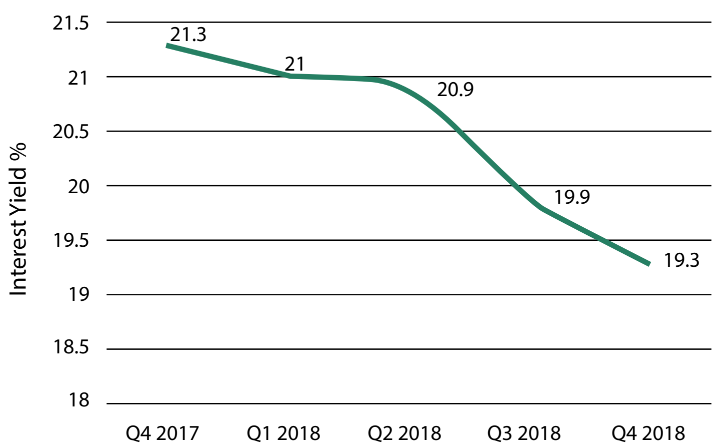

Figure 7.8: Equitas' Interest Yield Over the Last One Year

Source: Investor presentation of Equitas Holdings Limited, Q4 FY18 and FY18. https://www.equitas.in/holdings-details.php?category=Cw&section=Dg. Accessed on 20 July 2018.

AU SFB: The case of an NBFC (Non-MFI)[24]

AU started its journey in the year 1996 as an NBFC, Au Financiers, and over the last two decades it worked as a retail-focused, customer-centric, asset-financing NBFC. It touched over a million plus customers prior to becoming a bank in April

2017. AU Bank was the only asset financing NBFC amongst nine other successful applicants of the SFB licence. AU Bank is listed at both the leading exchanges, namely the NSE and the BSE (market capitalisation around US$ 3 billion) and the bank's IPO (Rs 1,912 crore) in 2017 was highly successful. Its primary asset business is what it calls 'wheels', representing loans for auto/cars for personal use, commercial vehicles, tractors and construction equipment.

By March 2018 AU SFB had been operating in 11 states with 306 branches, 97 asset centres and 71 BCs, 392 ATMs and had a balance sheet size of Rs 18,883 crore, which was 93 per cent higher vis-à-vis the total balance sheet size of Rs 9,781 crore as of 31 March 2017.

Post-SFB the challenge for AU has been mobilising deposits, opening bank branches, investment in IT as well as diversification of its loan portfolio.

Deposits: Innovative approach but long way to go

AU has a total branch network of 306 excluding BCs and asset centres. The geographical distribution of branches shows an even balance with metropolitan and tier 1 urban locations having 154 branches, tier 2 to 4 centres or suburban areas having 132 branches and 20 branches in rural areas. It seems that the rural areas strategy of AU is to cover them through BCs as during the year 2017–18 it opened 71 BC outlets, all of which are in rural areas. At present BCs offer account opening, lead generation for loan products, cash deposit, card-based cash withdrawals and card-based balance enquiries. It is planned to add other services like NEFT/IMPS transactions in the near future at BC outlets. In addition to BCs and tablet-based account opening, AU's deposit mobilisation strategy has three innovative things:

1. No deposit slips at branches: customers can deposit their cheque/cash without having to fill up a deposit slip. AU generates a receipt of deposit for the use of the customer.
2. At AU Bank, a cheque can be used to transfer funds via RTGS or issue a demand draft by mentioning it on the instrument obviating the need to fill an additional form.
3. The bank has developed a savings product targeted at banking requirements of the central government, state governments, central and state public sector undertakings (PSUs), boards and other government departments—what it calls 'government business', which includes zero-balance salary accounts.

The borrowing/liability profile of the bank as of 31 March 2018 shows diversified sources, but despite efforts total deposits including CDs constitute 50.9 per cent (excluding CD, the share is 43 per cent), the other major sources being refinance from financial institutions and NCDs (Figure 7.9). Despite mobilising CASA and term deposits of Rs 6,742 crore, the challenge for AU has been meeting its loan growth—the balance sheet grew by 93 per cent in 2017–18. The fact that it commenced operations in April 2017 is also significant as it has completed only 12 months of operations as an SFB.

AU had a CASA of 32 per cent as of 31 March 2018, with CA accounting for a negligible share of 6 per cent. Thus, majority share of term deposits and savings. While retail households account for 94 per cent of accounts, their share in the amount is low at 24 per cent, which effectively means retail deposits are Rs 2,139 crore. As per AU's annual report, the average ticket size in savings account is Rs 40,000 and term deposits Rs 7.9 lakh, which is indicative of the fact that its reach and target at present remain focused on middle to higher income classes.

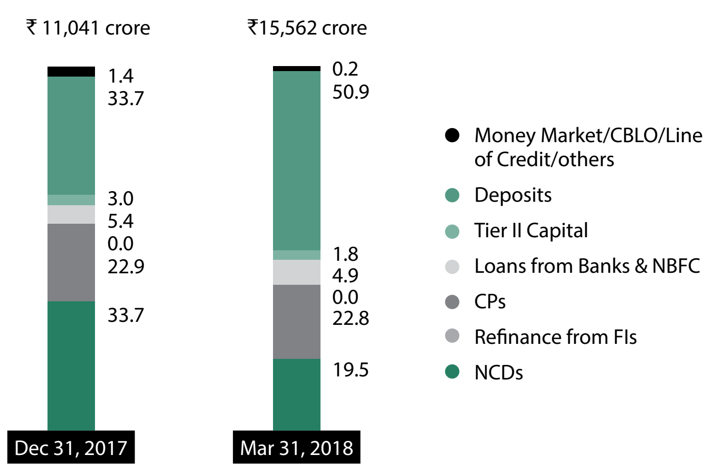

Figure 7.9: AU's Resource Mix (in per cent)

Source: AU, *Annual Report* (Jaipur: AU SFB, 2018).

Table 7.6: AU Deposits as of 31 March 2018

1	Total deposits including CDs	Rs 7,923 crore
2	Total no. of deposit accounts	5,31,062
3	Of 1, % of savings account share	26%
4	Of 1, % of current account share	6%
5	Of 1, % of term deposit share (43%, non-callable)	68%
6	Share of household deposits in 1 (Of 2, the share is 94%)	27%

Source: Data given by AU to author.

Table 7.7: AU's Asset Business Products

Retail assets	Small- and mid-corporate assets
Wheels (vehicle loans)	Financial institution lending: Lending to NBFCs, housing finance companies (HFCs) and MFIs—also offers cash credit and overdrafts
Gold loans	Construction finance—credit requirements of small builders
Secured business loan—MSME (typically annual turnover Rs 10 lakh to 10 crore)	Business banking—vertical to extend fund-based working facilities such as overdraft, cash credit and non-fund-based facilities like letter of credit and bank guarantee, among others, to MSME and SME customer segments
Secured business loans—SME (Typically entities with annual turnover more than 10 crore)	
Agri-SME loans—focused on agriculture and allied value chain like food processing units, fertiliser/seeds wholesalers and retailers	
Home loans	
Gold loans	
Consumer durables loan—pilot in partnership with Snapmint, a digital platform, wherein cashless EMI option to customers are offered	

Loan portfolio: Dominated by the legacy of 'wheels' and larger size loans

Post-SFB, AU has diversified its loan products and started many new product lines such as agri-SME loans, gold loans, home loans and consumer durable loans. The annual report says 'after becoming a bank in FY 2017–18, we significantly broadened our product portfolio from just six assets products to more than 27 product offerings'. The asset business is broadly divided into two segments, retail assets and small and mid-corporate.

While AU's annual report says that 'As on 31st March 2018 we had priority sector lending Qualified Advances of Rs 9,424 crore out of Total Advances of Rs 13,312 crore', its product offerings are more upmarket than the non-MFI portfolio of other SFBs. This is reflected in the fact that the average ticket size under retail assets was Rs 5 lakh and under small- and mid-corporate assets at Rs 70 lakh.[25] Retail assets constitute 81 per cent of AUM as of March 2018 and the balance is accounted for by small- and mid-corporate segments.

The product-wise AUM for March 2018 is indicative of the strong dominance of legacy products. Vehicle finance makes up for 44.5 per cent share, followed by secured business loans for MSME at 31 per cent. The only other product of sizeable size is lending to NBFCs, which has a share of around 10 per cent. New products introduced in the retail segment like gold loan, agri-SME, housing loan and construction have put together a negligible share—a reflection of the fact that AU had less than a year to build the portfolio.

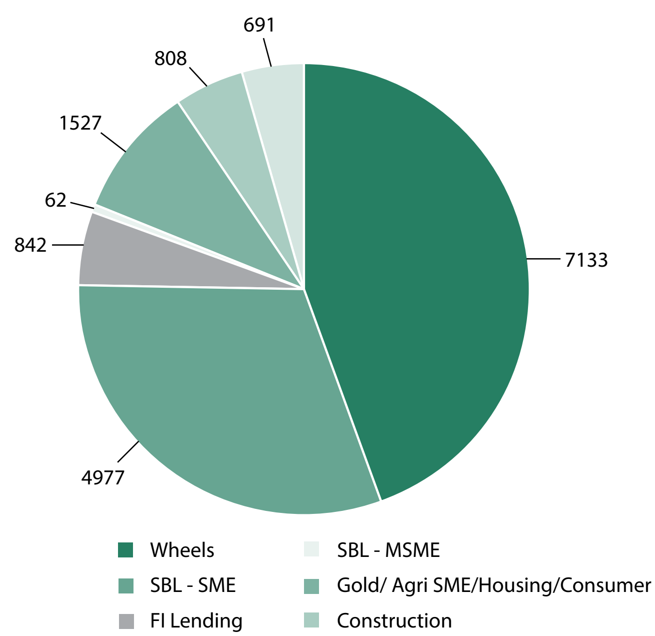

Figure 7.10: Product-wise Break-Up of AU Bank AUM (in Rs crore) (March 2018)

Source: Investor Presentation of AU SFB, Q4 FY 18/FY 18. https://www.aubank.in/investor-relations.

If we look at AU's portfolio in terms of loan size, loans below Rs 2 lakh total a mere Rs 606 crore.[26] A majority of its loans are below Rs 25 lakh and the same is mentioned in the annual report: 'in FY 2017–18, 97 per cent of the total number of loans disbursed were of amounts less than Rs 25 lakh.'

Despite a major part of its loan portfolio being secured, it had a gross NPA of 2.5 per cent in March 2018 with the secured-MSME loan segment having a higher GNPA of 6 per cent. Though AU SFB meets the priority sector requirements prescribed for SFBs, from an inclusion perspective its product mix is more aligned to asset NBFCs—what it was before becoming an SFB—than the generally expected role of SFBs. The average ticket sizes under retail and small- and mid-corporate segments have been mentioned, and to buttress the point, even in the case of secured business loans for MSMEs, 64 per cent of loans are between Rs 10 lakh and Rs 1 crore.[27] It is quite likely that with the launch of several new loan products, its AUM break-up will reflect more of an inclusion focus in the coming years.

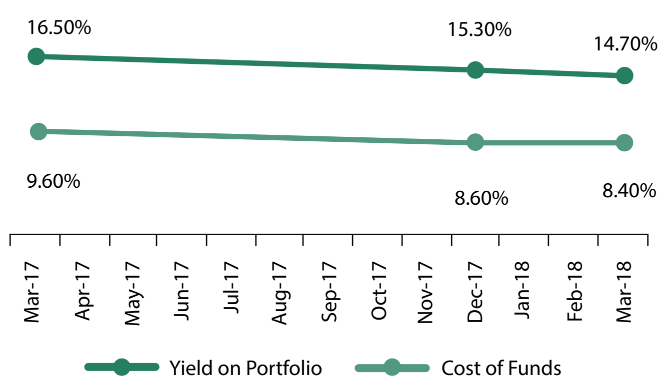

Figure 7.11: AU SFB's Yield and Cost of Funds

Source: AU, *Annual Report* (Jaipur: AU SFB, 2018).
Investor Presentation of AU SFB, Q4 FY 18/FY 18. https://www.aubank.in/investor-relations.

Interest rates on loans: Moving southward like other SFBs

After becoming a bank in April 2017, AU's COF has declined from 9.6 per cent to 8.4 per cent (Figure 7.11) and so has the yield. As the GNPA position has improved in March 2018 over the previous quarter, the possible reason for reduction in yield seems to be reduction in interest rates. The current IRR in major products is: Wheels new: 11 per cent to 15 per cent; wheels used: 17 per cent to 21 per cent; SBL-MSME: 14 per cent to 18 per cent. The MCLR of AU SFB is also low compared to other SFBs, ranging from 11.20 per cent (overnight tenure) to 13.15 per cent (three years)[28]

The one year of AU SFB shows its difference from other microfinance-focused SFBs in its loan book, but it also reflects similar challenges of retail deposit mobilisation, gathering traction in newly launched loan products, getting the branch and asset centres' strategy right, and diversifying the business while retaining the inclusion perspective.

THE CHALLENGING FUTURE OF SFBS

Though SFBs are still in their early days, the performance so far has thrown up some critical challenges which will continue to persist for the short to medium term. It was well anticipated that SFBs would face the challenge of technology, liability mobilisation, business diversification and people skills. The performance so far shows that SFBs have done well on technology and the advantage of being able to integrate the recent and best technology platforms has in fact put them a step ahead of other banks. Human resources is an area which seems to be also fine so far, but most microfinance SFBs will face the problem in the future of upskilling their microfinance or asset centres. While one may argue that the skills are adequate for a microfinance business, the moot point is whether they can continue to have a large share of the unsecured microfinance portfolio. The answer is a no both from a regulatory perspective and as an objective of the SFB. As the share of retail deposits increases, the regulator is likely to be not comfortable with large exposure to unsecured loans. Banks themselves will not be comfortable from a risk perspective. This point was underlined by Rajeev Yadav, CEO and MD of Fincare SFB during the 11th Mint Annual Banking Conclave in 2018 by saying:

> Some of these risks[29] will materialise at some point of time and given the root causes of what triggered some of the issues, they are related to loan waivers, they are related to some degree of political activities and we do ask ourselves this question that with elections in various states coming up, in the central government elections coming up, would some of those issues come up again in some form and if they were to come up, how do you mitigate your risk at the bank level and strengthen the portfolio to diversify across various asset classes.[30]

Portfolio diversification while retaining the financial inclusion focus will be a major challenge in the years to come; efforts have started but are yet to show results. The RBI guidelines also mention the inclusion focus by placing emphasis on 'unserved and underserved sections including small business units, small and marginal farmers, micro and small industries and unorganised sector entities'. Even these indicative guidelines have a broad area and the current business diversification of SFBs suggests a more proactive approach towards the so-called creamier layer of the underserved—as can be seen in the dominance of loan against property, gold loans and vehicle loans with few exceptions. The seemingly real intent of policy in creating SFBs was to cater to the needs of the missing middle (discussed in chapter 4). This segment has its own challenges and needs a greater level of appraisal. P.N. Vasudevan, MD and CEO of Equitas Bank, alluded to this in the 11th Mint Annual Banking Conclave by stating the challenges of this segment:

> Not really having proper financial documents to show their income levels. When we go for credit assessment, and we are not able to see any documented proof of the income and we have to do lot of surrogate methods to determine the income, from an internal perspective we treat that as an informal sector.

Lending to this segment has huge potential and it is felt that the SFB which manages to tap this segment will be best positioned to balance business diversification with inclusion objectives.

Liability mobilisation has been a challenge and the performance so far shows that it will continue to be a challenge. Despite an encouraging performance, the bulk of the deposits continue to be from institutions and not retail households. It seems to have been realised early by SFBs that their microfinance client base would not be able to contribute a meaningful share to the deposit kitty and they have to depend on a different strategy for deposit mobilisation. The problem is further compounded by the low share CASA, which is the prime factor for reduction in the COF. Currently, the low share of CASA leads to a high operational cost of creating CASA as the base is low. There is also a feeling that the regulatory guidelines requiring SFBs to mention SFB against their name is detrimental to deposit mobilisation. R. Baskar Babu, MD and CEO of Suryoday SFB, alluded to this fact at a conclave by saying:

> People question what are you. But the regulator insists that you have to mention SFB. The word small finance doesn't really go well with south India. They think we are some company. Then we have to show the licence. Then they go check in the website.[31]

The other larger question aligned to SFBs' value proposition relates to the expectation of reduced rates of interest riding on lower COF. Lending rates have shown some decline but still remain above the banking sector on account of factors like unsecured lending, technology costs associated with the banking business, branch expansion costs and a lower share of CASA. It remains to be seen as to how long the patience of public policy, and more importantly the regulator, will last to the continued high lending rates. Additionally, SFBs after having got a taste of operationalising the SFB business are not too comfortable with business restrictions in the form of higher capital adequacy requirement of 15 per cent, 75 per cent PSL, 50 per cent loans to be less than Rs 25 lakh and constraints on branch licensing. SFBs have also been facing quite a few operational issues, which were raised with the deputy governor of the RBI during the roundtable of SFB CEOs organised by Access Assist in April 2018. The future of SFBs is fraught with these challenges and how different SFBs will evolve strategies to meet these challenges will become clearer in the next two to three years.

PAYMENTS BANKS: OBJECTIVES AND PROGRESS*

PBs were conceptualised with the objective of furthering financial inclusion in the country by offering differentiated banking services, mainly money transfers and small deposits. Of the original 11 that were granted in-principle licences, 6 have already launched their operations (Box 7.3). Of the business houses that were granted licences, telecom companies like Airtel, Vodafone and Reliance's Jio showed great promise in their ability to leverage existing outreach to unserved and underserved areas through their MNO services; entities like Fino already had an established client base to leverage and the Department of Post had a formidable network of bricks-and-mortar offices and a field force that has the potential to achieve the RBI's mandate for PBs. One of the key expectations was to also see these entities as technologically enabled

*The author is grateful to the help by Devahuti Choudhury for help in writing this section

with the RBI guidelines clearly articulating the need for such banks to be fully networked and technology driven from the beginning of their operations. Of the now six operational entities, the latest entrant is Jio Payments Bank that formally launched its operations in April 2018.

> ***Regulatory Pathway***
>
> - September 2013: Nachiket Mor Committee on comprehensive financial services for small business and low-income households formed
> - January 2014: Committee recommends formation of a new category of banks—Payments Bank
> - November 2014: The RBI releases final guidelines for PBs
> - February 2015: The RBI releases a list of 41 applicants for PB licence
> - August 2015: In-principle agreement to grant licences to 11 entities
>
> ***Operationalising PBs***
>
> - November 2016: Airtel Payments Bank (APB)
> - January 2017: India Post Payments Bank (IPPB) announces soft launch
> - May 2017: Paytm Payments Bank (PBB)
> - June 2017: Fino Payments Bank (FPB)
> - February 2018: Aditya Birla Idea Payments Bank (ABPB)
> - April 2018: Jio Payments Bank (JPB)
> - Undisclosed launch date: National Securities Depository Payments Bank
>
> Cholamandalam, Tech Mahindra and Dilip Sanghvi-IDFC-Telenor joint venture surrendered their licences. Vodafone merged with Idea cellular in August 2018.

With a fairly well-articulated regulatory framework announced by the central bank in November 2014 and the subsequent operation launches by different PBs between November 2016 and February 2018, expectations from these entities have been high with some banking gurus also anticipating them to be a disruptive force to reckon with. Further, in terms of products these banks are mandated to accept deposits not exceeding Rs 1,00,000 per account and to offer remittance services. In a concerted effort to strengthen the BC outreach, the RBI has also made provisions for PBs to act as CBCs for mainstream commercial banks. This step will strengthen the current BC network that already stands at 5,15,317 banking points in rural areas and 1,42,959 in urban areas.[32] Many of the PBs have tied up with mainstream banks as their CBCs. Fino, for instance, is now an active BC for ICICI Bank and offers a suite of ICICI products such as loans for housing, auto, gold and personal purposes. In the same vein, Airtel Payments Bank recently tied up with Bharati AXA Life insurance to offer a life cover of up to Rs 2,00,000.

Current Status of Operations at PBs

As mentioned at the start of the chapter, it has been difficult to get data from banks and the fact that the RBI data for March 2018 is also awaited at the time of writing this report, the operational facts have been pieced together from company websites, news articles and reliable blogs. Further, the number of debit cards has been used as proxy for accounts.

Airtel Payments Bank[33]

Airtel Payments Bank (APB) commenced operations in November 2016 and is the first among the 11 licensed entities to have launched its operations. The APB is a joint venture between Bharti Airtel and Kotak Mahindra Bank with them holding 80.1 per cent and 19.9 per cent stake, respectively.

> **Number of retail outlets:** Around 5,00,000, including outlets that sell airtime across 29 states
> **Client leverage:** 270 million customers with Bharti Airtel
> **Number of accounts activated:** 17,48,580[34]
> **Products:** Savings/current accounts; free digital debit cards (Mastercard); Airtel Money (wallet); life insurance cover of up to Rs 2,00,000 (Bharati AXA Life); account-linked accident insurance of up to Rs 1,00,000; DBT of government cash subsidies where accounts are seeded with Aadhaar as primary bank accounts; mobile banking app for checking balance and statement, bill payments and online transfers
> **Interest on deposits:** 4 per cent per annum (revised from the initial 7.5 per cent at launch)
> **Transaction costs:** 0.65 per cent of transaction value for withdrawal

Fino Payments Bank[35]

Fino Payments Bank (FPB) announced the launch of its operations in June 2017 and is one of the first to go live with 422 branches called customer service points (CSPs) and around 25,000 own BCs. The FPB had the leverage of its existing physical presence through its microfinance operations and was able to scale almost immediately till the regulator halted its operations in May 2018 due to violations of licensing and operating guidelines. The FPB brands its approach as 'phygital' that leverages both physical touchpoints as well as digital technology for last-mile service delivery. CSPs offer a full suite of services and also withdrawals for other banks' clients through micro-ATMs. More than 60 per cent of transactions recorded take place outside the branches. About 25 per cent of FPB customers have downloaded the mobile banking app BPay, while 50 per cent have RuPay debit cards. The FPB is a fully owned subsidiary of Fino PayTech Limited.

Number of retail outlets: 422 branches, around 25,000 own BCs, 648 onsite ATMs and 4,198 offsite ATMs
Client leverage: Existing BC network, clients of Fino Finance
Number of accounts activated: 2,82,823
Products: Savings/current accounts with differentiated products that include DigiPay, an online zero-balance digital account—some savings accounts type may also require a minimum balance of Rs 1,000; free classic and platinum debit cards (RuPay); account-linked accident insurance of up to Rs 1,00,000; life, general and health insurances in partnership with ICICI Prudential, ICICI Lombard and Exide; acting as a BC for banks like ICICI and providing loans in the range of Rs 18,000 to Rs 35,000 as a BC agent. Mobile banking app for checking balance and statement, bill payments and online transfers
Interest on deposits: 4 per cent per annum
Transaction costs: 1 per cent of transaction value

Paytm Payments Bank

Paytm Payments Bank (PBB) started its operations in May 2017 through a beta launch of its banking app on the iOS. The PPB is a joint venture between its parent company One97 Communications and Vijay Shekhar Sharma. At the time of its launch, the company announced a plan to invest US$ 500 million towards the establishment of physical banking points. Earlier this year in August 2018, the regulator asked the PPB to stop onboarding new customers following compliance-related observations. While the bank is striving to meet compliance requirements, it can continue serving existing customers as long as they are KYC compliant.

Number of retail outlets: one onsite ATM; information about number of banking points unavailable; by end of 2018 the PPB is expected to open one lakh banking points[36]
Client leverage: Existing wallet customers of Paytm
Number of accounts activated: 4,16,36,757
Products: Zero-balance savings account; free insurance cover of up to Rs 2,00,000; fixed deposit facility in partnership with IndusInd Bank; free digital RuPay card; wallet including digital food coupons; prepaid toll payment facility in partnership with FASTag
Interest on deposits: 4 per cent
Transaction costs: Rs 125 for issuance of physical debit cards with an annual maintenance charge of Rs 100 thereafter; Rs 20 inclusive of taxes for cash withdrawals beyond three transactions in urban areas and five transactions in rural areas; Rs 8 inclusive of taxes for mini statement, balance check and pin change beyond three transactions in urban areas and five transactions in rural areas

India Post Payments Bank[37]

India Post Payments Bank (IPPB) announced a soft launch in January 2017 but formally started operations in September 2018. As a public sector company under the Department of Post and Ministry of Communications, the IPPB is a fully owned subsidiary of the Indian government that holds 100 per cent equity in this entity. It is the largest PB in terms of its network size and definitely has an edge over its peers with the bank set to operationalise banking access through all the 1,54,965 post offices before 31 December 2018. The formal launch was also propelled by the recent equity infusion of Rs 1,435 crore by the government to help the IPPB compete with its peers that have already been operating for some time now. The IPPB makes a fairly strong case for itself by emphasising on its differentiated products whereby it will complement POSB's (Post Office Savings Bank) focus on mobilising small savings by concentrating largely on digital transactions.

Number of retail outlets: 650 branches; 3,250 banking points
Client leverage: 356.7 million account holders at 1,54,965 post offices and around 1,50,000 postal workers under the POSB
Number of accounts activated: 322
Products: Savings/current accounts; money transfer; DBTs; bill and utility payments;

enterprise and merchant payments; instead of issuing debit cards, provides a free QR card requiring biometric authentication; doorstep services for cash withdrawal and deposits using the agent network of existing postal workers; sweep facility whereby deposits exceeding Rs 1,00,000 will be swept into the client's POSB account; mobile banking app for checking balance and statement, bill payments and online transfers
Interest on deposits: 4 per cent per annum
Transaction costs: Doorstep services through the postal network; Rs 25 (plus GST) for cash transactions and Rs 15 (plus GST) for non-cash digital transactions

Jio Payments Bank

A 70:30 joint venture between Reliance India Limited (RIL) and the SBI, Jio Payments Bank (JPB) launched its operations in April 2018. Through the partnership, the SBI is planning to leverage Reliance Jio's telecom network to deepen its reach. The bank is also looking to leverage the 4G-enabled feature phones newly launched by Jio Infocomm Limited to drive digital transactions.[38] Though it has been six months since its official launch, the bank is yet to get its feet on the ground and official reports extracted from the RBI and the NPCI websites do not show any significant activity for the bank.

Number of retail outlets: Undisclosed
Client leverage: 227 million Reliance JIO customers[39]
Number of accounts activated: None based on debit cards issued as per footnote 34
Products: Savings/current accounts, utility payments, personal loans; still working on their product suite as indicated on their website
Interest on deposits: 4 per cent
Transaction costs: Undisclosed

Aditya Birla Idea Payments Bank

Aditya Birla Idea Payments Bank (ABPB) launched its operations in February 2018. The new PB has been formed by the newly formed Aditya Birla Financial Services with the merger of Grasim Industries and Aditya Birla Nuvo that originally received the licence.[40] With Idea merging with Vodafone M-Pesa in September 2018, the new PB has a significant leverage of tapping nearly 440 million subscribers as potential banking customers that now exceeds Bharti Airtel and Reliance Jio.

Number of retail outlets: Undisclosed
Client leverage: 440 million subscribers with Vodafone Idea
Number of accounts activated: 2,240
Products: Savings account; ABPB wallet to facilitate money transfer and/or utility payments; insurance products offered in partnership with Aditya Birla Sun Life Insurance company and Aditya Birla Health Insurance Company Ltd.; personal loans as BC agents of banks (undisclosed); online banking; debit cards
Interest on deposits: 4 per cent
Transaction costs:[41] Rs 500 as minimum balance if bank account is opened through the BC channel; no minimum balance required for accounts opened digitally; Rs 75 for issuance of debit/shopping card; 0.3 per cent of deposit value in case deposits exceed the limit of five transactions per month; 0.85 per cent of the transaction value

Deep Dive into the PB Ecosystem: Will They Measure Up?

The regulatory room within which PBs have to operate is small with differentiated services extended to only accepting small deposits and remittances. One of the assumptions that drove the operational viability of PBs is their mandate to serve segments of the population that mainstream banks cannot reach out to. However, the fact that most PBs use a fairly complex digital interface poses a problem for the underserved, who are not digital savvy and need physical touchpoints. It will require concerted capacity-building efforts on the part of these entities to build the capabilities of unserved segments, as confidence-building measures and such learning curves take time and resources to establish. Features such as digital debit cards as offered by Airtel and Paytm or QR code-enabled cards by India Post are difficult products to scale given the limited capacities of low-income households that these banks are mandated to reach out to. It is not hard to anticipate that most of the products offered by these banks are currently suited to the urban and the more technological savvy and possibly not the financially excluded.

Moreover, the path to growth and sustainability for PBs remains extremely dynamic and unstable. Events such as the RBI's ban on the APB in January 2018 on acquiring more customers following a large-scale cooking gas subsidy payout in accounts that were opened without the consent of clients, followed by similar restrictions imposed on Fino and Paytm in August 2018, have greatly impacted the growth plans of these banks.[42] Even though the APB resumed customer acquisition in July 2018 after getting the nod from the RBI, senior officials from the bank anticipate challenging times ahead. On the regulatory front, policy change around wallet interoperability and the recent Supreme Court judgement barring private companies including banks from insisting on Aadhaar details of end clients are viewed as major dampeners for PBs. New entrants like the IPPB, the JPB and the ABPB that have experienced delays in the launch of their operations may have lessons to draw from the experiences of their peers. PBs have focused mainly on remittances and third-party products and not deposits—a recent newspaper report pegs the total deposits with PBs at Rs 540 crore.[43] A major reason for a lower focus on deposits has been the falling yields on one year G-Secs (PBs have to invest 75 per cent of their demand deposit balances in SLR eligible government securities/ treasury bills with maturity up to one year).

The focus on the remittance business is also now under competitive pressure, as the RBI[44] on 16 October 2018 issued guidelines for the interoperability of PPIs, which indicate that this will be introduced in a phased manner. In the first phase, interoperability of PPIs issued in the form of wallets will be introduced through the UPI. In the second phase, wallets and bank accounts will be made interoperable through the UPI and, eventually, in the last phase, cards will be implemented through card networks. These guidelines level the playing field between mobile wallets and PBs. The only difference will be that PBs will earn interest on deposits, while wallet balances will not yield any return. This is a major game changer as PBs also have been mainly focusing on payments and not deposits, and now they have to compete with PPIs also.

> PPI interoperability brings PPIs almost on par with PBs in payments

As the ecosystem changes, PBs which are already going through difficulties now face another turning point. The future for the payments space looks exciting from a customer standpoint, but from the business perspective of PBs it is challenging to say the least.

Trends and Issues Seen in the PB Model Based On Operations and Last Year's Events

Customer acquisition

PBs are vying for attention in the same markets that SFBs and NBFC-MFIs are trying to serve. Moreover, the PMJDY has achieved almost 99 per cent coverage (households) and it is backed by an aggressive push to bank BCs. In such a scenario, PBs have a very limited playing field to reach out to a new, unique customer base for deposits as well as payments. And now PPIs have also joined the payments ecosystem. The mandate to achieve financial inclusion for those pockets where mainstream banks are not able to reach seems difficult. Areas where people may have bank account access but are not 'ready' need deployment of large resources towards capacity building and infrastructure development. Most PBs are starting their operations in areas that already have a historical footprint for financial institutions. In addition, they are looking to leverage existing outreach either through their MNO operations (Airtel, Aditya Birla Idea), their bricks-and-mortar structures and human agent network (India Post) or their microfinance operations and BC agent network (Fino). Therefore, it makes pragmatic sense to onboard these clients first on to their PB platform.

Significant events around customer acquisition and KYC

As mentioned earlier, in December 2017, the UIDAI suspended the APB from using e-KYC services following complaints of bank account opening during routine verification of mobile connections without customer consent. With as much as 167 crore cooking gas subsidy routed through nearly 3.1 million bank accounts, the APB irked not just the UIDAI and the RBI but also oil companies whose customers complained about the 'missing' subsidy in their regular bank accounts.[45] Subsequently, after receiving supervisory reports and finding the APB in contravention of the 'operating guidelines for payment banks', the RBI imposed a penalty of Rs 5 crore on Airtel.[46] In a similar vein, in August 2018 the FPB's accounts were found to have deposits higher than the mandated Rs 1,00,000 that led to a halt in further opening of bank accounts on the direction of the RBI.[47] Earlier in June 2018 the PPB was asked to halt its operations following anomalies in the e-KYC verification process. In addition, branches of the PPB were found to be sharing premises with its parent company, One97 Communications, with decisions around account opening being taken by the parent company's agents who were also BCs for the PPB, amounting to the exposure of banking information to third-party service providers.[48] While the RBI allows for PBs to outsource the collection and verification of KYC for customers, the decision of bank account opening for a potential customer needs to rest with the bank. The intention seemingly was to optimise operational efficiency by onboarding mobile phone customers as bank account owners into the PB. However, one of the key steps for PBs is to differentiate their products and services from their parent company's especially where customer consent is concerned. The PPB was found to be in contravention of this regulatory expectation.

In the UIDAI's circular on the classification of global and local authentication user agencies (AUAs) released in May 2018, the APB was conspicuously absent thus rendering their ability to use e-KYC services ambiguous. The APB lost almost seven tense months and regained permissions to enrol new customers and using the UIDAI's e-KYC services only in July 2018.[49] Media sources state that the FPB and the PPB are currently in dialogue with the RBI and await the next step as far as customer acquisition goes.[50]

Another significant event that majorly impacts costs for onboarding customers for PBs is the historic Supreme Court ruling of 27 September 2018 on the constitutionality of Aadhaar. While the SC dismissed the possible use of Aadhaar data as an instrument of surveillance and subsequent invasion of Aadhaar holder's privacy, a significant ruling has been made regarding the access to Aadhaar details by private companies including PBs. Phone numbers and bank accounts do not need to be seeded with Aadhaar numbers rendering the entire KYC verification of the current systems at PBs obsolete. This literally translates into an exponential increase of almost 5–6 days in onboarding customers where initially it would take just 30 minutes to recruit a potential client into a PB's systems. In rural areas customer acquisition may become even more arduous with inevitable delays in registration.[51] For a system that was supposed to be completely automated from onboarding to product access to transactions, this ruling will require the entire banking system including the regulator to go back to the drawing board.

> Inability to use Aadhaar for e-KYC significantly raises costs for PBs

Governance and Compliance

The dismissal of executive positions in two of the PBs and months lost in taking compliance measures, concerns regarding the governance structures of some of the PBs have also been raised. Most of the PB licences have been granted to business houses. There have been doubts about their capabilities to function as a bank, and in the initial years of laying their foundations PBs will have to focus on getting the right people on board and offer comfort to the regulating authorities, employees and even end clients through the application of their experience in working with low-income segments. During a roundtable meeting organised by Access Development Services with CEOs of PBs, held earlier this year in April, the RBI deputy governor specifically pointed to the need for giving paramount importance to audit systems within banks with processes to ensure that the information flow from all relevant departments can be streamlined and well positioned for compliance purposes. The directive is clearly to err on the side of caution than take risks towards non-compliance.

The RBI clearly has zero tolerance for non-compliance. Coupled with recent events, there is tremendous pressure on PBs to build a strong compliance infrastructure. This requires a large investment in terms of building processes, deployment of human resources, communication protocol, and most importantly, placing the right talent to nurture a positive relationship with the regulator and other statutory authorities such as the UIDAI. The APB, the FPB and the PPB faced significant loss of time and focus in compiling compliance-related reports that took away resources and energies from building their operations on the ground.

> PBs need to consider whether their product offerings are suited to the excluded and low-income segment or guided by the focus on being profitable

Product suitability

One of the most important steps for PBs is to be able to differentiate their offerings from mainstream banks, and in some cases, their parent business houses. The target market for these banks consists of low-income households that have limited market recourse and it is the responsibility of the bank to ensure absolute transparency in the way products, features and aftersales services are communicated to the client. With financial inclusion being the primary mandate of PBs, it is of utmost importance that products are created keeping in mind the profile of low-income segments. At the same time regulations as well as cost structures demand PBs to keep processes as lean as possible and leverage technology to the fullest extent. It is therefore not surprising that most PBs are pitching digital products as their contribution to a less cash ecosystem. However, these products necessarily have to be suited to the capabilities of the end clients that banks are trying to serve. These segments are typically defined by limited digital capabilities, low adoption of banking services and general lack of trust for non-mainstream service providers, which call for PBs to push a significant investment into not just product design but also effective mechanisms to engage with clients in order to facilitate long-term adoption. For example, the APB is offering a digital debit card in partnership with Mastercard and the IPPB is planning to offer QR-enabled cards as part of their product suite. Even though bank account access is high owing to the PMJDY push for universal bank account opening, debit card ownership and usage in significant volumes is still a distant reality for low-income segments. The transition from deposits into PB accounts to using digital mediums to rotate such funds for different requirements is a long drawn out one for a typical low-income household. Therefore, it is to be seen if the excitement of such digital products actually translates at scale for the target market of PBs. The rush to offer third-party products like insurance, loans and mutual funds is borne out of viability concerns, but the question to be asked is whether low-income clients are ready for the adoption of such products and is it in line with the mandate. The burden of proof also lies with the regulator since as part of the operating guidelines for PBs, due permissions need to be sought from the RBI before a product is launched. Mainstream commercial banks do not need such approvals but agencies offering PPIs and PBs are exceptions.

A viable customer base

Establishing a viable customer base is also an important proposition that PBs will have to consider and in some cases re-evaluate. If the RBI mandate is for these entities to reach out to low-income households previously unserved by existing institutional structures in place, there is a tough road ahead with coverage and product overlaps. With an almost universal coverage of BSBD (basic savings and basic deposit) accounts through the PMJDY scheme and the push for digital platforms like the UPI, both the deposit and transaction mandate of PBs is in conflict with existing and perhaps more robust products. Inclusion of PBs as part of the DBT infrastructure seems reassuring at first but if seen from close quarters, it is the BSBD accounts opened under the PMJDY that are preferred for receiving government subsidies both by the government and the end customer. In addition, the DBT path is something that PBs are willing to tread only with extreme caution especially given the APB experience and the months lost in currying favour with the regulator and the UIDAI. For a segment of the population that already has a major psychological distance from the formal banking infrastructure, such multiplicity of choices can be confusing if not differentiated well. Most of the PBs websites provide bill and utility payments including DTH, water and gas as product offerings. Given that a typical low-income household will in all likelihood not have/have limited access to such services, the question around the understanding of the target client base remains pertinent.

Critical role of the agent network

Even though PBs are popularly defined by their fully-digital identities, the role of a human agent network is paramount. PBs are expected to have a robust banking point network operated by human agents that should cater to information and aided-transaction needs of customers. In this ecosystem, agents are even more uniquely positioned because of the key role they play in influencing behavioural change whereby a largely cash-driven population segment is expected to finally adopt digital products. The regulatory restrictions imposed on the APB and the PPB earlier this year are further testament to the fact that unless agents are empowered and trained to provide transparent information and adopt fair, customer-centric practices, the backlash will have long-term implications leading to loss of client loyalty, revenue and the regulator's goodwill. In addition, from a channel management perspective, it is important to unify the code of conduct for all service providers offering banking/wealth management services. Entities like NBFC-MFIs, SFBs, PBs and fintech providers are all dealing with low-income segments, but each is mapped to a different network or code. For example, while NBFC-MFIs follow the MFIN-Sa-dhan code of conduct, banks follow the BCSBI/IBA codes.[52] The differential treatment meted out will only throw off a potential low-income customer who is anyway trying to bridge the psychological distance from the formal banking system. The future of PBs, at least in their ability to scale and establish viable operations, will depend on the success with which they are able to maintain a sustainable agent network. Towards this end relevant stakeholders must realise that many agents lose focus while providing banking services due to the low commissions earned. However, with differentiated banking products on offer, the agent network must be incentivised through additional revenue-making opportunities such as aided-ecommerce transactions.

Need to have a client-focused code for PBs agent network

Financial viability and revenue streams of PBs

The regulator and the selection committee for the grant of licences clearly had a keen eye for entities that would have deep pockets for the long haul. Big business houses from telecom, financial/fintech and e-commerce services and government-owned entities were expected to have the wherewithal to withstand the expected trials and tribulations of a space that is vying to create a niche for itself amidst the wider financial architecture in India. However, the last two years have showcased the increasingly clipped aspirations of a sector that had otherwise started on a very energetic note. Compliance and regulatory issues notwithstanding, the slowdown of operations and the search for getting the business model right has led to a loss of time and resources for these PBs. In addition, opportunities for establishing stable revenue streams seem limited. The case of the IPPB stands separate from the rest, as while it has announced that it will piggyback on the branch network and field staff of India Post, it is not clear how costs and revenues will be shared. It is worthwhile to draw the lens closer on each of the plausible revenue streams for PBs in the following sections.

Remittances

Around 92 per cent of the workforce in India is categorised as the informal workforce (unorganised sector workers plus informal workers in the organised sector),[53] of which the migrant workforce is made up of almost 120 million workers. This mobile workforce hails from under-connected and infrastructure poor areas and makes up almost 80 per cent of the remittances market in India. This market serves two purposes for entities like PBs. One, it meets their targeted outreach since a bulk of the clients in this segment belong to low-income households and are typically excluded from formal financial services. Two, it provides an opportunity to serve a client group that is already engaging with the product and will appreciate a more hands-on engagement in terms of the process, low-risk transactions as opposed to traditional means (friends/family, agents) as well as cost-effectiveness. Domestic remittance in India is valued at more than Rs 900 billion per year, including non-traditional modes of transfer. Rural India's contribution is over Rs 700 billion per year, of which traditional channels comprise a mere 40 per cent or Rs 300 billion. The rest of the remittance happens via non-traditional modes.[54] Given the high risk of these remittance modes, there is a huge scope to expand traditional remittance avenues like PBs. PBs have understood this opportunity and most larger entities have pushed for competitive products in this space. The remittance product is a great selling point for PBs and is an effective place of entry into the desired customer segment. For example, the FPB already had a large network of banking points at inception and has a presence in the rural areas of UP, Bihar, Maharashtra, MP and in over 110 urban locations that are migration corridors. The FPB claims that its remittance business has tripled since its inception in 2017, with a monthly transaction of almost Rs 1,150 crore.[55] As other PB peers ramp up their customer acquisition efforts, it will be worth noting the extent to which PBs are able to alter and formalise the remittance space in India, particularly for low-income segments. Table 7.8 lists the fund transfer charges levied by most active PBs in India. The JPB has not published its schedule of charges and is therefore missing from this list.

The remittance battle for dominance among PBs is driven by financial might as seen in Table 7.8. Paytm is offering its remittance customers free transactions and it is not clear how this translates into viability of operations. It seems the focus is on acquiring customer loyalty.

Deposits

Lending is not an option by regulation and therefore where a commercial bank can cash in through a robust credit business, PBs are only saddled with the liabilities side of the trade. Apart from the requirement of maintaining a CRR/SLR on the outside liability, they are required to de facto maintain

Table 7.8: Fund Charges of Active PBs in India

Payments Bank	IMPS		NEFT	
	Intra-bank network	Inter-bank network	Intra-bank network	Inter-bank network
Airtel PB	Free	1% of amount transferred	Free as per regulation	Website mentions, as per RBI guidelines
Fino PB	Free for mobile transactions; Rs 5 for branch-based transactions; Rs 10 for transactions at merchant locations	Up to Rs 1,000—Rs 5, Rs 1,001–4,999—Rs 10, Rs 5,000–9,999—Rs 15, Rs 10,000–25,000—Rs 20, Rs 25,001 and above—Rs 30	Free as per regulation	Undisclosed
India Post PB	Free	2 remittances free every month; Rs 5 per transaction up to the value of Rs 1,00,000; for mobile banking Rs 4 per transaction up to the value of Rs 1,00,000	Free as per regulation	Up to Rs 10,000—Rs 2.5 per transaction; Rs 10,000 to Rs 1,00,000—Rs 5 per transaction
Paytm PB	Free	Free	Free as per regulation	Undisclosed
Aditya Birla PB	For assisted channels: Up to Rs 10,000–Rs 5, > Rs 10,000–Rs 10 For digital channels: Free	Up to Rs 1,000—Rs 2.5, Rs 1,001 to Rs 10,000—Rs2.5, Rs 10,001 to Rs 25,000—Rs 5, Rs 25,001 to Rs 2,00,000—Rs 10	Free as per regulation	Up to Rs 10,000—Rs 2.5, Rs 10,001 to Rs 1,00,000—Rs 5, Rs 10,001 to Rs 25,000—Rs 5, Rs 1,00,001 to Rs 2,00,000—Rs 15, > Rs 2,00,000—Rs 25

Note: All charges mentioned in the table are as they appear on the respective PB's website.

a 75 per cent SLR on their demand liabilities and face a cap on keeping deposits with commercial banks at 25 per cent of their current and time deposits. This reduces the business of PBs to that of a fixed spread business. PBs faced a twin problem on the deposits front. First, the decline in yield on one year G-Secs, and second, field observations of the author show that PBs are still not the preferred accounts for deposits, with most of the target segment leaning towards the PMJDY-endorsed BSBD accounts for parking their savings. These two factors have led to PBs offering competitive returns on deposits, for instance, a return of 7.5 per cent by the APB at the time of its launch has been brought down to 4 per cent. Similarly, most other players offer returns in the range of 4 to 5 per cent in line with mainstream commercial banks, much lower than SFBs and a few private banks. PBs' inability to offer differentiated rates of interest on deposits to a typical retail account holder leaves very little motivation for the account holder to shift loyalties.

> Lowering of interest rates on deposit balances necessitated by falling yield on G-Sec

Further, regulatory requirements mandate PBs to maintain a robust network of physical access points, of which at least 25 per cent must be in rural areas. It is also expected that such efforts be complemented by building banking infrastructure such as ATMs. Building such infrastructure can be expensive and therefore it is not a surprise that most entities that finally launched their operations have field leverage, and those that did not withdrew from the race. However, such an investment, coupled with limited liquidity options (as described above), also offsets the assumption that PBs can adopt low-cost technology-driven models and therefore offer cost-effective, affordable products. This is thus a strange situation for PBs to grapple with and only time will tell if regulatory expectations and a positive financial bottom line can meet midway to sustain the current business model.

Following are some of the regulatory allowances and leverage points that PBs can possibly look at to secure their cash flows going forward.

Linked to the volume of deposits are the sweep out arrangements for end-of-the-day deposits exceeding Rs 1,00,000 per retail account. Excess amounts are swept out into a linked account with a partner commercial bank (examples: the PPB with IndusInd Bank, the FPB with ICICI Bank and the IPPB with the POSB) in the form of a fixed deposit that will yield an annual interest for the account holder. As confirmed from industry sources, standing instructions in the form of a consent form is taken from clients whereby such sweep out may be facilitated. A percentage of the interest earned is apportioned by the PB and the rest is passed on to the customer. Again, it is to be seen if and when this revenue stream will sufficiently materialise returns for banks as data on sweep-out balances is not available. In addition, the current deposit levels are too low for this particular facility to yield any significant returns for PBs.

Transaction fees

This seems to be one of the most viable revenue streams given that digital transactions and ease of CICO facilities are one of the salient features that were supposed to differentiate PBs from mainstream commercial banks. However, with the successful launch and uptake of the government's UPI and the entry of several other payment firms offering PPIs such as wallets, which will now become interoperable, the digital differentiation has blurred for PBs. Even so, every PB has tried to competitively price its transaction costs to attract clients and facilitate adoption of their medium as the preferred mode. However, this will only be realised in due time with an increase in client base, uptake of products and the subsequent adoption reflected through a high frequency of transactions.

Third-party partnerships

Fostering partnerships is a critical part of the PB ecosystem. Since banks are restricted by regulation to offer only certain types of liability products like savings account, they are bound to use third-party networks to offer credit and other products like insurance. This makes pragmatic sense since the established route to garner customer stickiness, especially in the low-income segment, is through the credit route. It is therefore not surprising that most PBs are leveraging their identity as banking agents to cross-sell credit products for their mainstream bank partners. For example, the FPB is offering auto loans, home loans and personal loans on behalf of ICICI Bank to its customers. Similarly, the PPB offers a digital loan facility in partnership with ICICI Bank using an artificial intelligence (AI) powered algorithm to determine the creditworthiness of its clients. The amount for the zero-interest loan ranges from Rs 3,000 to Rs 20,000 for a period of 45 days, beyond which there is a fee of 3 per cent per month levied on the customer.[56] The newly launched IPPB has already tied up with the PNB and Bajaj Allianz to offer loans and insurance products. These partnerships allow PBs to offer insurance, mutual funds and fixed deposit facilities opening up a whole new avenue for wealth management products to the target audience. From a revenue-generating perspective, this is a creative way for PBs to make up for their regulatory constraints and help position themselves as a one-stop shop for banking and wealth management products using digital platforms. There is not very credible data available for the agreed commission terms between PBs and their third-party networks, therefore it is not easy to determine clearly how much these banks stand to gain through such partnerships.

Additionally, from a customer-targeting perspective, both the intention of the regulator and the commitment of PBs towards the inclusion of low-income/last-mile clients will only be evidenced if these products actually reach the low-income segments. This, as reiterated in the sections above, will involve a large investment on the part of PBs to build the capacities of a typical low-income client, find ways to provide transparent product/process-related information through non-digital means[57] and introduce confidence-building measures that can enable a behavioural shift among low-income customers.

RECENT POLICY-LEVEL CHANGES AFFECTING PAYMENTS BANKS: AADHAAR AND PPI INTEROPERABILITY

The much-discussed Supreme Court ruling around Aadhaar's constitutionality has invoked a new set of challenges for the PB ecosystem. Section 57 of the Aadhaar (Targeted Delivery of Financial and Other Subsidies, Benefits and Services) Act, 2016 allows the use of Aadhaar details for establishing the identity of an individual for any purpose, whether by the state, corporate or individual. The SC verdict passed on 27 September 2018 strikes down Section 57 of the Aadhaar Act and asks for a deconstruction of the clause from the private entity's perspective. As far as the current verdict goes, Aadhaar can still be accessed by government entities and is in fact a necessary means of identification for benefit/subsidy transfers to Indian citizens. From a PB's perspective this is a debate-worthy development for many reasons.

1. For an entity that is to be largely driven by a low-cost digital interface, the prospect of conducting physical KYCs can skew the entire operational model. The severity of the judgement is not yet clear since portions of the published verdict also imply that if provided by choice, private companies may use Aadhaar-based KYC subject to informed consent by the end client.[58]
2. The verdict definitely will require PBs, among others, to ramp up their data protection assessments, and in the immediate future this increases their operational liability with an anticipated impact on both expansion as well as revenue generation.
3. On a more urgent basis, PBs and other affected entities are already scrambling to find alternative ways to conduct KYC for their respective customers. While an e-KYC process could be completed in just about Rs 15, a physical KYC verification can cost anywhere between Rs 100 (in urban areas) to Rs 300 (in rural areas).
4. Use of PBs as part of the DBT infrastructure also gets hampered by the verdict as the entire transaction for the purposes of benefits/subsidy validation rests on Aadhaar verification. Participation in the DBT value chain is a reasonable revenue model for PBs to explore and the SC verdict has the potential to completely shut down the possibilities on such a front.

The Payment Council of India (PCI) is already lobbying with the government in an effort to pave the way for a more reasonable option that can ensure data protection for consumers as well as help private entities such as PBs to leverage the UIDAI infrastructure. However, it will be a long drawn wait for all stakeholders involved, further impacting the much-needed operational stability for PBs.

In addition to the above, policy-level changes introduced through wallet interoperability issued by the RBI in October 2018 have serious ramifications on the business of PBs. This feature will enable end customers to use the UPI and transact between wallet providers with whom they are registered. While this feature comes with certain caveats both on the regulatory as well as KYC front, interoperability will allow compliant PPI service providers to offer products such as remittances, utility payments and mobility of funds between different wallets that potentially overlaps with the differentiated services that PBs are expected to offer. This definitely puts the operational model for PBs in a flux since PPI service providers, such as Oxigen, MobiKwik, will have a regulatory 'edge' over PBs as for them compliance and capital requirements are more relaxed.

It is but evident that the only differentiator in such a case remains the savings account available through PBs which, as established, has not been able to capture the customer's interest in any significant way. With mainstream banks offering a full suite of products and PBs having to share their space with PPI service providers and NPCI products such as the UPI, there is little clarity on how PBs will pull through with a stable and viable operational model. Constantly moving pieces in the ecosystem are bound to have an adverse effect on PBs' operations, especially when they are still struggling to fix the business model.

CONCLUDING OBSERVATIONS

It is still early to say that differentiated banking has come of age or even matured as both class of institutions continue to grapple with different sets of challenges. It involves sailing unchartered territories as there are no examples from the past to look up for assessing success or failure metrics. Rapid changes in the ecosystem and policy compound the problem. Of the two, as of now SFBs seem to be on a firmer footing, primarily because of their legacy lending business. The major challenge for SFBs has been mobilising deposits and diversification of lending. Section 4 of the chapter lists out the challenges being faced by SFBs and it is clear that the future success among 10 SFBs will hinge on the ability to mobilise retail deposits which will lower COF, build traction in an array of diversified loan products introduced and meet the human resource challenges involved in upgrading the skills of pre-SFB staff geared towards a different business model. SFBs need to be cautious in diversifying their loan book; diversification with a financial inclusion drift may not be looked at positively by the policy. For balancing diversification with inclusion, SFBs will have to focus on the lost middle or the micro and small segment. This may temper growth plans but has immense potential and fits in with the policy objective of SFBs.

On the other hand, PBs are still in the ring to prove a business case for themselves. The deep pockets afforded by the investors for most of these entities have helped them meander through an otherwise cragged pathway. But before the business model could become even visible and concrete, the twin challenge of the Aadhaar ruling of the Supreme Court and the PPI interoperability guidelines of the RBI have further roughened the road. Of the available business lines, the current focus is on CICO operations, digital transactions, third-party products and customer acquisition. PBs, especially the MNO-backed PBs, need to look at the wealth of consumer data that they have access to. Transactions-led data includes data around mobile recharges, bill payments, e-commerce spends and offline merchant transactions. Mining such data for determining consumer profiles and applying predictive analysis principles can complement efforts made by entities such as credit bureaus for different lending institutions such as NBFC-MFIs and SFBs. It is almost certain that remittance operations are now likely to face a strong challenge from PPIs, and PBs to maintain edge will need to establish their presence in rural areas with a phygital approach. Focus on retailing third-party products can boost income but PBs have to question whether that is the mandate for establishing them.

Fortification of compliance infrastructure should remain a strong priority for the regulator and PBs will have to ensure a zero-tolerance policy stance in order to strengthen their systems, processes and people network. This is an absolute necessity for PBs to grow and scale their operations as also gain credibility.

Overall, the PB ecosystem is still testing waters and the business case based on the objectives of PBs is not clear. Therefore, it becomes important that the regulator maintains an open dialogue to ensure the viability of these entities along with achieving the objectives.

ANNEXURE 7.1: Ujjivan's IT Initiatives

Ujjivan has always believed that technology will be the engine that will drive us through the journey of becoming the best mass market bank. The journey is about creating technology that will help our customers embrace banking with ease, experience banking at their convenience and stay engaged through superior services.

Our technology strategy has three pillars (a) providing banking at the door step (b) leverage platforms and partnerships for tailor-made products (c) adopt digital to service customers better.

Our Technology Foundation

The technology platform implemented allows our customers to be served at the door step. As he gets familiar with banking, the customer can also reach us through a channel of his choice (mobile, telephone or through our branch).

- Biometric is our new pin. The philosophy is actually implemented while on-boarding an account as well as while providing basic banking services to our customer
- Our USP is paperless door-spep delivery at your convenience. The account relationship journey starts through the ubiquitous Hand-held device by using Aadhar. In addition, to opening an account, the device allows for a host of services including deposit opening, remittances and withdrawals.
- The loan originating system has additionally been put in place for MSE/ Housing that allows for sourcing, verification as well as underwriting in a seamless way. The entire cycle is integrated with the respective bureaus to ensure a high degree of straight through process.

Ey Initiatives

- With the foundation laid, the latter part of the year saw a shift in renewing a focus on less-cash economy and also embarking on the digital journey
- Ujjivan has been one of first banks to have a biometric ATM. Customers can transact with a fingerprint. Last year saw additional installations of the biometric ATM.
- Aadhar based payments have been implemented through our business correspondents to further facilitate transactions from our customers as well as "other bank" customers using only Aadhar.
- In order to further a less-cash ecnomy, the loans disbursed have been credited to the savings account. The system has been configured to open an account as part of the loans process itself. In addition, a debit-card is also given instantly to ensure that the money can be withdrawn at their convenience.
- In order to ensure better customer service and usage of the debit card, insta-kit has been launched. The insta-kit is a delivery kit (with the ATM card and pin) given instantly that ensures the account can be used immediately.
- It was found that customers forget their pin or do not use their pin despite getting one. In order to help customers, the technology team has implemented a green-pin option that allows customers to choose their own pin number through the ATM.

Our Technology is built to empower our employees to serve our customers better.

Source: Ujjivan's Annual Report 2017-18

ANNEXURE 7.2:
Suryoday Small Finance Bank's Loan Products—Key Features

Product	Eligibility	Tenure	Loan Amount Range	Interest rate (p.a.)	Security
Inclusive Finance					
Microfinance JLG	Group of women having income generating activity and residence stability	12 to 24 months	INR 10000 to 42000	25.4% to 26.08 %	Unsecured
Microfinance Individual	Convered to MSME Micro [T Nagar] now				
Vikas loan	Customers who have completed minimum 2 loan cycles of JLG	24 to 36 months	INR 30000 to 1 lakh	24.88% to 25.60%	Unsecured
MSME Micro [T nagar]	Small business loan with distinctive business premises	12 to 36 months	INR 50000 to 300000	24.66% to 25.92%	Unsecured
Retail assets					
MSME	Income program (Debt burden ratio / Debt service coverage ratio based), ITR, Banking and Repayment track record surrogates	12 to 48 months	INR 1 lakh to 25 lakh	19.5% to 30.5%	Unsecured
Housing Loan	Income and Fixed obligation to income ratio based	Upto 20 years	INR 3 lakh to 100 lakh	10.5% to 14%	Secured
Loan Against Property	Income and Fixed obligation to income ratio based	1 to 10 years	Upto 5 crore	12% to 18%	Secured
Commercial Vehicle	Existing vehicle ownership, free finance ratio of 35%, existing repayment track record and standard assets	3 to 5 years	INR 15 lakh to 10 crore	10% to 18%	Secured
FIG (secured) / SME (unsecured)	Profit making entities for atleast 2 years, positive net worth, turnover criteria, satisfactory gearing, current ratio and DSCR and satisfactory repayment track record, external credit rating and geography (in case of FIG)	1 to 7 years	Upto 5 crore	12% -19%	Secured / unsecured
Overdraft against FD	Margin of upto 15% on fixed deposit	Upto 1 year	Upto 1 crore	2% above FD rate	Secured

Source: Provided by Suryoday Bank to the author

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Digital Finance: Progress and Challenges

8

OVERVIEW AND DIGITAL RAILS

The frenzied pace of development in advancing digital finance and using fintech to deliver financial services makes the topic of financial inclusion inextricably linked to this ensuing digital journey. Innovations are happening in the government's service delivery as well as in financial institutions. Other chapters in this book cover the digital aspect related to the topic of the related chapter. This chapter is more about recent developments in policy and operational issues furthering the digital journey, tracking and analysing progress at a pan-India level, especially in the case of payments, analysing the constraints or barriers to progress, and discussing a few institutional initiatives. The description of constraints being faced at present is not aimed at questioning the digital journey, but is rather geared towards tempering expectations as also to point to the challenges waiting to be addressed.

Foundation: Digital India Programme, India Stack and Open APIs

While there have been numerous initiatives and innovations, if we have to ascribe the foundational work in digital development to anything, it has to be the Digital India initiative of the government, the JAM trinity, and the associated India Stack. Digital India sets the overall vision for the country's digital journey and has three broad areas (Figure 8.1)

Each vision area has sub-objectives and pillars, like internet connectivity, with year-wise targets. The vision setting and target-based approach has added urgency to the Digital India programme,

Digital infrastructure as a utility to every citizen	Governance and services on demand	Digital empowerment of citizens
• High-speed internet • Unique digital identity • Mobile phone and bank account • Common services centre • Private space on the cloud • Secure cyberspace	• Integrated services • Online and mobile services • Portable citizen entitlements • Ease of doing business • Financial transactions—electronic and cashless • GIS as DSS	• Digital literacy • Digital resources • Indian languages • Collaborative digital platforms • No physical submission of documents

Figure 8.1: Digital India Vision

Source: http://digitalindia.gov.in/writereaddata/files/3.CEO%20NEGD%20Digital%20India_12022018_5.pdf

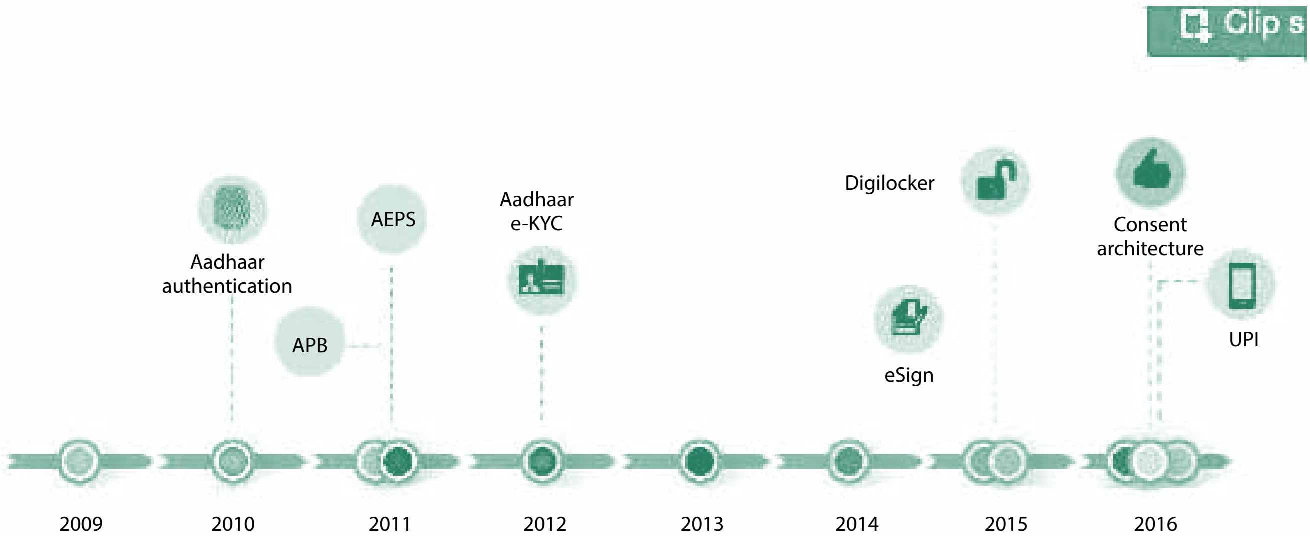


Figure 8.2: The Evolution of India Stack Built on JAM

Source: https://www.slideshare.net/indiastack/india-stack-a-detailed-presentation

which is being anchored and monitored by the MeitY, formed in 2016.

The digital vision has been supported by enabling infrastructure or the ecosystem building carried out since the formation of UIDAI. The foundation of India Stack is a combination of biometric identity in the form of Aadhaar with corresponding bank accounts and mobile phones linked to Aadhaar, which are together called the JAM trinity, and other innovations built on this foundation like Digi Locker for cloud-based data storage and simplified payments through the UPI. The progress over the years in the building of India Stack is shown in Figure 8.2. The benefits of these changes are: (i) separation of place and identity through biometric identity; (ii) digital records, eliminating paper records; and (iii) bringing all bank accounts belonging to an individual on a single application, promoting cashless behaviour.

Along with the government's policy push for the Digital India programme, JAM and India Stack, open APIs complete the digital rails. Open APIs allow providers to capitalise on these assets by letting third parties develop software programs that can 'talk' to their platforms. An API makes it easy for one application to 'consume' capabilities or data from another application. The provider and the third party enter into a contract, defining what information should be supplied from the platform and what actions will be taken. Once it is executed, the API extracts the data. By connecting third parties to established platforms, open APIs essentially turn providers' platforms into digital rails that a developer can leverage to deliver innovative services to address the needs of many customers.[1] In simple terms, open APIs allow different players to interact with each other and build solutions that leverage the strength of both. For example, a bank may provide open APIs for its platform to mobilise savings for other players like MFIs. This development is leading to the breaking down of silos with ever-increasing innovation, and the fintech story is based on this. In India the government initiated the process by opening up APIs for its various services and data, in addition to Aadhaar and its associated India Stack architecture. The website data.gov.in/ogpl_apis has 6,780 APIs on topics as diverse as air quality index, state-wise supply of LED bulbs and water supply.

These developments over the years have laid the bedrock as well as vision for a digital society in India, which should lead to more innovation, transparency, ease of access as well as financial inclusion. In the last year, a few more specific initiatives were taken, and the aspect of data privacy associated with the digital ecosystem also came to the fore.

Developments during Last Year

Umang, UPI 2.0 and rationalisation of charges

MeitY and the NeGD developed the UMANG app to drive e-governance in India. It was launched in December 2017 and provides a single platform for all Indian citizens to access pan-India e-gov services, ranging from central to local government bodies. At present, it has 276 services, 62 applications, and in addition to the union government schemes, it covers schemes of 14 state governments in all.

UMANG intends to deliver major services offered by central and state government departments, local bodies and other utility services from private organisations. It provides a unified approach where citizens can install one application to avail of multiple government services. UMANG has been made available on multiple channels like mobile application, the web, IVR and SMS, which can be accessed through smartphones, feature phones, tablets and desktops. The app is available in 13 languages, including English and Hindi. UMANG is also integrated with Aadhaar and Digi Locker. This allows the system to automatically fetch profile information from the Aadhaar system, and one can avoid filling the same information across services. The Aadhaar linkage also enables e-KYC in cases where Aadhaar details are accepted as an identity proof. By bringing diverse services into one app, UMANG fulfils a major need for simplification and one source application. However, data on user downloads and use of services on UMANG app are not available on the website, which limits examining its popularity and usage.[2]

The UPI, launched in April 2016 by the NPCI, has revolutionised the payments space in India. With its unique features, like the ability to combine multiple bank accounts of the user into one UPI account, a simplified address system and two-factor authentication, it was upgraded in 2018. The UPI 2.0 upgrade was launched as BHIM in mid-August 2018 with the following additional features:

- A one-time mandate for a scenario where money can be transferred later by providing commitment in the present;
- the facility to link overdraft accounts to the app;
- invoice generation option to boost transparency—designed for customers to check the invoice sent by the merchant prior to making a payment; and
- signed intent and QR designed for customers to check the authenticity of a merchant while scanning the QR code. It notifies the user with information to ascertain whether the merchant is a verified UPI merchant or not.

Though there was much hype about UPI 2.0 before its launch, many of the anticipated features like: (i) doubling of person-to-merchant transaction limit to Rs 2 lakh; (ii) standing instruction for auto-debit from a bank account for services like loan repayment; and (ii) capability to refund money by merchants without initiating another transaction, are not part of UPI 2.0 as they were apparently not approved by the RBI.[3]

While the arrival of UPI 2.0 was awaited, the RBI and the government took a few steps during the year to promote the pace of digital payments. MDR refers to the fee paid by the merchant to the acquirer bank that provides card acceptance infrastructure, like POS machines at shops. While MDR is not levied on the customer, it is to be paid by the merchant and split between the acquirer bank, the issuer bank and the payment platform provider (Visa/Mastercard/RuPay). The RBI revised the MDR on debit-card transactions from 1 January 2018.[4] In place of the earlier transaction size-based MDR, the new guidelines introduced a cap, a difference in charges between POS and QR code-based transactions, in addition to dividing merchants into two categories based on their turnover (Table 8.1).

Table 8.1: Revisions in the MDR

Merchant category	MDR for debit card transactions (as a per cent of transaction value)	
	Physical POS infrastructure including online card transactions	QR code-based card acceptance infrastructure
Small merchants (with turnover up to ₹20 lakh during the previous financial year)	Not exceeding 0.40% (MDR cap of ₹200 per transaction)	Not exceeding 0.30% (MDR cap of ₹200 per transaction)
Other merchants (with turnover above ₹20 lakh during the previous financial year)	Not exceeding 0.90% (MDR cap of ₹1,000 per transaction)	Not exceeding 0.80% (MDR cap of ₹1,000 per transaction)

Source: RBI. https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11183&Mode=0. Accessed on 11 July 2018.

In a move parallel to the RBI's revised guidelines on MDR, the Government of India announced that the MDR applicable on transactions made through debit cards, UPI and AEPS that are less than or equal to Rs 2,000 would be borne by the government for a period of two years, with effect from 1 January 2018. It is expected that as a result of this, the government will have to compensate banks and payment platforms to the tune of Rs 2,500 crore.

In August 2018, the GST Council cleared a pilot project to offer digital incentives in the form of cashback of 20 per cent of the GST, paid on business-to-consumer transactions using RuPay and BHIM/UPI platforms, subject to a cap of Rs 100 per transaction. It is reported that the revenue department and the GSTN will coordinate with the NPCI for the development of software to facilitate the refunds in these digital transactions. It will then be started as a pilot project.[5]

Even though the last year did not see any major ecosystem changes compared to previous years, like the launch of the UPI, the initiatives discussed earlier show the intent of the government, in tandem with the RBI, to 'nudge' people towards digital transactions, even at a cost to the exchequer, by providing discounts and refunds. The focus of these nudges is also clearly on retail segments and low-value transactions. The reported cash shortage across a few states, reported in mid-2018, frequent occurrences of dry ATMs and unavailability of desired denomination notes also seem to be part of that 'nudge'.

The RBI Working Group on Fintech and Digital Banking

The FSDC–SC had set up a working group to examine the granular aspects of fintech and its implications so as to review and reorient the regulatory framework appropriately. Considering the wide-ranging issues involved, the RBI set up an inter-regulatory working group, comprising representation from the RBI, SEBI, IRDA, and PFRDA, from select financial entities regulated by these agencies, rating agencies such as CRISIL, and fintech consultants and companies.

Terms of reference of the working group[6]

- To undertake a scoping exercise to gain a general understanding of major fintech innovations/developments, counterparties/entities, technology platforms involved, and how markets and the financial sector in particular are adopting new delivery channels, products and technologies.
- To assess opportunities and risks arising for the financial system from digitisation and the use of financial technology, and how these can be utilised for optimising financial product innovation and delivery to the benefit of users/customers and other stakeholders.
- To assess the implications and challenges for various financial sector functions such as intermediation, clearing and payments being taken up by non-financial entities.
- To examine cross-country practices in the matter and study models of successful regulatory responses to disruption across the globe.
- To chalk out an appropriate regulatory response, with a view to realigning/reorienting regulatory guidelines and statutory provisions for enhancing fintech/digital banking associated opportunities, while simultaneously managing the evolving challenges and risk dimensions.

The report of the working group, made public in February 2018, dwells on topics like what is fintech, impact of fintech on Indian financial services, regulatory and supervisory issues, future work area for stakeholders, and recommendations (Box 8.1).

The key recommendations veer towards a more light-touch approach geared towards encouraging innovations by adopting a sandbox approach and learning by doing things together (collaboration between regulators as well as between banks and fintechs). The potential of digital disruptions and regulatory challenges are real and keep evolving, necessitating a regulatory approach which starts with light-touch and evolves with developments in the field. The modularisation of financial services, referred to in the first chapter, is going to accelerate in the coming years. Technology-enabled modularisation of financial products, wherein one product from origination to distribution is handled by different institutions, will also require interconnectedness between regulators. The idea of a self-regulatory body is a novel suggestion, and the industry should try to build self-regulation centred on innovation and customer centricity, which can then feed into formal regulation.

Box 8.1: Recommendations of the RBI Working Group on Fintech and Digital Banking

- There is a need to have a deeper understanding of various fintech products and their interaction with the financial sector, and thereby the implications on the financial system, before regulating this space.
- The regulatory actions may vary from 'disclosure', to 'light-touch regulation and supervision', to a 'tight regulation and full-fledged supervision', depending on the risk implications.
- There is a need to develop a more detailed understanding of risks inherent in platform-based fintech.
- Various financial sector regulators to identify sector-specific fintech products and regulatory approaches.
- The adoption of digital channels to replace manual, time-consuming processes to empower customers and/or workforce in the insurance sector.
- Innovation labs may be established, including within insurance companies, to combine brand and product managers with technological and analytical resources.
- As and when any securities market fintech products are introduced or emerge in the market, regulators may assess the product and see whether it can be monitored, by way of registering them as an intermediary or through the activity regulations.
- Insurance companies may collaborate with 'insurtech' entities or start-ups to provide better customer experience in a cost-effective manner.
- Financial sector regulators need to engage with fintech entities in order to chalk out an appropriate regulatory response and with a view to realigning regulation and supervision in consideration of the changing environment.
- In order to identify and monitor the challenges associated with the development of major fintech innovations, and to assess response to opportunities and risks arising for the financial system from these innovations, a 'dedicated organisational structure' within each regulator needs to be created.
- An environment for developing fintech innovations and testing of applications/APIs developed by banks and fintech companies to be provided.
- An appropriate framework may be introduced for 'regulatory sandbox/innovation hub' within a well-defined space and duration, where financial sector regulators will provide the requisite regulatory support so as to increase efficiency, manage risks and create new opportunities for consumers in the Indian context, similar to other regulatory jurisdictions.
- Partnerships/engagements among regulators, existing industry players, clients and fintech firms will enable the development of a more dynamic and robust financial services industry.
- Regulators may explore the use of 'Reg Tech', which may facilitate the delivery of regulatory requirements more efficiently and effectively than existing capabilities.
- The organizational structure and HR practices of regulators have to be reoriented to meet the challenges of innovation, in terms of adapted HR hiring profiles, learning and educational programmes.
- There is a need for a stand-alone data protection and privacy law in the country.
- Banks/regulated entities may be encouraged to collaborate with fintech/start-ups to improve their customer experience and operational excellence. They may also consider undertaking fintech activity in areas such as payments, data analytics and risk management.
- Models of engagement and checklist to be developed by each regulator for each of the activities.
- Given that fintech companies are in their infancy but are growing at a rapid pace, the government may consider introducing tax subsidies for merchants that accept a certain proportion of their business revenues from the use of digital payments.
- The requirement of increasing the levels of education/awareness of customers should be highlighted by all market regulators.
- A self-regulatory body for fintech companies may be encouraged.

Source: https://www.rbi.org.in/Scripts/PublicationReportDetails.aspx?UrlPage=&ID=892#ES.
Accessed on 4 September 2018.

Smart Campaign: Roadmap for Client Protection in Digital Credit

Smart Campaign is a global initiative to unite microfinance leaders around the goal of keeping clients at the centre of operations and refocusing microfinance to a double bottom line objective. CFI brings together a global and diverse coalition of microfinance institutions, networks, associations and other stakeholders under the umbrella of Smart Campaign. Global agencies like CGAP, ADB, African Development Bank, and national agencies like SIDBI have endorsed the Smart Campaign. As part of its work on client centricity, Smart Campaign has formulated seven client protection principles and a certification for microfinance institutions. These principles, with their numerous indicators, are aimed at implementing a common code of conduct governing how clients should be treated.

In July 2018, Smart Campaign released a paper on responsible digital credit. The paper, using the client protection principles as a framework, lists the emerging risks and also suggests good practices and steps to be taken by service providers and regulators. At a time when digital finance is emerging as a major disruptor and regulation is evolving, it is critical to mainstream the interest of clients. The paper finds that all seven client protection principles are relevant to digital credit, albeit with a different focus, and it adds one more principle related to security and fraud risk management (Table 8.2).

The paper lists out common problems faced by clients across the eight principles and suggests the parameters to mitigate the risk. For example, under the principle 'fair and respectful treatment of clients', it suggests documenting the reasons for algorithmic features and the policy for call to customers that ensures non-threatening calls. Often clients do not understand why they have been denied credit based on the algorithm, which is a feature associated with digital, and hence there should be a policy to make clients understand the rationale.

While digital and fintech are supposed to facilitate credit and accelerate turnaround time, the risks associated with credit, disbursed in a minute or so, are also coming to the fore. CGAP,

Table 8.2: Proposed Consumer Protection Standards for Digital Credit

Industry digital credit standards	• Detailed practices
Appropriate product design and delivery	• Matching product design and usage • Using appropriate mobile technology experts when designing for mobile channel delivery • Advertising and marketing best practices
Prevention of over-indebtedness	• Avoidance of debt traps • Responsible underwriting • Responsible credit-reporting/sharing • Pressure-free loan principles
Transparency	• Borrower disclosure standards • Investor disclosure standards (P2P platforms)
Responsible pricing	• Pricing terms and standards that are reasonable and affordable
Fair and respectful treatment	• Clear collection policies and procedures • Fair collection practices
Data privacy and usage	• Responsible data usage • Consistent review of data privacy standards • Consent to communicate electronically • Informed consent and opt-in/opt-out policies • Management of third-party providers to protect client data
Complaint resolution	• Timely, clear and responsive complaint resolution practices
Security and fraud risk management	• Authentication practices • Industry standards on security compliance

Source: John Owens, Responsible Digital Credit (Washington, D.C.: Center for Financial Inclusion at Accion, 2018).

in its blog on digital credit in Kenya, points to this risk by saying: 'The rise of the digital credit market has raised concerns about the risk of excessive borrowing, and over-indebtedness, among lower-income households. Digital loans are easy to obtain, short-term, carry a high interest rate, and are available from numerous bank and non-bank institutions'. Another newspaper report from Kenya, where digital credit has become mainstream, talks about how Kenyans have been lured into the debt trap. The easy availability of credit, requiring only a smartphone and allowing lenders access to social media accounts of the borrower, creates an irresistible allure for borrowers of instant credit, as opposed to the onerous loan application process of microfinance institutions and banks. This is reported to have led to the use of loans for purposes such as betting, balancing multiple loans (taking a loan from one to pay off another), and causing or increasing indebtedness.

The CFI paper, in talking about risks of digital credit, also flags this issue. It rightly says:

> While regulators, policy makers and consumer protection advocates, have advocated for simpler and easy to use digital financial services, including digital credit, very simplistic products, that offer near automatic access to credit, come with their own risks. When combined with push marketing, easy to use digital credit models, with artificially short timelines, may force borrowers to make too quick, unconsidered decisions. This is a particular issue for credit delivered via mobile phone, primarily due to the instant, automated, and remote nature of the transaction, as well as mobile screen size limitations.

While the country contexts will be different, it is important to have a principles-based client protection matrix for digital credit and fintech. It is heartening that the RBI's working group report talks about light-touch regulation, backed by self-regulatory initiatives. Global initiatives like Alliance for Financial Inclusion, the World Bank, Smart Campaign and the ITU working group on digital finance have brought out high-level principles for digital finance, which can be used as basic framework and adapted to suit the country context. Annexure 8.1 contains the World Bank's 'Good Practices for Financial Consumer Protection', adapted to digital finance.

Privacy of data is part of the client protection framework, and in the current year, India has seen a lot of debate on this issue. As it is central to the financial inclusion discourse, the issue is discussed in some detail in the following section.

AADHAAR LINKAGE, DATA PROTECTION AND FINANCIAL INCLUSION

Aadhaar is at the core of the JAM trinity and an enabler for financial inclusion by being the common KYC across agencies, replacing PIN or password with biometric authentication in financial transactions, as also acting as the identifying thread for the credit bureau. While Aadhaar enrolment and linkage is ongoing, the year saw numerous reports of data leakage,[7] denial of services on account of non-linkage of Aadhaar,[8] or failure of biometric authentication, the security of Aadhaar data. There were questions on whether the linkage of bank accounts, mobile phones and every other government service will lead to a surveillance state. The data leaks involved government agencies as well as private agencies, exposing personal information, client names, their unique 12-digit identity numbers and their bank details. While the leakage of personal information and its misuse is widely contested on both sides, there is unanimity on the ill effects of denial of services due to non-linkage of Aadhaar. Various news reports of denial of food ration and some cases of starvation deaths blamed on Aadhaar forced the government to issue instructions on non-denial of services using Aadhaar as a pretext.

The Aadhaar project, Aadhaar Act, 2016 and a host of issues linked to it, like mandatory linkage to bank accounts and tax returns, have been challenged in the courts. The Supreme Court collated 27 different petitions before a five-judge constitution bench, and the year 2018 saw marathon hearings lasting 38 days, which are said to be the second longest hearings after the Keshavananda Bharti case that questioned if Parliament's power to amend the Constitution was unlimited, to the extent of taking away all fundamental rights. As of mid-August 2018, the judgement has been reserved by the Supreme Court, and as a result the project of mandatory linking of Aadhaar has also been deferred.

The essence of the arguments against the Aadhaar project relate to the sharing of biometric information as violation of the right to privacy, mandatory linking leading to fears of state surveillance, sufficiency of protection of massive amounts of data stored with Aadhaar, and whether the state has a right to exclude people from welfare schemes in the absence of Aadhaar. Opponents have argued that what was supposed to be a scheme for better targeting of welfare schemes has been expanded to cover all facets of life, leading to a 360-degree profiling. It is further argued that the use of data by private agencies, in the absence of any data protection law, is open to misuse. The UIDAI and proponents of Aadhaar on the other hand, have explained how Aadhaar is safe, keeps minimal information and cannot be used for profiling. UIDAI came out with full-page advertisements on the facts about Aadhaar and posted an FAQ on the myths associated with Aadhaar on its website—a very useful set of information.[9] As a second layer of safety, the UIDAI introduced VID in June 2018.[10] The VID can be generated by an Aadhaar cardholder from the UIDAI website, and the same can be produced for various authentication purposes instead of sharing the actual 12-digit biometric ID. UIDAI also made it mandatory for all telecom operators and e-sign service providers to start accepting the VID from 1 July 2018 instead of the Aadhaar number, while banks will have time till 31 August to deploy the new feature. VID is a critical security measure for protecting people's privacy and their Aadhaar information.

The Aadhaar debate has been so complex that it is difficult for a layperson to form an opinion. While the Supreme Court's decision is awaited, one thing is definite that this controversy has created apprehensions in the minds of people related to Aadhaar-based profiling and has also affected the entire financial inclusion space. Viewed from a financial inclusion perspective of low-income clients, people have argued that a vocal minority of citizens have hijacked the debate and dented the financial inclusion drive based on Aadhaar. It has been argued that centralised authentication is far superior to distributed and varied authentication, and biometric-based financial transactions suit the poor far better than other smart card and pin-based options. Financial institutions have also borne the brunt of this uncertainty—starting with a massive drive to link Aadhaar in the first quarter of 2018, followed by an indefinite extension, and now having systems in place to accept VID authentication. International organisations, be it CGAP or the World Bank or ITU, have also hailed Aadhaar as the driver of financial inclusion in India by providing a robust KYC.[11]

Probably, the truth lies somewhere in between. There is no doubt that Aadhaar has helped the cause of financial inclusion, and a person at the margins is more concerned about access to services than to debates on surveillance and data privacy. However, in a democracy, even a minority voice counts and rightly so. The result of this has been improvements in Aadhaar, like data storage guidelines for global and local user agencies and VID as authentication. While the balance between financial inclusion objectives and concerns of citizens occupied most of the year, and the Supreme Court judgement will provide finality to this debate, it can be said that probably limiting Aadhaar to financial inclusion and welfare schemes in a non-mandatory manner could have helped in avoiding this situation. Mandatory linkage of Aadhaar and expanding the scope to include almost all services gradually could have also avoided this situation. News reports of people dying of starvation due to the mandatory requirement of Aadhaar roused the conscience of the nation and did much damage to the cause of Aadhaar and the JAM trinity.

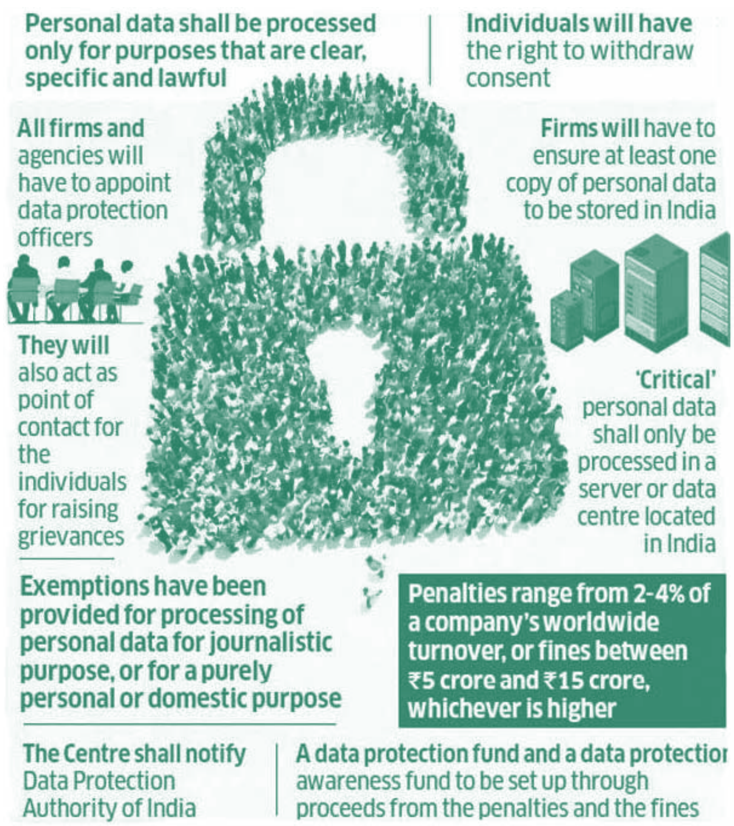
'…a person at the margins is more concerned about access to services than about debates on surveillance and data privacy.'

Debates are the essence of democracy, and listening to the concerns of every segment of society often leads to superior policy outcomes. Aadhaar is no exception to this, and in addition to measures initiated by the UIDAI to add security layers, another positive outcome of this debate was the constitution of the Justice B.N. Srikrishna committee on a data protection law for India. The committee submitted its draft report in July 2018. Now the government has to examine it, take the views of stakeholders, get it cleared through cabinet and then pass the legislation in Parliament. While this process may take some time, it has set a framework for data protection, which will also affect the Aadhaar Act, 2016. Justice Srikrishna succinctly captured the core principle of a data protection law by saying that 'The citizen's rights have to be protected, the responsibilities of the states have to be defined, but the data protection can't be at the cost of trade and industry.'[12]

Box 8.2 gives some of the highlights of the Srikrishna report. The recommendation for a data protection agency, storing of critical data in India and provision for penalties are some of the key suggestions in the report.

Since its release, the report has again generated an expected debate. It has been argued that the committee exceeded its brief of framing a data protection law and became a proponent of the digital economy; the committee had majority representation from the government; much of the issues outlined in the earlier white paper have been diluted; the penalty framework is lenient on government data breaches; exemption given for national security may become a tool for surveillance; and the concept of data localisation may increase cost of business as well as invite backlash from countries which outsource data processing to India.[13] Others have argued that personal data is key to the digital economy, and there is no point stepping back from the digital promise. But what is important is that the committee ring-fences personal data with concepts of collection and purpose limitation, penalties for breaches, as well as a dedicated agency overseeing the data protection regime. Coming months will see some closure through the court judgement as well as the data protection law. It is hoped that the outcome will balance data privacy concerns with welfare and financial inclusion objectives. The policy has to recognise that apart from data issues, the key concern to be addressed from a financial inclusion perspective is that Aadhaar is an enabler and it should not be used to discriminate or deny services to anybody.

Box 8.2: Key Recommendations of the Srikrishna Committee



Source: https://economictimes.indiatimes.com/news/politics-and-nation/justice-bn-srikrishna-committee-submits-report-on-data-protection-here-re-the-highlights/articleshow/65164663.cms. Accessed on 1 September 2018.

PROGRESS IN DIGITAL PAYMENTS

The Payments Landscape

The policy nudge towards the digital ecosystem had set a goal of 25 billion digital payments during 2017–18. This was labelled as too ambitious, as it required matching infrastructure, and more importantly, behavioural changes. The policy has tried to work on both these constraints, and there are positive results. The progress on digital payments from a financial inclusion perspective needs to analyse the changes in infrastructure as well as retail payments. The payments landscape in India as of now consists of both retail payments and SIFMI, which has more to do with government securities market, foreign exchange and RTGS (Figure 8.3). See Annexure 8.1 for brief details of payment instruments in Figure 8.3.

If paper-based clearing and SIFMI are excluded, the remaining payment instruments give us a picture of retail payments. Though the RTGS is part of SIFMI, as it relates to transaction values over Rs 2 lakh, customer transactions are also part of it and reported by the RBI separately. In our analysis of retail payments, we have included customer transactions under RTGS, as they account for nearly 95 per cent of the RTGS volume. The ecosystem consists of payment instruments/gateways managed by the RBI (RTGS, NEFT, ECS) and NPCI (IMPS, UPI, NACH). The exclusion of other instruments of SIFMI do affect the overall analysis of value, as

1. RTGS	3. Government Securities Clearing
Financial Markets Clearing (2+3+4)	4. Forex Clearing
2. CBLO	Total SIFMIs (1 to 4)
Retail Payments	
Paper Clearing (5+6+7)	(IMPS) UPI
5. CTS	
6. MICR Clearing	12. NACH
7. Non-MICR Clearing	Card Payments (13+14+15)
Retail Electronic Clearing (8+9+10+11+12+UPI)	13. Credit Cards
	14. Debit Cards
8. ECS DR	15. PPIs
9. ECS CR	
10. EFT/NEFT	Total Retail Payments (5 to 15+UPI)
11. Immediate Payment Service	

Figure 8.3: Systematically Important Financial Market Infrastructure

Source: Niti Aayog, Digital Payments: Trends, Issues and Opportunities (New Delhi: Niti Aayog, 2018).

Table 8.3: Data on Technology Enabled Touchpoints and Transactions over the Years

	2013	2014	2015	2016	2017	2018	May '18
Infrastructure (in thousand)							
Onsite ATMs	56	83	89	102	110	107	107
Offsite ATMs	58	77	92	97	99	100	103
Online POS	841	1,050	1,126	1,385	2,526	3,083	3,247
Total touchpoints	968	1,226	1,308	1,585	2,737	3,290	3,457
Credit cards (in million)							
Outstanding credit cards	19.54	19.18	21.11	24.51	29.84	37.48	38.60
Transactions at ATMs	0.23	0.3	0.44	0.61	0.49	0.79	0.74
Transactions at POS	35.62	46.11	56.91	72.22	107.61	127.29	137.66
Amount at ATM (in Rs billion)	1.49	1.66	2.34	2.8	2.29	3.69	3.49
Amount at POS (in Rs billion)	111.22	145.49	178.99	226.94	333.9	443.08	470.52
Debit cards (in million)							
Outstanding debit cards	331.2	394.42	553.45	661.82	854.87	861.08	925.11
Transactions at ATMs	482	571.5	624.21	731.72	710.11	774.94	748.04
Transactions at POS	45.38	56.98	76.11	112.87	271.17	318.90	352.12
Amount at ATM (in Rs billion)	1,556.41	1,796.10	######	2,245.82	2,259.46	2,663.50	2,647.51
Amount at POS (in Rs billion)	66.87	85.77	108.28	134.63	356.99	418.57	468.08
No. of ATM transactions per debit card	1.46	1.45	1.13	1.11	0.83	0.90	0.81
No. of POS transactions per debit card	0.14	0.14	0.14	0.17	0.32	0.37	0.38

Notes:
1. The numbers for 2017 pertain to the ATMs of 56 SCBs and for 2018 for 49 SCB in the following ownership category—foreign banks, public sector banks (including IDBI Bank), and old and new private sector banks. However, some foreign banks, RRBs, SFBs and all the co-operative banks (both rural and urban) were left out. Total reported ATMs are 22.2 lakh. Numbers for May 2018 pertain to 49 SCB, 7 payment banks and 10 small finance banks.
2. Apart from these ATMs of banks, there were 14,451 white label ATMs in 2017 which increased to 15,195 in March 2018.

Source: ATM/POS/Card Statistics at https://rbi.org.in/scripts/ATMView.aspx and region-wise ATM statistics at https://rbi.org.in/SCRIPTS/StateRegionATMView.aspx. Accessed on 4 August 2018.

SIFMIs accounted for 1 per cent of all payments in volume, and 89 per cent in value during 2017–18.[14] The analysis however is focussed on retail payments because in volume of transactions, the retail segment accounts for 99 per cent and is also more indicative of the digital change. G2P transactions in the form of DBT are an integral part of the digital story and hence analysed separately.

The Infrastructure

The key to digital payments is the transaction infrastructure in terms of ATMs, POS devices, debit and credit cards, and the associated transactions.

The policy intent is clearly visible in the touchpoints, with the number of ATMs seeing a decline for the first time in the last six years by 2.5 per cent in 2018. This combined with news reports of non-functioning ATMs or dry ATMs add up to the digital push, as ATM transactions are done to withdraw cash, which goes against the digital ecosystem being built. This change is being supported by higher POS terminals, which have seen a more than 100 per cent jump in two years, though per population coverage of POS still remains far below the benchmark in developed countries. Still, the change is noteworthy, as after a period of low growth during 2013–16, where the number of POS increased from 0.84 million to 1.3 million, now it has touched 3.2 million. In the cards space, debit cards have the predominant share, accounting for 96 per cent of all cards issued in India. The growth trajectory in the number of debit and credit cards has been following a steady upward trend with no major fluctuations (Figure 8.4). The slightly steep increase in debit cards during 2014–2017 can be attributed to RuPay debit cards issued with PMJDY accounts.

While the infrastructure in terms of reduced ATMs, doubling of POS and a steady growth in cards tells a positive story of the digital journey, transactions also tell a similar story.

Annual growth in transactions through both debit and credit cards at POS is significantly more than at ATMs, in volume as well as in value (Table 8.4). While card transactions at ATMs are also growing, POS transactions are growing at a faster pace. Moreover, the average rupee transaction made at ATMs has also remained more or less stagnant in the range of Rs 3,000 to Rs 3,500. The figures in the table indicate that the increased availability of POS has translated into increased use, which is a positive sign of customer adoption. The propensity of cash withdrawal through ATMs has at least not increased in average value, while increase in the number of transactions are due to the increase in cards issuance. Overall on the infrastructure side, while there are positive outcomes, the availability of POS is still an issue of concern. Even after a 200 per cent jump in the last two years, the number of POS available per million people in India stands at 2,539 in 2018. This compares very unfavourably with other countries like Australia (39,337), Canada (38,870), Singapore (33,219) and China (17,744).[15] It puts in perspective the digital infrastructure work to be done—without an ecosystem wherein the POS, either working on cards or QR code, is easily available, the propensity to withdraw and use cash will persist and grow, as the data reveals.

Table 8.4: Transactions during 2017–18 (in per cent)

	Growth in number of transactions	Growth in value of transactions
ATMs	9.17	17.93
POS	17.80	24.72

Source: RBI data on payments.

There have been several studies on understanding why POS availability remains low in India. Most have cited the high cost of POS (around Rs 10,000), MDR and turnover issue of low-volume enterprises as the major reasons for low penetration of POS. It would be right to say that the demand for POS has also to be seen from the perspective of customers: if customers demand POS payments over cash, merchants will have to invest in POS infrastructure. In a recent survey of 2,500 small businesses in Jaipur by Catalyst & Price, merchant perceptions

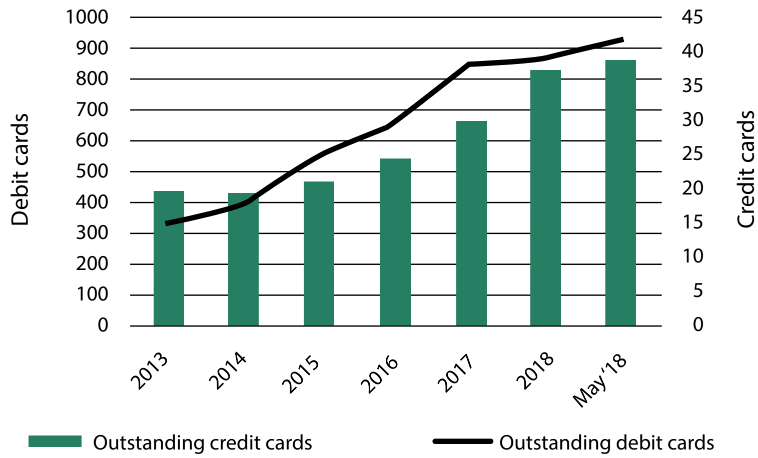
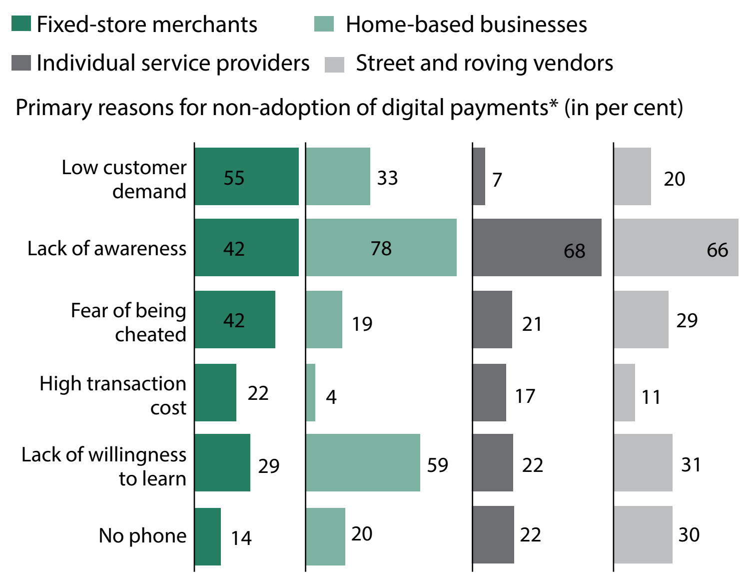


Figure 8.4: Debit and Credit Cards (in million)

on adopting digital payments differed according to their profile. Though this survey covered both POS and phone-based digital payments like UPI, the results threw up interesting insights. While the primary reason for fixed-store merchants was low customer demand, among smaller enterprises, comprising of home-based business and street vendors, lack of awareness was the major reason. Surprisingly, among the small enterprises, nearly 25 per cent cited not having a phone as the major reason (Box 8.3). Overall, the survey showed that

Box 8.3: Digital Payments—
A Survey of Merchant Perceptions



Source: Live Mint. https://www.livemint.com/Opinion/nuRRlsiLkbMMRLJ7iAN-5nN/Opinion-What-makes-merchants-adopt-digital-payments.html. Accessed on 14 August 2018.

the issues are specific to particular segments, and may also differ based on geography, making the situation more complex. Behavioural issues in the form of lack of awareness and fear of getting cheated are also a strong factor. Another interesting finding of the survey was that as against the conventional digital logic that cash is prone to theft and has a cost, 'less than 1% of the merchants reported any cash being stolen in the past year, and experienced no significant cash handling or reconciliation concerns'. Thus, the cost to business of dealing in cash is not significant, though other players in the value chain like banks have a cost in dealing with cash.

Thus, at present there is no single point to be addressed in boosting digital payment infrastructure, but a host of issues ranging from awareness of both consumers and merchants, availability of phones or POS at an acceptable cost and security perceptions need to be addressed. This could be the reason for cash transactions going back to pre-demonetisation levels.

Trends in Retail Digital Payments

This section analyses the trend in retail digital payments, excluding SIFMIs except RTGS which also has a retail customer segment. The period of analysis is from August 2016 till May 2018. August 2016 has been taken as the start to see the picture before demonetisation in November 2016, and May 2018 is the month up to which data is available across all retail digital channels at the time of report writing in mid-August. In some cases, data is also available for the month of June, but for the sake of consistency May 2018 has been taken, as data across all channels is available for May.

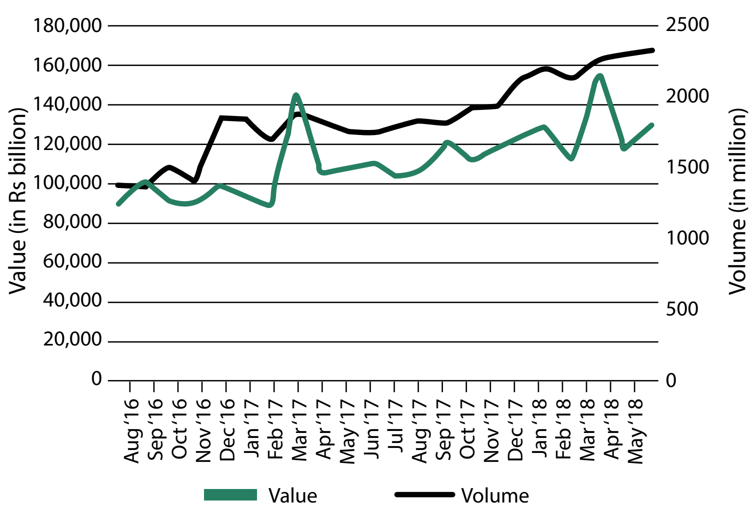


Figure 8.5: Growth in Digital Retail Payments

Source: RBI RBI. https://www.rbi.org.in/Scripts/BS_ViewBulletin.aspx?Id=16609. Accessed on 5 August 2018.
NPCI.https://www.npci.org.in/product-statistics/upi-product-statistics. Accessed on 6 August 2018.

Although the payments landscape has been described in section 3.1, it needs to be reiterated in terms of what has been included in analysing digital retail payments. Various papers and reports use different measures, and the attempt here is to be comprehensive. Payment channels included are RTGS (customer transactions), NEFT, ECS, NACH, IMPS, UPI, *99#, PPIs, credit cards and debit cards. The data used for the analysis has been taken from the RBI[16] and the NPCI,[17] and the full month-wise data set across these channels is given in Annexure 8.2.

25 billion target turning into reality…

The composite trend in growth of retail digital payments has been impressive during the period August 2016 to May 2018, clocking a growth of 68 per cent in volume and 43 per cent in value. Nearly 70 per cent growth in volume of digital transactions is a testimony to the policy push, demonetisation and the Digital India programme. The total volume of retail digital payments touched 2.3 billion transactions in May 2018, with a value of Rs 129,022 billion. In August 2016 the volume was 1.3 billion. Even if RTGS (customer transactions) is excluded, the figures do not change much, as RTGS accounts for 11 per cent of the total volume.

In the union budget for 2017–18, the finance minister had announced a target of 25 billion transactions during the year through UPI, USSD, Aadhaar Pay, IMPS and debit cards.[18] If the twelve-month period ending in May 2018 is considered, total retail digital payments touched 24.8 billion, almost on target. It is acknowledged that the finance minister had used the financial year as a reference and also limited the payment instruments, focussing on newer initiatives of IMPS and UPI, but the thing to be celebrated here is the spirit of moving towards digital payments, and the fact that significant progress has been made. For record's sake, if the count is limited to UPI, USSD, IMPS and debit cards, total transactions in the last twelve months were 14.63 billion.

Trends across channels: Cards dominate despite the UPI surge

A comparison of various retail digital payments channels' contribution to volume and value of transactions between August 2016 and May 2018, along with the growth percentages, throws up interesting insights on developments in the last two years.

Table 8.5: Percentage Share of Different Retail Digital Payment Channels and Growth

	August 2016 (per cent share)		May 2018 (per cent share)		Growth (in per cent)	
	Volume	**Value**	**Volume**	**Value**	**Volume**	**Value**
RTGS	0.62	86.20	0.50	81.95	34.23	336.26
ECS	0.13	0.01	0.03	0.01	-67.42	-13.01
NEFT	8.56	9.74	7.46	13.29	45.85	95.71
IMPS	2.45	0.30	5.03	0.84	244.11	304.39
NACH	11.08	0.76	10.23	0.75	54.63	41.75
UPI	0.01	Negligible	8.18	0.26	2,03,641	1,073,722
Credit cards	6.11	0.29	5.97	0.37	63.32	81.96
Debit cards	64.09	2.64	47.47	2.41	24	30.90
PPI	6.96	0.06	15.13	0,12	264.29	174.90

Notes:
1. USSD has been excluded because of negligible share.
2. UPI growth percentage looks abnormally high because of a very low base.

Table 8.5 provides a clear snapshot of what is happening across channels. As the number of transactions provides a better answer to digital deepening as well as its alignment with the government's target, it can be inferred that all channels are growing, except ECS which is on account of ECS transactions moving to NACH. The high growth channels are the UPI, IMPS and PPIs. A valid inference can be drawn from the data points that despite the surge in transactions under new channels, debit cards continue to account for nearly 50 per cent of retail digital payments, and it needs to be considered whether the financial inclusion objective will be better served by promoting card-based payments. This is so because debit cards have been in existence for long and a large section of society has become used to them. Further, PMJDY has ensured last-mile delivery of debit cards. Another positive feature associated with cards is that their use at POS for merchant transactions has seen an increase, and while the high reached during demonetisation has dipped considerably, it is still high as compared to the pre-demonetisation period (Figure 8.6).

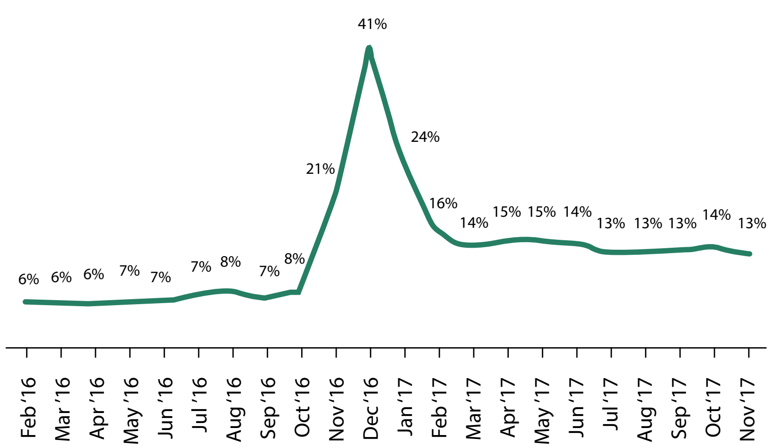


Figure 8.6: POS Share of Total POS and ATM Spend

Source: MasterCard internal data.

This is a welcome feature, as the higher share of ATM usage implies that cash is being required to make transactions, while POS transactions reduce the need for cash. Possibly, with higher availability of POS machines, the share will go further up.

Despite the talk that with the advent of the UPI, which is linked directly to bank accounts, PPIs will soon be a thing of the past as they have the limitation of cash-in and cash-out through a bank account, the figures do not suggest so. PPI transactions also grew by 265 per cent in the two-year period, though not as fast as the UPI. This suggests that customers who are tech savvy and appreciate the features of a particular PPI are ready to accept the limitation.

The phenomenal surge in the UPI: Is it an affluent middle-class phenomenon?

Monthly transactions through the UPI crossed the 200-million mark for the first time in June 2018 as per the NPCI data. The UPI recorded 246.37 million transactions amounting to Rs 40,834.03 crore during June 2018, which is an increase of 30 per cent in transaction volume compared with the

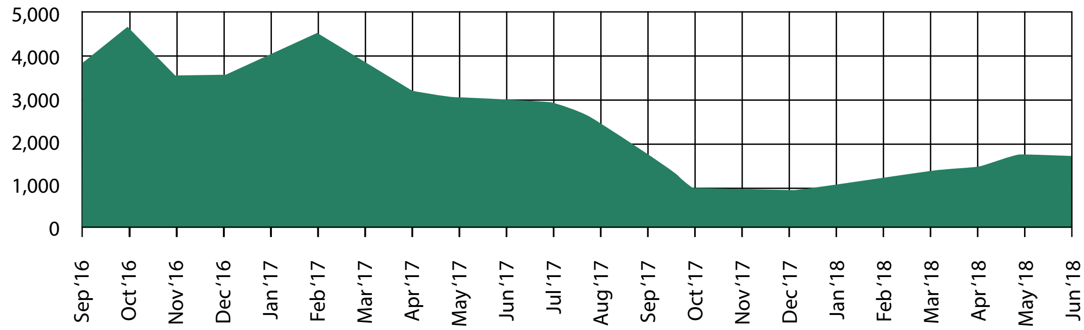


Figure 8.7: UPI Average Transaction Value (in Rs)

Source: NPCI website.

189.4 million transactions worth Rs 33,289 crore in May. The highest volume of transactions on a single day was recorded on 20 June with more than 10 million transactions on the platform. Of the total UPI transactions recorded in June 2018, 16.3 million transactions amounting to Rs 6,261.3 crore took place through the BHIM platform.

Figures clearly show the popularity of the UPI backed by its adoption by banks and other players. Total monthly transactions grew twelve times over a one-year period (June 2017 to June 2018). Analysis of the average amount transacted shows that with maturity the average amount is falling, which shows that the UPI is being used for small day-to-day transactions. The average amount transacted in June 2018 was Rs 1,657 (Figure 8.7).

However, it is not possible to decide the impact of the UPI's growth on financial inclusion as the NPCI does not provide data on place of origin of transactions to analyse the UPI's geographical traction, both state-wise and rural/urban. Recent reports suggest that out of 189.4 million transactions in June 2018, nearly 150 million are accounted for by Paytm, PhonePe[19] and Google Pay. As the NPCI does not release these figures, it is difficult to verify these claims, and accordingly there have been rival claims by these companies on their share.[20] These are apps built on the UPI platform for payments and derive their maximum customer base from tie ups with online merchants like eBay, Flipkart, Amazon and other e-commerce, travel and merchandise platforms. Also, much of these transactions take place on the back of lucrative discounts being offered, as the race is to acquire a customer base. How long such transactions will sustain is a moot point. If the UPI's growth is driven by these apps, it can be said to be boosting digital payments, but seems to be of not much relevance to the financial inclusion space. It is a broad generalisation, but most will agree that these apps largely cater to the affluent middle class for their e-commerce purchases, and the lower average ticket size of the transactions does not seem to indicate any deepening.

From a financial inclusion perspective, the USSD *99# channel and the number of Aadhaar-based authentications can be a measure, as the former has been created for users with basic mobile phones (known as feature phones) and the latter is more prevalent in rural areas.

*The declining trend in the *99# channel and the steady growth in the AEPS*

The code *99# is a USSD-based mobile banking service of the NPCI that was initially launched in November 2012. It was dedicated to the nation by the prime minister on 28 August 2014 as part of the PMJDY. When the UPI was launched in 2016, which is a mobile application-based solution primarily catering to Android/internet compatible phones (smartphones), the NPCI also enabled the UPI for non-internet-based mobile devices (smartphones as well as feature phones) in the form of a dialling option (*99#), which is known as USSD 2.0. This option is intended to take banking services to the last mile, considering that most people in India do not own smartphones (about 70 per cent of the more than one billion connections are still using feature phones). It enables customers to transact through an interactive menu displayed on the mobile screen by dialling *99# on their basic phones. Services include sending and receiving funds from one bank account to another and balance enquiry, which can be

Table 8.6: *99# Transactions in 2017–18

Month	No. of transactions	Value (in Rs million)
January 2017	3,08,383	54.136
February 2017	2,22,159	59.203
March 2017	2,08,141	82.937
April 2017	1,87,146	97.15
May 2017	1,90,500	76.058
June 2017	1,98,815	81.105
July 2017	1,90,584	84.347
August 2017	1,91,812	82.443
September 2017	2,02,700	71.406
October 2017	1,84,557	98.545
November 2017	1,82,523	94.302
December 2017	1,79,852	80.634
January 2018	1,72,811	82.057
February 2018	1,56,073	94.195

Source: NPCI website.

accessed in 13 different languages, including Hindi and English. Considering its objectives and features, this option can be said to be catering to the financial inclusion of BoP customers.

However, while the UPI has 114 live banks on its platform at present, the *99# channel has only 49 banks, which means a majority of the banks do not offer this service. Further, after its relaunch as USSD 2.0, the channel is provided by all GSM service providers. Despite this, the service has not seen much traction. The volume of transactions is on a declining trend, while volume is almost stagnant, implying an increase in average transaction value. Its utility as a channel serving low-income customers is also demonstrated in its average value of transaction of Rs 603 in February 2018, which is much lower than the average UPI transaction of Rs 1,657 and of around Rs 3,500 for cards.

The NPCI or banks need to study the factors impeding the growth of the *99# channel as a majority of the population with basic phones are its customer base. Anecdotal evidence suggests that the *99# channel is difficult to use and is relatively expensive for the average transaction value, as the telecom companies charge for every step of the several steps that comprise every transaction using the channel. This per step charge could be as high as Rs 1.50, which makes the use of the service for money transfer often unviable. Moreover, transaction failures have been reported while money transfers were being attempted. Thus issues of viability and reliability for low-value users are factors that need to be looked into.

The AEPS is a bank-led model which allows online interoperable financial transaction at the POS (micro ATM) through the BC or bank mitra of any bank using Aadhaar authentication. As most rural BCs use Aadhaar as authentication, this also provides a useful measure of digital financial inclusion. For making financial transactions under the AEPS, one needs to remember one's Aadhaar number and the name of the bank to which it is linked. During field visits, it was seen that BCs normally noted down the Aadhaar number of the customer in the latter's passbook obviating the need to remember the 12-digit number.

AEPS transactions have grown five times in the two-year period, however growth is much slower as compared to other new channels like the UPI. The number of AEPS transactions in May 2018 accounted for 4.9 per cent of the total volume of retail digital payments. This shows there is lot of scope for increase in AEPS transactions. People in rural areas prefer AEPS at Bank Mitras, wherein they are assisted with their bank transactions and simple AEPS-based biometric authentication.

DIRECT BENEFIT TRANSFER: A BIG LEAP FORWARD, BUT…

DBT has been the pillar of the digital ecosystem in India. It was started in 2013 as a means for better targeting of welfare schemes, and consequent savings for the public exchequer. The DBT architecture rides on bank accounts linked with Aadhaar and the network of Bank Mitras for client-level transactions. It started with 43 districts and later 78 more districts were added in 27 schemes pertaining to scholarships, and women, child and labour welfare. Post-2014, there were two major changes driving the DBT's growth. First, the DBT mission was transferred from the department of expenditure to the cabinet secretariat in September 2015. Second, the scope of the scheme was expanded across the country in December 2014.

As of August 2018, 435 schemes of 56 ministries are covered under the DBT scheme, which the DBT operates in both cash transfer and kind (physical delivery of food and fertiliser) modes. For cash transfer, bank accounts seeded with Aadhaar are the backbone, as transfers are done using the APBS developed by the NPCI. The ABPS platform links government departments and their banks on one side and beneficiary banks and beneficiaries on the other. Kind transfers, like distribution of fertiliser, require the person to authenticate oneself on the biometric device with the retailer.

Bringing 435 schemes under its net, the scope of the DBT has increased immensely in the last two to three years, and this is reflected in the amount of money channelled through the DBT as well as the number of beneficiaries covered under the scheme. During 2017–18, the government transferred Rs 1,70,292 crore under the DBT, as compared to Rs 74,689 crore in the previous year, a jump of more than 100 per cent (Figure 8.8). There has also been a massive growth in number of beneficiaries covered under the schemes, which touched 124 crore. This appears high as it is a cumulative number of various schemes, and one person could be covered under more than one scheme, increasing the count.

However, a major chunk of the DBT transfer (around 75 per cent) is accounted for by the cooking gas subsidy, PDS of foodgrains and the employment guarantee scheme (MGNREGS). According to government statistics, savings to the public exchequer during 2017–18 on account of the DBT was Rs 32,983 crore. These savings have mainly accrued from detection of fake cooking gas connections, fake ration cards, ghost MGNREGS beneficiaries as well as the voluntary giving up of subsidy by many. Details of savings across schemes with reasons are given in Annexure 8.3.

How Is the DBT Faring on the Ground?

It is critical to examine the perception of beneficiaries covered under the DBT, as the state saving money from it can only be a positive externality and not the core objective. Various studies of the DBT provide a mixed picture.

J-PAL study of the PDS

J-PAL did a study for Niti Aayog in 2016–17, covering food subsidy operation in the three union

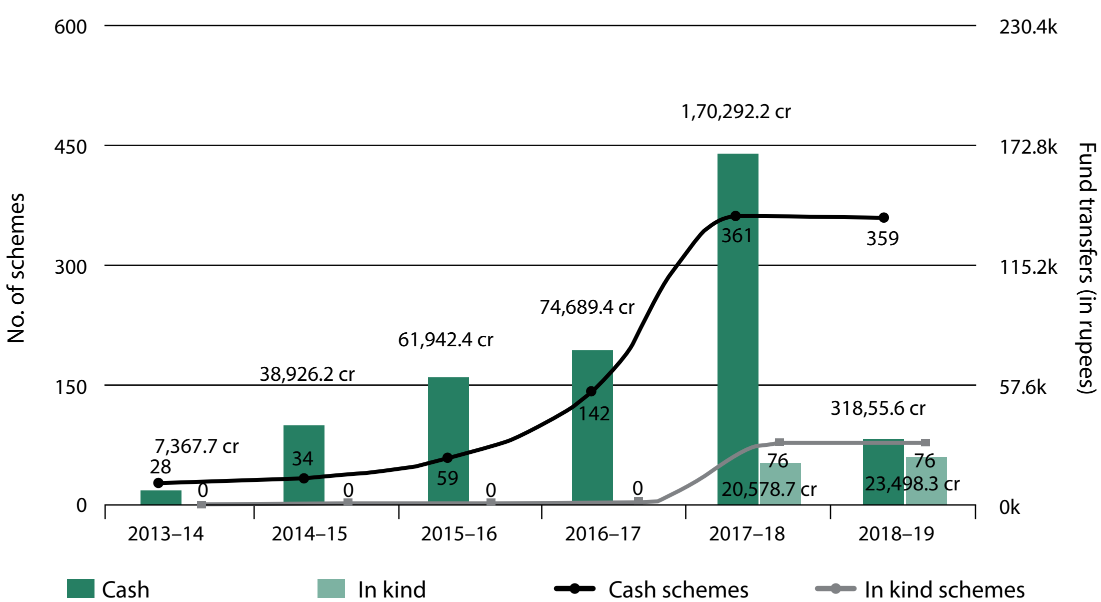


Figure 8.8: Year-wise Fund Transfer under the DBT

Source: https://dbtbharat.gov.in. Accessed on 4 September 2018.

territories of Chandigarh (CDG), Puducherry (PDY), and Dadra and Nagar Haveli (DNH).[21] Though the study is one-year-old and covered the economically well-off parts of India, it provided interesting insights. On the negative side, it found that while government records indicate a money transfer failure rate of less than 1 per cent, around 20 per cent of beneficiaries reported not receiving benefits even till March 2017. The report offered possible reasons for non-receipts, like lack of awareness or knowledge of transfers, payments being made into bank accounts beneficiaries do not access, or processing errors. On the positive side, 95 per cent beneficiaries preferred cash transfers, as those allowed them to diversify their dietary intake since supplies in kind through the PDS were limited to select staples. As cash transfers allowed beneficiaries to buy the foodgrains they wanted, it was reported that the purchase of higher quality grains at a higher price made them feel that the subsidy amount was not sufficient. While the choice upgrade is a behavioural thing and not a reflection on the DBT, the fact that 20 per cent reported not having received the cash transfers is a serious issue. The absence of a dedicated grievance redressal system was also a major reason for dissatisfaction. Based on the findings, the study recommended that:

> The next phase of DBT-based reforms in the PDS should consider an intermediary approach: providing beneficiaries the choice between social assistance in cash and kind, before taking away in-kind entitlements completely. This will ensure that we de-risk beneficiaries, particularly the most vulnerable, from the challenges of the sort seen in the UT pilots.<blockquote ends>

The present approach of the government in food subsidy does follow the intermediary approach.

MicroSave study of DBT-fertiliser

MicroSave conducted three rounds of evaluation of DBT-F, with the last round in July to September 2017. The findings were published in July 2018.[22] Fertiliser subsidy is one of the main components of the government's subsidy budget, albeit a contentious one. The Union Budget of 2016–17 stated the intent to bring fertiliser subsidy under the DBT system. DBT-F is a modified subsidy payment system under which the government remits the subsidy to fertiliser companies only after fertiliser retailers have sold fertiliser to farmers through successful Aadhaar-based authentication. The pilot was launched in 14 districts and currently a pan-India rollout is underway. MicroSave's study in the third round covered all 14 pilot districts, reaching 5,659 farmers and 427 retailers. The subsidy process in DBT-F is shown in Figure 8.9.

The findings were mixed, like the one for the PDS done by J-PAL. While they covered a host of issues ranging from policy to operational, the discussion here is being limited to the core of the digital debate, which is Aadhaar-based authentication and its

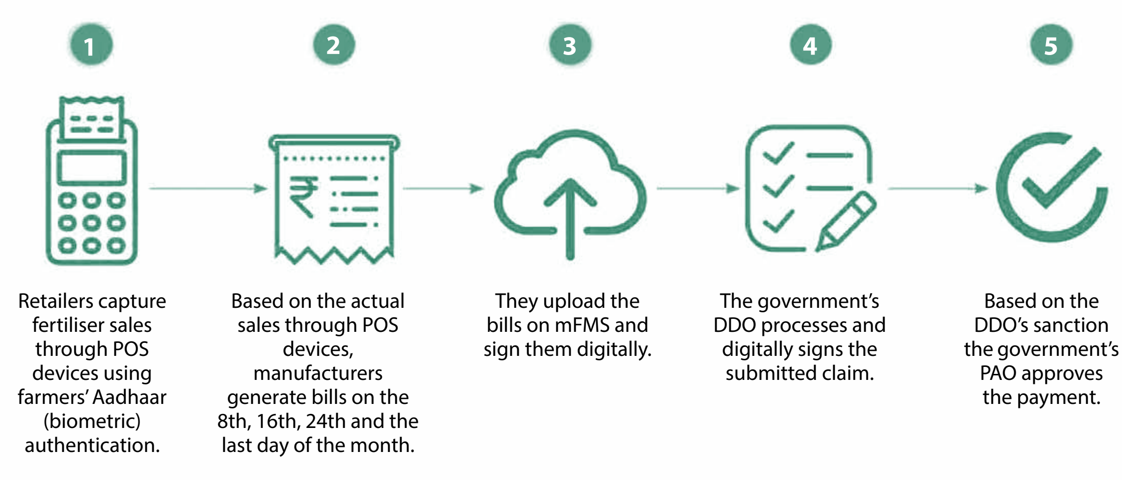


Figure 8.9: Process Flow of DBT in Fertiliser

Source: Niti Aayog and MicroSave, 'Assessment of Direct Benefit Transfer in Fertiliser: Pilot Sudy', April 2018. http://www.microsave.net/files/pdf/Assessment_of_Direct_Benefit_Transfer_in_Fertiliser.pdf. Accessed on 9 November 2018.

impact on end customers or farmers. The report observed that adjustment transactions (defined as using someone else's Aadhaar for authentication) increased to 21 per cent as compared to 10 per cent, observed in the second round. These types of transactions happened because of the unavailability of Aadhaar with farmers at the time of fertiliser purchase, as also Aadhaar authentication failure. It is to be noted that there was no restriction on the quantity of fertiliser that could be availed of by one farmer, nor any mechanism to verify the purchaser was indeed a farmer. The average time taken for a POS transaction was five minutes, and in 62 per cent cases farmers were able to authenticate on the first attempt. On repeated attempts, authentication success rate went up to 97 per cent. Noticeably, only 54 per cent of the retailers and 59 per cent of the farmers preferred the DBT-F over the manual system of fertiliser distribution. Lack of a grievance redressal system remained a concern, like in the case of the PDS. An informal redressal mechanism in the form of a WhatsApp group led to low satisfaction, and a toll-free number launched recently did not have vernacular capacity, thus limiting its effectiveness. Awareness that Aadhaar is mandatory in availing benefits under the scheme was found to be low, with only 66 per cent farmers reporting knowledge about it. Low awareness, POS failure, absence of a robust grievance redressal mechanism and adjusted transactions remained issues to be addressed. It is a matter of concern that in some cases where farmers did not have Aadhaar with them at the time of transaction, retailers used the Aadhaar of someone else to carry out the transaction, while in a few cases fertiliser was denied to the farmer.

Internet connectivity remains a challenge, with only 57 per cent retailers being happy with connectivity, and 43 per cent reporting poor connectivity, which also led to authentication failure. The study also examined the preference for cash transfers in bank accounts in place of fertiliser distribution. Nearly 75 per cent farmers indicated that they would not prefer cash transfers, as it would be difficult for them to arrange for the lump sum in advance before receiving a money transfer from the government. The study report also listed several operational issues at the level of retailers, like POS receipts not being inclusive of GST, and needing to be done manually, as well as low margins.

Center for Global Development study of Rajasthan's Bhamashah programme[23]

The DBT is part of a larger paradigm of digital governance, and Rajasthan's Bhamashah programme is unique in being much wider than the DBT in its scope. Bhamashah is a nuclear-family-level identity system in Rajasthan, under which each family is registered with a unique family ID number, and the card issued for the family contains names of each family member along with their Aadhaar numbers. It was first conceptualised in the year 2008 and rolled out at scale from 2014 onwards.

With the passage of the Rajasthan Bhamshah Act, 2017, enrolment under the programme has become mandatory for availing benefits under nearly 150 schemes, funded wholly or partly by the Rajasthan government. The Bhamashah programme is built on the foundations of the JAM trinity, but also superimposes women's empowerment on it by mandating that women be the head of the household in the Bhamashah card.

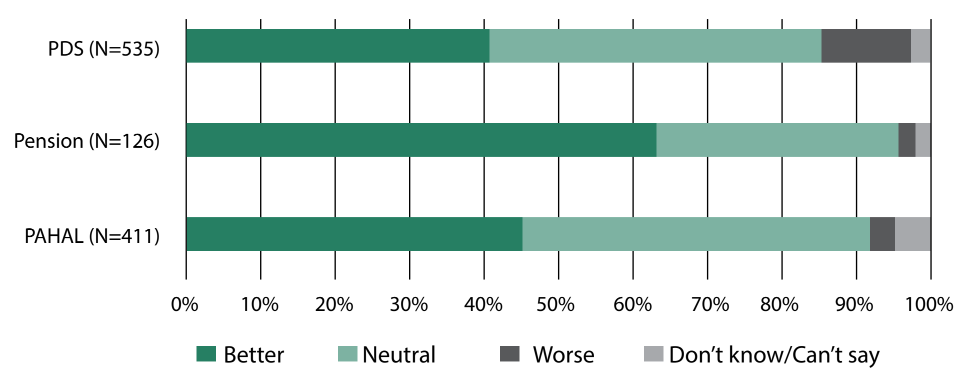


Figure 8.10: Beneficiary Perception of Technology-enabled Delivery of Services

Source: Gelb, Alan, Anit Mukherjee and Kyle Navis, 'Digital Governance in Developing Countries: Beneficiary Experience and Perceptions of System Reform in Rajasthan', working paper 489, Center for Global Development, Washington, D.C., 2018.

The study covered 633 families across all seven administrative divisions of Rajasthan. Perceptions about the new technology-based Bhamashah programme across three schemes were mixed (Figure 8.10).

The study found that dissatisfaction grew with the number of attempts required to authenticate transactions, that the ownership of phone and familiarity with its use was positively correlated with satisfaction, that OTP-based authentication was found to be cumbersome, and BPL customers rated higher satisfaction than APL customers. On the positive side, the study found impact on leakages as well as on financial inclusion. The report stated,

> Our data indicates that nearly 66 percent of women heads of household opened bank accounts at the time of Bhamashah registration. This indicates a huge push towards financial inclusion, through the design of the program. Almost 90 percent of these accounts have also been linked to Aadhaar. Moreover, most of the women who opened bank accounts are in the bottom three income categories of the survey, indicating that the process of financial inclusion was highly equitable, and covered those women who would have otherwise probably been left out of the formal banking system.

All three studies reported mixed results and it is expected to be so, as digital change is new, and at this scale, a few hiccups are anticipated. Improvements in technology infrastructure, grievance redressal and digital literacy appear as three major areas of future work. In this scenario, is mandatory insistence on digital delivery of services likely to lead to exclusions? There have been arguments on both sides, with a vocal point emerging that unless the system is robust, we should not go for mandatory digital delivery. Jean Drèze et al., in their study of the Aadhaar-based PDS system in Jharkhand, found positive features, but also observed this:

> The imposition of ABBA on the PDS in Jharkhand seems to be a case of 'pain without gain.' On the one hand, the system has led to serious exclusion problems (particularly for vulnerable groups, such as widows, the elderly, and manual workers), as well as higher transaction costs. On the other, it has failed to reduce quantity fraud, which is the main form of PDS corruption in Jharkhand. Nor has it helped to address other critical shortcomings of the PDS in Jharkhand, such as the problem of missing names in ration cards, the identification of Antyodaya households, or the arbitrary power of private dealers.[24]

The insistence on Aadhaar linkage to ration cards and the consequent denial of rations to many households was in the news, and some reports also blamed starvation deaths on this. In this scenario, and also taking into account the findings across the three studies, it seems prudent to make the DBT policy flexible, work on the gaps and not set unrealistic goals in terms of digital delivery of services.

The last section of this chapter further discusses the impediments to Digital India which need to be addressed and underlies the importance of tempered aspirations.

PROGRESS IN DIGITAL FINANCIAL SERVICES OUTREACH

InterMedia Survey: Bank Account or Mobile Phone Ownership Is Not Equal to Digital Inclusion

InterMedia, under its financial inclusion initiative (www.finclusion.org), brings out annual findings of its surveys on financial inclusion in eight countries, India being one of them. Its current report on India, released in June 2018, provided useful insights on digital financial inclusion, customer readiness, perceptions on digital finance and awareness of digital features.[25] As all banks in India offer digital services to account holders, the report suggested that 78 per cent of the Indian adult population was digitally included and an additional 2 per cent of the population had mobile money accounts. It is not clear how this conclusion had been arrived at where services offered are being equated with digital inclusion. At best it can be concluded to be the potential market.

The InterMedia report placed emphasis on mobile phones as the core of digital financial services, while there can be other modes, like cards, POS and computer-based transactions. Before going into the mobile phone-based findings, it needs to be mentioned that the digital discourse at present sometimes takes a unidimensional view. Some argue that mobile phone-based transactions are the future, while some say cards are easier to use and the preferable mode of digital inclusion. Policy has to avoid both extremes leaving the choice up to the customer, and luckily Indian policy in recent years has exhibited this blend. Issuance of RuPay cards

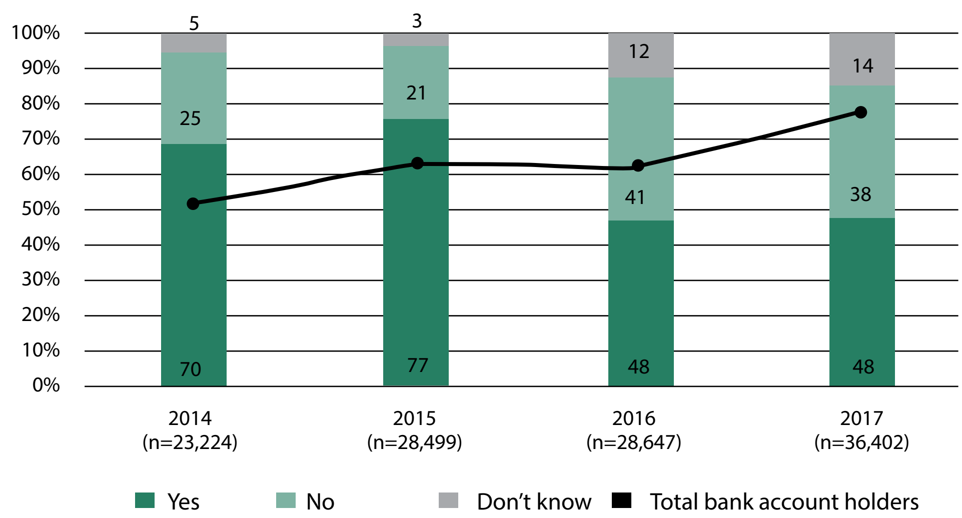


Figure 8.11: Bank Account Holders Reporting Any Digital Feature by Year

Source: InterMedia, 'India Financial Inclusion Insights Survey: Wave Five Technical Report', 2017. http://www.finclusion.org/uploads/file/reports/india_wave_5_technical_report(1).pdf. Accessed on 9 November 2018.

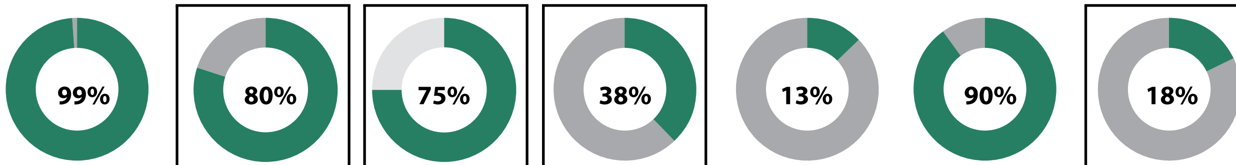
along with PMJDY accounts and phone-based payment in the form of the UPI are examples.

Coming back to InterMedia's survey findings, they indicated that 60 per cent adults in India owned phones, but 38 per cent owned a basic phone, 14 per cent owned a feature phone and only 15 per cent owned a smartphone. Considering the fact that quite a few digital transactions can be done on feature phones also, the total adult population ready for mobile phone-based transactions comes to 29 per cent. A majority of phone owners (basic phones) have to rely on the *99# service, which has not taken off, as discussed earlier. As mere ownership of a phone and a bank account does not translate into digital inclusion, the survey looked into factors like what percentage of bank account holders were aware of the digital features associated with the bank account such as fund transfer, card-based transactions, mobile phone app of the bank as well as website-based transactions. The findings were revealing (Figure 8.11). It was seen that while account ownership had gone up, it had also resulted in lower awareness about digital features. In 2015, 77 per cent of account holders reported being aware of digital features, which came down to 48 per cent in 2017. The inclusion of marginalised and excluded sections of society under PMJDY's drive seems to be the reason, which points to the requirement of work in digital literacy to move from access to usage. The associated findings of linking individual profile to awareness substantiated it. Lack of awareness is strongly associated with being rural, female, more than 35 years old and BPL category.

The survey looked into what functions of a phone had been used by the owner. While 77 per cent used mobile phones to make calls and 30 per cent received or sent text messages, only 9 per cent did any financial transactions. Thus, even though nearly half of the mobile phone users were aware of the digital financial features, it did not translate into the adoption of phones for doing financial transactions. The demonetisation exercise of 2016 is reported to have influenced 5 per cent mobile phone owners to adopt digital transactions, but half of them were either unwilling to continue or were not sure of continuing.

> Only 9 per cent mobile phone owners reported using it for making financial transactions

The survey report also examined the readiness of the adult population to adopt mobile phone-based digital finance on seven parameters: ID, phone ownership, SIM ownership, ability to send and receive messages, financial literacy, basic numeracy and mobile money awareness (Figure 8.12).



	Necessary ID	Mobile phone access (own/ borrow)	Own a SIM card	Ability to send and recieve text messages	Financia literacy	Basic numeracy	Mobile money awareness
2016	98%	68%	40%	26%	17%	97%	8%
2015	98%	90%	41%	38%	NA	95%	10%
2014	98%	86%	41%	40%	NA	87%	13%

Figure 8.12: 2017 – Key Indicators of Readiness to Adopt Digital Financial Services

Source: InterMedia, 'India Financial Inclusion Insights Survey: Wave Five Technical Report', 2017. http://www.finclusion.org/uploads/file/reports/india_wave_5_technical_report(1).pdf. Accessed on 9 November 2018.

While the Aadhaar ID has become universal, the report did not provide answers to the dip in phone ownership (own/borrowed) in 2016 and 2017 as compared to 2015. Financial literacy also dipped to 13 per cent from 17 per cent in 2016, and mobile money awareness remained low at 18 per cent despite having gone up from the previous year. These findings clearly showed that mobile phone-based digital finance, at present, needs to cross many hurdles before becoming a popular channel.

THE FINTECH STORY: CENTRED AROUND AFFLUENT AND TECH-SAVVY ELITE

Whenever digital finance is talked about, the mention of fintech as a practical application to provide financial services follows. The literature on the subject talks about its disruptive potential, and the potential to make financial services scalable, cost-efficient and speedier, riding on the rich digital data.[26] Newspapers carry daily reports about new investments in fintech, and based on the personal experience of the author, it will not be an exaggeration to say that without the use of fintech as a value proposition it is difficult to attract investments. From this report's perspective, the question to be examined is: Are fintechs enabling institutions to reach the unserved? In a country where the excluded segment of the population exhibits characteristics such as not having a digital footprint, unreliable access to the internet, phone ownership limited to basic or feature phones, the fintech promise has always seemed divorced from ground realities of the financial inclusion challenge.

The question has been dealt with in a recent study by MicroSave and IIM Ahmedabad for J.P. Morgan,[27] which precisely answered this question by looking at the fintech landscape in India and the market it is catering to. The report indicated that the fintech ecosystem in India has around more than 1,500 fintech companies, of which nearly 600 entrants started in 2017. Most (95 per cent) fintechs in financial services are in partnership with established players—termed incumbents in the report—like banks, which shows that the established players see the potential and are increasingly forging alliances with fintechs. A lot of money is flowing into fintech, with the study reporting deals worth \$2,173 million in 2017. Around 75 per cent of investments are in the top 10 companies.

Fintechs are offering varied financial services, but credit and payment services dominate, accounting for 32 per cent and 25 per cent share, respectively. Savings and insurance account for 20 per cent and 7 per cent share, respectively. However, despite the largest share, credit fintechs have been placed at a growing stage in terms of maturity, while payments fintechs have now matured, probably thanks to India's leapfrogging with the UPI. The maturity pattern of various types of fintech companies also reveals that artificial intelligence and blockchain technology is still in its infancy in India (Figure 8.13). Although the report did not include alternate data scoring-based models, like social profile and psychometric scoring, these are also at an emerging stage in India.

From an inclusion perspective, the findings were not encouraging. Geographically, 82 per cent of fintech companies are located in three metro cities and cater mainly to the affluent elite. The report, while estimating market segmentation, classified the population into five segments based on daily household income.[28] The report found that out of

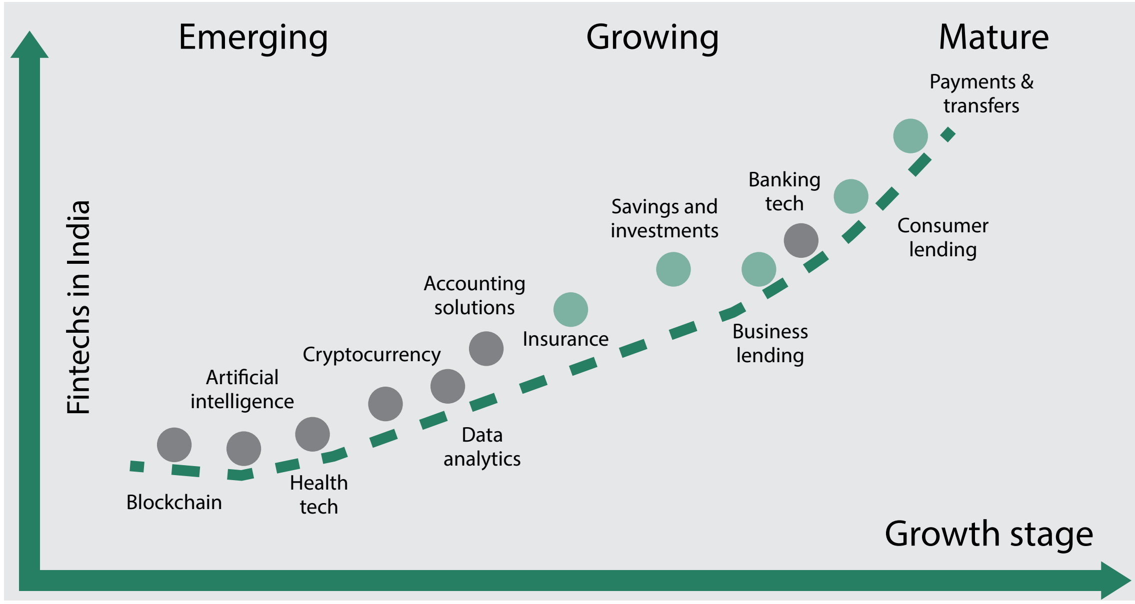


Figure 8.13: Growth Stages of Fintech in India

Source: MicroSave and IIM(A), 'Fintech Study to Model a Financial Inclusion Lab: Supporting Fintechs to Cater to the Low- and Middle-income Segments', August 2018.

the estimated 200 million outreach of fintech, 70 per cent was accounted for by outreach to the top two strata of the population classified as 'Elite' and 'Affluent'. The segment below these two top strata, termed as 'Aspirers' and 'Strugglers' and falling in the per day household income range of \$2 to \$10, is rightly defined as the addressable LMI market. The size of this LMI market is estimated at 380 million, which would also link up with the 'missing middle' discussed in the chapter on MSMEs.

The typical client profile of fintech companies, described in the report, also provides an insight that fintech has largely remained an urban elite phenomenon (Box 8.4). The characteristics are pointers to the negligible impact of fintech on reaching the excluded segments of society which belong to the low- and middle-income category. Much of fintech at present is geared towards e-commerce payment solutions, savings and investments options for the salaried, and credit to those who are already digital adapters. The report also offered reasons for concentration of fintech to the affluent digital savvy class. These range from technical aspects, such as mismatch between legacy technology of the incumbent and new technology of fintech, to operational aspects, like process inefficiencies and tweaking of ideas by banks, as well as a critical one like mindset constraints. Fixation with per unit economics (profit on each transaction—bite-sized transactions do not stand the test), long gestation period from start of operations to profitability, uncertainty about market readiness, high cost of acquiring small-value customers, and a limited digital footprint have been cited as reasons for confinement of fintech to urban affluent class.

Box 8.4: Key Characteristics of a Typical Fintech Client

Customer

- Millennials seeking financial independence
- Active users of smartphone
- Consume mobile internet for multiple purposes
- Value technology and convenience
- Mainly from salaried class

Micro-entrepreneur

- Accept digital payments; require affordable credit
- Use smartphones for communication and entertainment
- Want to explore value proposition of fintech

Source: MicroSave and IIM(A), 'Fintech Study to Model a Financial Inclusion Lab: Supporting Fintechs to Cater to the Low- and Middle-income Segments', August 2018.

CONCLUDING OBSERVATIONS: BARRIERS TO BE OVERCOME

From the chapter discussion, one pattern emerges clearly—despite the policy push and building of an ecosystem or digital rails, other than the DBT, much of the buzz around payments and fintech has remained confined to privileged citizens. And this is so when we are at first-generation issues of the digital journey, i.e., any transaction done digitally is a step forward. The real test of digital adoption will come when the cash in circulation reduces. This would entail a scenario wherein a borrower or saver would have no need, or a reduced one, to withdraw cash, but would like to spend the money digitally. The absence of such a scenario has resulted in a situation wherein despite digital progress, cash as percentage of the GDP is inching back towards pre-demonetisation levels.[29] As a note of caution, it needs to be stated that the author does not take any stand on the contentious issue of whether digital transactions are inherently superior or otherwise to cash transactions. This is an issue beyond the scope of the report, but the debate does highlight the fact that customer choice and preference has to be paramount, and ideally there should be no forced nudge. Along with this, there has to be an acknowledgement that behaviour change cannot happen overnight and will require prolonged efforts. The following points are those which need to be resolved by policymakers and practitioners for higher digital adoption.

Connectivity challenge

Connectivity is at the core of digital inclusion, as technology-based solutions, be it card or phone based, like the UPI or Bharat QR code, require reliable net connectivity. The studies cited in the chapter also show that problems related to connectivity lead to issues like delay and failure in authentication, which in turn lead to customer apathy or distrust towards digital development. The government has done significant work in the recent past through schemes like BharatNet and NOFN. BharatNet has been tasked to provide broadband connectivity to 2.5 lakh gram panchayats in the country using optical fibre. The entire project is funded by the USOF, levied on telecom operators, which was set up for improving telecom services in rural and remote areas of the country. As an enabler, BharatNet will make it possible to take internet and telecommunication services to every nook and corner of the country. It is the world's largest rural broadband connectivity project through the optical fibre network and is being implemented in partnership with the centre and states.

However, despite the progress, region-wise penetration of internet exhibits a lot of gaps (Figure 8.14). Overall internet connections have gone up by 71 million in the last year to reach 493 million, but the share of narrowband connections is still at 16.5 per cent. More challenging for the last-mile digital reach is the fact that the share of narrowband in rural connections is as high as 37 per cent. Regional concentration is also seen distinctly, with south India accounting for 26 per cent of internet connections. Further, the share of narrowband is higher than the national average in the east and northeast. Beyond this, there are various definitional and practical issues. TRAI defines any speed above 512 kbps as broadband,

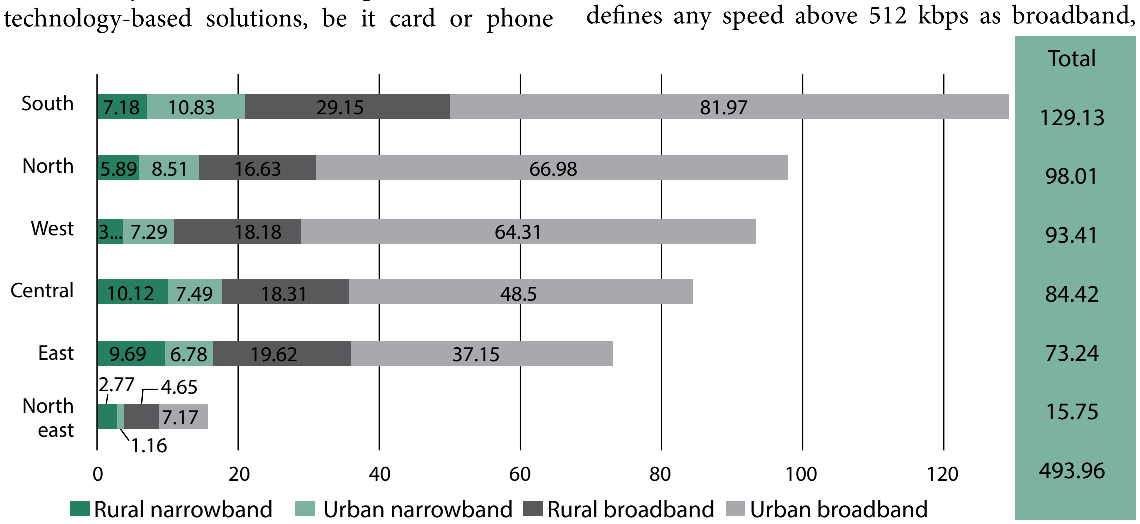


Figure 8.14: Region-wise Penetration of Internet Connections (in million)

Source: Telecom Regulatory Authority of India. https://www.trai.gov.in/sites/default/files/PIReport27062018_0.pdf . Accessed on 4 August 2018.

which is much lower compared to global standards. Further, it is not clear how much double counting there is in internet connections, as one person having a mobile phone with internet and a fixed-line connection will be counted as two connections, and there are many such cases in urban areas. Thus, if the benchmark is raised, the actual count of internet connections is lower and broadband coverage is also lower.

The connectivity challenge is further compounded by the fact that even broadband connections like 4G and 3G face problems of low speeds and disruptions. A 2018 report by the global internet testing firm Ookla said that India ranked 67th in fixed broadband speed and 109th in mobile internet speeds.[30] This was despite the fact that 4G services were being offered by most telecom operators in the country.

In such a scenario, it is logical that digital finance has been more concentrated in urban areas. Under the BharatNet project, optical fibre is to be laid till the gram panchayat, but the challenge will be to extend it to households through fixed-line connections or mobile towers, as the service providers will require volume for viability. A stable high-speed broadband connection at an affordable cost, considering the economic profile of the population, is a basic requirement for the Digital India vision. Considering the challenge and time required to address it, the policy needs to be tempered in pushing digital services.

Mobile phone ownership: Low smartphone ownership and the gender skew

Most new-generation financial apps are built for use on mobile phones, like the UPI and PPIs, and banks also offer phone-based apps. While connectivity is one challenge, ownership of a phone is another. Against this backdrop, overall phone ownership is limited to 60 per cent of the population, of which only around 20 per cent have smartphones on which these apps work. There are differing estimates of smartphone ownership. The InterMedia survey put it at 15 per cent, while a Pew Research Center survey put it at a little over 20 per cent (Figure 8.15). Even at the latter percentage, India lags behind countries like Kenya and Nigeria. Low smartphone ownership along with connectivity issues pose a double challenge for mobile phone-based digital financial services in rural areas. While services like *99# have been started for basic phones, the off-take has not been good (discussed earlier). Field visits of the author show that the small screen of basic phones makes it difficult to execute financial transactions, and often the small memory of these phones leads to non-receipt of messages—which further erodes confidence of low-income clients to undertake digital transactions. All these issues are reflected in the high share of the urban and tech savvy in digital transactions, as also the concentration of fintech companies in metro cities. As digital history is key to the operation of most fintech companies, their focus seems logical.

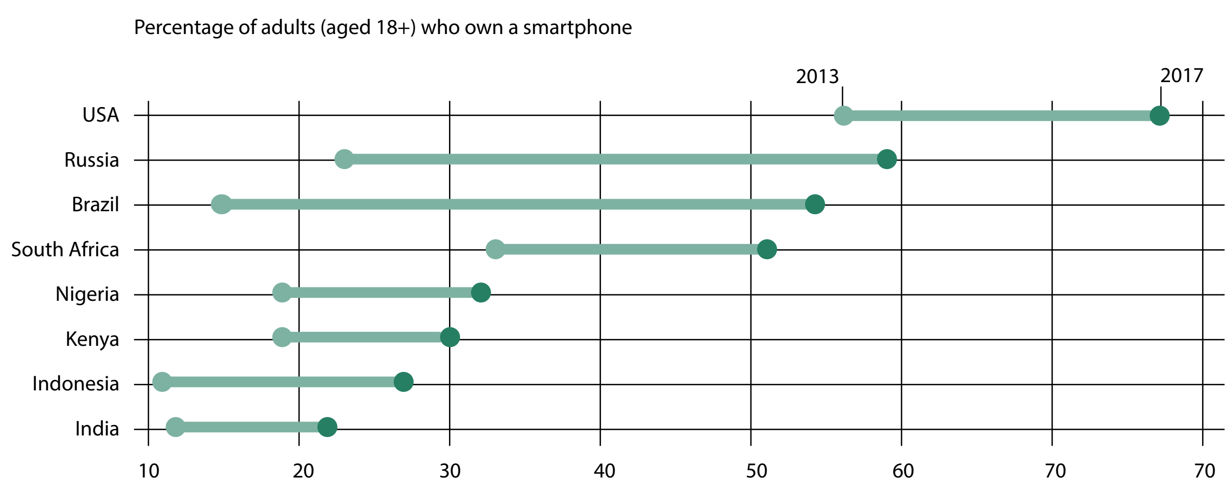


Figure 8.15: Smartphone Ownership across Countries

Source: Pew Global Attitudes Survey.

For the cause of financial inclusion, this has two important policy issues. First, considering the price sensitivity of a majority of rural people, is it realistic to assume that smartphone ownership will increase significantly in the coming years? If not, then maybe a better choice would be to focus on assisted modes of transaction, like through banking correspondents as well as focusing on increasing the card-acceptance infrastructure. It is also acknowledged that women from low-income segments in rural areas face issues related to social mobility as well as participation in financial decisions of the household. Mobile phone-based transactions have the potential to overcome these by allowing women to do transactions from home, but it seems a little distance away. Phone ownership is further skewed at the gender level. Last year's report by the Grameen Foundation1 found 2 per cent smartphone ownership among rural women as compared to 5 per cent for men. The figures for basic phones were 36 per cent and 86 per cent respectively. The Grameen study and a study by MicroSave on cashless payments among MFIs found a preference for phygital model or assisted model, wherein the customer goes to an access point and is helped to transact digitally, in a typical BC-model approach. Once the customer gets used to assisted digital transactions, it is easier to do transactions by themselves. Owning smartphones has a cost and many low-income clients have neither the resources nor the confidence to do self-transactions.

Difference between literacy and digital literacy

Adoption of digital channels is also dependent on the ability to make digital transactions with confidence, and is quite different from basic or financial literacy. This was corroborated by the author's interaction with low-income clients as well as the GF study. The study observed that a basic ground-level understanding of technical aspects can suffice, and it found a weak link between improvement in financial literacy and improvement in frequency of banking transactions. The InterMedia survey reported only 9 per cent of phone owners made a phone-based financial transaction, while 30 per cent could send or receive text messages. Recognising this, the government has launched an expansive digital literacy scheme, the PMGDISHA, one of the largest digital literacy programmes in the world, which aims to make six crore households in rural India 'digitally literate' by March 2019, with an expected budget of Rs 2,351 crore. The 20-hour programme content includes training to operate digital devices (tablet, smartphones and computers), browse the internet, use e-mail, access online citizen-centric services and carry out digital payments. While this is a welcome move, as it separates digital literacy from financial literacy—the common theme nowadays—the mechanisms to check delivery quality and level of competence after training has gaps, which the government is trying to address. The effort of the government needs to be supplemented by financial institutions, be they banks, NBFCs or MFIs. Moreover, in order to have a uniform perspective, the course design needs to be standardised; multiple contents have the potential to confuse the participant.

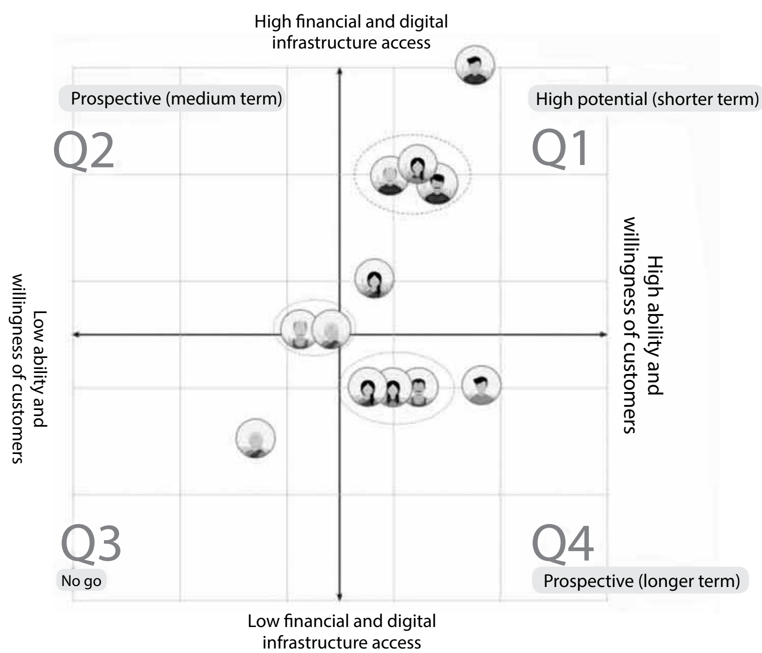


Figure 8.16: Potential Digital Customer Segmentation

Source: IFMR LEAD, *Digital Financial Inclusion and Consumer Capabilities in India* (Chennai: IFMR LEAD, 2017).

Further, the training content needs to be based on broad market segmentation, as the needs of someone with a basic phone and access to a physical touchpoint will be different from a feature phone owner at some distance from a physical touchpoint, or someone having an Android phone in a rural location. A study by IFMR LEAD suggested a useful framework of four quadrants as a possible segmentation approach.

This will require collective national effort. Countries have done it, though the scale in India is vastly different. The study of the Bhamashah programme by the Center for Governance and Development cited Estonia as an example of this.

PMGDISHA in India is also modelled on similar lines, but the scale will call for a much larger effort, and quality concerns need to be addressed.

Keeping it simple versus multiple options and other issues

> Multiple channels are fine but are low-income clients interoperable?

Multiple digital channels are good for tech-savvy persons but create confusion among others. At present, a person in a rural or urban area looking to do a digital financial transaction has so many options—for payments they can use the services of a BC based on Aadhaar authentication, go to a bank and fill the money transfer form, use PPI wallets if the receiver also has an account, do the transaction with their phone using UPI-based applications (they have to choose from numerous applications), use the services of Paytm or Airtel kiosks, or use the *99# channel. If money has to be withdrawn, they can use a debit card at an ATM or with a BC. Each service has its distinct interface and transaction protocol, even a UPI-based application of the Paytm bank has a different screen from others like the SBI Buddy. All this looks simple to a tech-savvy person, but for a person used to the assisted mode, the multiplicity breeds confusion. To this is the added fear of pressing the wrong key and losing money through the consequent mistake in transaction. Yet the ecosystem keeps adding new devices and modes, with a recent news item indicating that the SBI has launched a new device titled MOPAD, or Multi Option Payment Acceptance Device, which is a POS terminal and would, along with cards, accept payments through the UPI, Bharat QR and the SBI Buddy wallet, which till now required different tools to receive payments. Innovation and interoperability at the payment options level is good, but are customers able to be interoperable—operate across multiple channels with ease—or do these add to their diffidence at being able to navigate the digital world? The IFMR LEAD study found that:

> After extensive training on the BHIM app on how to create an account, send money, collect money and scan and pay, individuals were largely unable to navigate the PayTM application, due to a lack of understanding of smartphone features, and low willingness to experiment with different buttons in the application.

In dealing with low-income clients, policy needs to factor in this important aspect, and maybe focus on a phygital channel like the BC and centre the digital training around that.

During field visits, two additional issues were observed. The functioning of the JAM trinity is based on the linkage of Aadhaar with bank account and mobile phone. It was observed that with a change in service provider (which happened on a mass scale last year), phone numbers linked to Aadhaar changed for customers, and thus they no longer received messages confirming transaction. While updating of Aadhaar seeding is possible on the UIDAI website or at customer centres, nobody had bothered to do so. The second issue relates to the UPI. While most clients in rural areas now have RuPay debit cards courtesy the PMJDY, they hardly use it. As setting up a UPI account requires a debit card, many clients stop there. There are other operational issues with the digital push, which in case of microfinance clients have been discussed in the chapter on microfinance.

Finally, the emerging regulatory issues from the modularisation of financial services and the increase in retailing third-party products referred to in the overview chapter also need serious attention. Fintech allowing for multiple players in a financial product through its different stages, from design to retailing and servicing, not only leaves regulatory gaps, but also leaves the customer unsure of a contact point in the case of grievance. The trend of an IVRS-based grievance redressal channel is not suited to low-income clients, who prefer a physical or a dedicated personal touchpoint. The issue of data privacy, with a digital history-based scoring model, is also an issue, especially with middle-income clients. Fintech companies now provide credit based on clients' consent to access digital information in the form of e-mails and social media posts. While at the time of need people give their consent, they are not fully aware of the information that is being used and how it is used. The RBI's working group on fintech has made some useful suggestions but not much action has been seen post the report. It is hoped that the finalisation of the data protection law based on the Srikrishna committee report will effectively address data privacy issues.

The goal of Digital India is seeing frenetic action, but for it to effectively include low-income clients will take time, and in the meantime, we should not nudge them into unfamiliar territory without addressing their concerns. The digital mode should be seen as an enabler, wherever possible, not as the endgame.

ANNEXURE 8.1:
Systemically Important Financial Market Infrastructure

Systemically Important Financial Market Infrastructure Financial Market Infrastructure (FMI) is defined as a multilateral system among participating institutions, including the operator of the system, used for the purposes of clearing, settling, or recording payments, securities, derivatives, or other financial transactions. Under this segment there are four instruments of payments. They are briefly discussed below:

RTGS:

Real Time Gross Settlement is defined as the continuous (real-time) settlement of funds transfers individually on an order by order basis (without netting). 'Real Time' means the processing of instructions at the time they are received rather than at some later time; 'Gross Settlement' means the settlement of funds transfer instructions occurs individually (on an instruction by instruction basis). This system is primarily meant for large value transactions. The minimum amount to be remitted through RTGS is ` 2 lakh. For inter-bank fund transfer there is no floor.

CBLO:

CBLO refers to a money market instrument called Collateralized Borrowing and Lending Obligation (CBLO). Clearing Corporation of India Ltd. (CCIL) has developed and introduced this instrument with effect from January 20, 2003 This represents an obligation between a borrower and a lender as to the terms and conditions of a loan. CBLO facilitates unwinding of both borrowing and/or lending positions before maturity and substitution of security given as collateral for borrowing. It also does not entail physical transfer of respective securities from borrower to lender or vice versa being a blend of hold-in-custody and tri-partite repo.

Government Securities:

A Government Security (G-Sec) is a tradeable instrument issued by the Central Government or the State Governments. It acknowledges the Government's debt obligation. Such securities are short term (usually called treasury bills, with original maturities of less than one year) or long term (usually called Government bonds or dated securities with original maturity of one year or more). In India, the Central Government issues both, treasury bills and bonds or dated securities while the State Governments issue only bonds or dated securities, which are called the State Development Loans (SDLs). G-Secs carry practically no risk of default and, hence, are called risk-free gilt-edged instruments.

Forex Clearing1:

The term 'Forex' stands for Foreign Exchange. In simple terms it is the trading in currencies from different countries against each other. In India the settlement of Forex transactions is done by CCIL which was started in November 8, 2002. This segment accepts the inter-bank Cash, Tom, Spot and Forward USD-INR transactions for settlement by providing netting benefits of well over 95%. CCIL has since moved to a settlement on a Payment V/S Payment basis from April 2015.

Retail Payments

Under the Retail Payments segment which has a large user base, there are three broad categories of instruments. They are Paper Clearing, Retail Electronic Clearing and Card Payments. The instruments under these three categories are discussed below:

Cheque Truncation System (CTS):

CTS or online image-based cheque clearing system is a cheque clearing system undertaken by the Reserve Bank of India (RBI) for faster clearing of cheques. As the name suggests, truncation is the process of stopping the flow of the physical cheque in its way of clearing. In its place an electronic image of the cheque is transmitted with key important data. Cheque truncation thus obviates the need to move physical instruments across branches and effectively eliminates the associated cost of movement of physical cheques, reduces the time required for their collection and brings elegance to the entire activity of cheque processing.

Non-MICR:

The Non-MICR clearing refers to the process of manual clearing of cheques where the cheque is physically moved between the bank branches/banks for clearing. Unlike MICR clearing where the MICR code on the cheques is scanned and the transaction is made, in MICR clearing the cheque is physically circulated for clearing.

ECS DR/CR:

ECS is an electronic mode of payment / receipt for transactions that are repetitive and periodic in nature. ECS is used by institutions for making bulk payment or for bulk collection of amounts. Essentially, ECS facilitates bulk transfer of monies from one bank account to many bank accounts or vice versa. ECS includes transactions processed under National Automated Clearing House (NACH) operated by National Payments Corporation of India (NPCI).

NEFT:

National Electronic Funds Transfer (NEFT) is a nation-wide payment system facilitating one-to-one funds transfer. Under this scheme, individuals, firms and corporates can electronically transfer funds from any bank branch to any individual, firm or corporate having an account with any other bank branch in the country participating in the scheme. It is offered by the Reserve Bank of India (RBI).

IMPS:

Immediate Payment Service (IMPS) offers an instant 24X7 interbank electronic fund transfer service through mobile phones. IMPS is an emphatic tool to transfer money instantly within banks across India through mobile, internet and ATM. It is offered by National Payments Corporation of India (NPCI), India's sole retail payment organization.

UPI:

Unified Payments Interface (UPI) is a system that powers multiple bank accounts into a single mobile application (of any participating bank), merging several banking features, seamless fund routing & merchant payments into one hood. It also caters to the "Peer to Peer" collect request which can be scheduled and paid as per requirement and convenience.

*99#:

USSD based mobile banking service of NPCI was initially launched in November 2012. The service had limited reach and only two TSPs were offering this service i.e. MTNL & BSNL. Understanding the importance of mobile banking in financial inclusion in general and of *99# in particular, various regulatory/trade bodies came together to ensure on boarding of all TSPs on *99# (USSD 1.0). With the wider ecosystem (11 TSPs), *99# was dedicated to the nation by Hon'ble Prime minister on 28th August 2014, as part of Pradhan Manti Jan Dhan Yojna.

NACH:

"National Automated Clearing House (NACH)" is a service offered by NPCI to banks which aims at facilitating interbank high volume, low value debit/credit transactions, which are repetitive and electronic in nature. The system leverages the Core-Banking Solution (CBS) of participating banks for centralized posting of inward debit / credit transactions and is run by NPCI.

Credit Card:

A credit card is a card issued by a financial company which enables the cardholder to borrow funds. The funds may be used as payment for goods and services, with a condition that the cardholder will pay back the original, borrowed amount plus any additional agreed-upon charges. The issuer pre-sets borrowing limits which have a basis on the individual's credit rating. These cards can be used domestically and internationally and can also be used to withdraw cash from an ATM and for transferring funds to bank accounts, debit cards and prepaid cards within the country.

Debit Cards:

A debit card is a payment card that deducts money directly from a consumer's bank account to pay for a purchase and eliminate the need to carry cash or physical checks to make purchases. In addition, they offer the convenience of credit cards and many of the same consumer protections when issued by major payment processors like Rupay, Visa or MasterCard, but unlike credit cards, they do not allow the user to go into debt, except perhaps for small negative balances that might be incurred if the account holder has signed up for overdraft coverage. However, debit cards usually have daily purchase limits, meaning it may not be possible to make an especially large purchase with a debit card.

Pre-Paid Instruments:

Prepaid Payment Instruments (PPIs): PPIs are payment instruments that facilitate purchase of goods and services, including financial services, remittance facilities, etc., against the value stored on such instruments. PPIs that can be issued in the country are classified under three types viz. (i) Closed System PPIs, (ii) Semi-closed System PPIs, and (iii) Open System PPIs.

Closed System PPIs: These PPIs are issued by an entity for facilitating the purchase of goods and services from that entity only and do not permit cash withdrawal. As these instruments cannot be used for payments or settlement for third party services, the issuance and operation of such instruments is not classified as payment systems requiring approval / authorization by the RBI.

Semi-closed System PPIs: These PPIs are used for purchase of goods and services, including financial services, remittance facilities, etc., at a group of clearly identified merchant locations / establishments which have a specific contract with the issuer (or contract through a payment aggregator / payment gateway) to accept the PPIs as payment instruments. These instruments do not permit cash withdrawal, irrespective of whether they are issued by banks or non-banks.

Open System PPIs: These PPIs are issued only by banks and are used at any merchant for purchase of goods and services, including financial services, remittance facilities, etc. Banks issuing such PPIs shall also facilitate cash withdrawal at ATMs / Point of Sale (PoS) / Business Correspondents (BCs).

Relative Contribution of Different Segments of Digital Payments:

The charts below indicate the relative contribution of the 2 segments of Digital Payments for the year 2017-18. As per this it is clear that in terms of volume, SIFMI has a very low share in the overall Digital Payments transactions whereas in terms of value it has a significant share i.e. 89%.

Source: Digital Payments-Tends, Issues and Opportunities, NITI Aayog July 2018

[1]https://www.ccilindia.com/ForexSettlement/Pages/Introduction.aspx

ANNEXURE 8.2:
Snapshot of Digital Transactions

Source	RBI	RBI	RBI	RBI	RBI	RBI	RBI	RBI	RBI	RBI	NPCI	NPCI	NPCI	NPCI	RBI	RBI	RBI	RBI	RBI	RBI
	RTGS transaction volume (in million)	RTGS value (in Rs billion)	ECS transaction volume (in million)	ECS DR value (in Rs billion)	EFT/NEFT transaction volume (in million)	EFT/NEFT value (in Rs billion)	IMPS transaction volume (in million)	IMPS value (in Rs billion)	NACH transaction volume (in million)	NACH value (in Rs billion)	USSD *99# transaction volume (actual)	USSD *99# transaction value (in Rs million)	UPI transaction volume (in million)	UPI transaction value (in Rs billion)	Credit cards transaction volume (in million)	Credit cards value (in Rs billion)	Debit cards transaction volume (in million)	Debit cards value (in Rs billion)	PPIs transaction volume (in million)	PPIs value (in Rs billion)
Aug-16	8.56	77,588.32	1.78	12.14	118.55	8,764.13	33.89	268.49	153.33	681.78			0.093	0.031	84.59	260.50	887.22	2,380.13	96.28	56.46
Sep-16	8.46	86,687.35	1.67	10.36	120.15	9,880.29	35.93	289.12	157.29	590.36			0.085	0.326	78.53	244.83	867.33	2,379.08	97.07	56.28
Oct-16	9.00	76,473.30	1.77	18.46	133.21	9,504.50	42.09	343.57	169.39	768.44			0.103	0.486	89.49	302.42	942.65	2,767.23	126.90	60.22
Nov-16	7.88	78,479.19	1.01	8.94	123.05	8,807.88	36.17	324.81	152.51	606.62			0.285	1.005	98.00	264.32	808.78	1,569.14	169.03	50.10
Dec-16	8.84	84,096.47	1.16	14.39	166.31	11,537.63	52.78	431.92	198.72	626.76	25,212	17.62	1.967	7.062	116.46	312.37	1,045.93	1,429.65	261.09	97.70
Jan-17	9.33	77,486.07	0.96	11.94	164.19	11,355.08	62.42	491.25	158.74	541.36	3,08,383	373.67	4.153	16.588	113.24	328.62	1,040.97	2,006.48	295.45	108.69
Feb-17	9.11	74,218.81	0.87	9.35	148.21	10,877.91	59.75	482.21	150.45	592.03	2,22,159	355.25	4.156	19.021	95.35	288.95	944.32	2,286.82	280.02	96.28
Mar-17	12.53	1,23,375.83	1.15	11.24	186.70	16,294.50	67.41	564.68	182.12	829.37	2,08,141	336.04	6.161	23.914	106.70	331.11	981.28	2,616.45	342.09	106.77
Apr-17	9.54	88,512.19	0.68	10.89	143.17	12,156.17	65.08	562.06	222.17	971.50	1,87,146	303.16	7.005	22.408	107.06	333.76	928.32	2,543.41	352.23	103.71
May-17	10.44	90,170.52	0.79	11.42	155.82	12,410.81	66.72	585.59	204.03	760.58	1,90,500	315.28	9.168	27.654	115.88	364.02	922.99	2,539.00	278.08	106.69
Jun-17	9.83	92,812.58	0.77	11.38	152.34	12,694.20	65.84	596.55	207.79	811.05	1,98,815	312.98	10.155	30.671	110.03	357.50	922.47	2,632.17	255.65	85.07
Jul-17	9.38	87,149.26	0.57	11.83	148.14	12,011.60	69.07	604.76	214.42	843.47	1,90,584	301.89	11.444	33.812	111.38	342.15	957.69	2,614.11	270.24	98.56
Aug-17	9.46	89,163.39	0.75	11.79	151.61	12,500.38	75.66	651.49	214.77	824.43	1,91,812	294.25	16.608	41.272	115.99	366.03	983.86	2,707.08	261.14	102.88
Sep-17	9.61	1,02,348.13	0.62	10.44	157.67	14,182.14	82.85	717.60	186.58	714.06	2,02,700	323.61	30.778	52.934	113.29	377.76	983.16	2,785.83	240.29	109.77
Oct-17	10.00	92,056.10	0.62	11.55	158.78	13,851.28	88.12	750.42	197.09	985.45	1,84,557	299.07	76.772	70.578	124.04	422.60	1,020.27	2,941.90	245.18	116.98

Source	RBI	RBI	RBI	RBI	RBI	RBI	RBI	RBI	RBI	RBI	NPCI	NPCI	NPCI	NPCI	RBI	RBI	RBI	RBI	RBI	RBI
	RTGS transaction volume (in million)	RTGS value (in Rs billion)	ECS transaction volume (in million)	ECS DR value (in Rs billion)	EFT/NEFT transaction volume (in million)	EFT/NEFT value (in Rs billion)	IMPS transaction volume (in million)	IMPS value (in Rs billion)	NACH transaction volume (in million)	NACH value (in Rs billion)	USSD *99# transaction volume (actual)	USSD *99# transaction value (in Rs million)	UPI transaction volume (in million)	UPI transaction value (in Rs billion)	Credit cards transaction volume (in million)	Credit cards value (in Rs billion)	Debit cards transaction volume (in million)	Debit cards value (in Rs billion)	PPIs transaction volume (in million)	PPIs value (in Rs billion)
Nov-17	10.83	98,410.49	0.67	11.21	161.97	13,884.00	89.49	782.58	207.97	943.02	1,82,523	287.4	104.841	96.406	116.41	395.85	1,002.30	2,857.91	236.16	133.21
Dec-17	10.89	1,00,907.79	0.64	8.08	169.05	15,779.20	98.01	871.06	202.26	806.34	1,79,852	299.4	145.563	131.443	124.48	421.98	1,054.32	3,047.99	319.85	143.34
Jan-18	11.16	1,07,488.40	0.62	9.47	170.21	15,374.07	99.56	882.14	218.96	820.57	1,72,811	290	151.833	155.712	130.73	417.78	1,040.12	2,957.83	361.20	147.71
Feb-18	10.63	91,765.63	0.58	8.50	165.59	14,843.90	99.25	882.70	210.10	941.95	1,56,073	259.3	171.4	191.262	115.44	379.81	1,000.28	2,845.24	345.37	149.59
Mar-18	12.68	1,26,340.30	0.37	7.96	212.01	22,540.77	110.15	1,038.04	217.31	1,313.70			178.05	241.726	128.08	446.77	1,093.84	3,082.07	293.66	118.82
Apr-18	10.66	94,045.75	0.70	12.58	167.35	16,326.64	109.55	1,022.40	263.52	1,227.04			190.08	270.2185	133.05	451.74	1,092.70	3,102.54	326.17	133.80
May-18	11.49	1,05,720.93	0.58	10.56	172.91	17,151.96	116.62	1,085.75	237.09	966.41			189.48	332.8851	138.41	474.01	1,100.17	3,115.59	350.74	155.21
Jun-18													246.37	408.3403						

Source: 1. 'Payment System Indicators, RBI Bulletin. https://www.rbi.org.in/Scripts/BS_ViewBulletin.aspx?Id=16609. Accessed on 5 August 2018.
2. 'UPI Product Statistics'. https://www.npci.org.in/product-statistics/upi-product-statistics. Accessed on xxxx.
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Notes: Data for latest 12-month period is provisional.
1.3: Pertain to multiateral net settlement batches.
3.1: Pertain to three centres: Mumbai, New Delhi and Chennai.
3.3: Pertain to clearing houses managed by 21 banks.
6: Available from December 2010.
7: Include IMPS transactions.
9: Includes ATMs deployed by scheduled commercial banks and White Label ATMs (WLA). WLA are included from April 2014 onwards.
12: NITI—Digital payment book add UPI payments in addition to other in retail electronic payment and it is not added in RBI bulletins.
PRESS! Convert all months to this format: Mar '17

ANNEXURE 8.3: Estimated Benefits/Gains from DBT & Other Government Reforms (up to March 2018)

DBT and other governance reforms have led to the removal of duplicate/fake beneficiaries and plugging of leakeges etc., as a result of which the government has been able to target genuine and deserving beneficiaries. Estimated savings/benefits from some of the schemes are as under:

	Ministry/Department	Scheme	Estimated Savings/Benefits(in Rs crore)			
			Cumulative up to March 2017	Total during 2017–18	Cumulative up to March 2018	Remarks
1	Petroleum and natural gas	PAHAL	26,769	12,506	42,275	3.79 crore duplicate, fake/non-existent, inactive LPG connections eliminated. In addition, 2.22 crore consumers stopped claiming subsidy (including 1.04 crore 'Give it Up' Consumers)
2	Food and public distribution	PDS	14,000	15,708	29,708	Deletion of 2.75 crore duplicate and fake/non-existent ration cards (including some due to migration,death, etc.)
3	Rural development	MGNREGS	11,741	4,332	16,073	Based on field studies, the ministry has estimated 10 per cent savings on wages on account of deletion of duplicate, fake/non-existent, ineligible beneficiaries
4		NSAP	399	39.6	438.6	Deletion of 2.2 lakh duplicate fake/non-existent ineligible beneficiaries (including some due to migration, death, etc.)
5	Minority affairs	Scholarship schemes	—	159.15	159.15	Deletion of 5.26 lakh duplicate, fake/non-existent ineligible beneficiaries
6	Social justice and empowernment	Scholarship schemes	—	238.27	238.27	Deletion of 1.79 lakh duplicate, fake/non-existent ineligible beneficiaries
	Others	Others	1,120	0.69	1,120.69	
	Total		57,029	32,983.71	90,012.71	

Source: https://dbtbharat.gov.in accessed on 18 July 2018.

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The Inclusive Finance India Report is an in-depth, well researched, well analyzed evidence on how the financial inclusion agenda has progressed at various levels and across all the broad themes.

The report covers a review of the performance of diverse institutional structures and delivery models in inclusive finance – the commercial banks, Regional Rural Banks and Cooperative Banks, the new specialised banks, non-bank finance companies, self-help groups and the microfinance institutions. The report covers the initiatives in digital technology that address the last mile delivery challenges and provides an overview of some new initiatives. The report also tracks the performance of programmes and scheme of the government to promote financial inclusion, as also contribution and new initiatives of large apex institutions and regulators.

The report aims to inform the policy development process on inclusive finance, inform banks and investors both national and international, highlight positive impact of various institutions, models and initiatives and identify policy and practice gaps. The methodology of development of the report includes consultations with the RBI, Ministry of Finance, Banks, apex financial institutions, technology services providers, diverse delivery models and technical agencies.

The Inclusive Finance India Report is the best reference book on the annual trends and progress of the financial inclusion in India, covering a comprehensive data based analysis of all streams of financial inclusion with most current information in terms of numbers and developments; a must for every stakeholder in the financial inclusion value chain.

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