

## India Post Payments Bank – Problems and Prospect

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**Type of Review:** Peer Reviewed.

DOI: <http://dx.doi.org/10.21013/jmss.v7.n2.p28>

### How to cite this paper:

**Meena Kumari, K.** (2017). India Post Payments Bank – Problems and Prospect. *IRA International Journal of Management & Social Sciences* (ISSN 2455-2267, 7(2), 364-372. doi:<http://dx.doi.org/10.21013/jmss.v7.n2.p28>

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**ABSTRACT**

*Payments Bank is a new kind of bank which is promoted with the express purpose of extending the reach of banking to vast majority of the unbanked and under banked segments of the population. Payments bank promoted by India Post is expected to use the physical network of post offices as well as digital platforms such as mobile, internet banking, debit cards, point of sale devices, etc. to provide the designated financial services at low cost to target population. Payments Bank might be able to provide last mile connectivity especially in those areas which do not have any bank branches but has a post office. Its' huge presence in rural areas and the trust that it enjoys among vast segments of population might enable it to succeed where commercial banks have failed. The present study examines the role and objectives of payments banks with special reference to India Post Payments Bank, relevance in achieving financial inclusion objective, prospective challenges and problems, suggestions for overcoming those.*

**KEY WORDS:** Differentiated Bank License, Unbanked population, Financial Inclusion, Postal services.

**INTRODUCTION**

With around 60 percent of the population still under banked, a need was felt for establishment of a Payments Bank which specializes in providing a channel for savings and for remittance and payment services. Payments Bank is a specialized bank formed with differentiated bank license and has limited purpose. The primary objective of setting up of payments banks is to further financial inclusion by providing small savings accounts and payments or remittance services to unbanked segments of population such as migrant workforce, low income households, small businesses and other unorganized entities. It facilitates a large volume of low value transactions in deposits and payments or remittances, in a secure technology-driven environment. As per the Reserve Bank of India Guidelines for Licensing of "Payments Banks" issued in November 27, 2014, the following are the guidelines:

- i. The payments bank will be registered as a public limited company under the Companies Act, 2013 with a minimum equity capital of Rs. 100 crore. It is a Scheduled bank and will be governed by the provisions of the Banking Regulation Act, 1949, Reserve Bank of India Act, 1934, Foreign Exchange Management Act, 1999, Payment and Settlement Systems Act, 2007, Deposit Insurance and Credit Guarantee Corporation Act, 1961, other relevant Statutes and Directives issued from time to time.
- ii. It can be promoted by existing non-bank Pre-paid Payment Instrument (PPI) issuers authorized under the Payment and Settlement Systems Act, 2007 and other entities such as individuals, professionals, Non-Banking Finance Companies, mobile telephone companies, super-market chains, companies, real sector cooperatives and public sector entities.
- iii. Maximum permitted balance in current or savings account is Rs. 100,000 per individual customer with aggregate withdrawals and transfers in a month not exceeding rupees ten thousand.
- iv. Its activities are restricted to acceptance of demand deposits, provision of payments and remittance services. It cannot undertake lending activities. It can issue ATM / Debit Cards, but cannot issue credit cards.
- v. It can use various channels such as branches, Automated Teller Machines (ATMs), Business Correspondents (BCs) and mobile banking, etc. for providing the aforementioned services. To leverage technology for providing services at low cost, it must have enabling systems in place, collaborations with third party service providers.

- vi. It can undertake other activities such as distribution of mutual fund units, insurance products, pension products, arrangement of utility bill payments etc. on behalf of its customers and general public.
- vii. It is required to maintain 25% of its current and fixed deposits as Cash Reserve Ratio (CRR) with RBI, invest minimum 75 per cent of its demand deposit balances in Government securities or Treasury Bills which are recognized by RBI as eligible securities for maintenance of Statutory Liquidity Ratio (SLR).

Thus payments bank is a new kind of bank promoted with the express objective of extending banking facilities to the unbanked. Since it caters to small depositors having limited means, their accounts can be opened as no frill accounts with no minimum balance, while the maximum balance can be Rs. 1 lakh. It cannot lend or issue credit cards. Hence, the main source of income is transaction fees and not interest spread. To be commercially viable, it has to provide services at low cost and in large scale. For this purpose, digital platforms such as mobile phones, debit cards, Point of sale devices, etc. would be used along with physical network of branches.

India post is one of the eleven entities to secure license from RBI for establishment of payments bank. It is expected to provide small savings accounts, payments and remittances to migrant workforce, low income households and others in rural and remote areas through linkages with its network of post offices across the country.

## LITERATURE REVIEW

Kesavan (2015) attempted to understand changes in the banking sector over a period of time and observed that innovative and new services are being provided through the establishment of Payments Bank. It would be beneficial to the customers as well as to the banking system as a whole.

Mehra (2015) observed that establishment of Payments Bank represents an effort to redefine banking in India. It would enable poorer citizens who primarily transact in cash to take their first step into formal banking and accelerate India's journey to cash less economy.

Merchant (2015) observed that Payments Bank will pave the way for financial inclusion through a combination of physical branches and digital platforms. Payments Bank with low cost innovative and convenient service, adequate capital would immensely benefit the consumer. However, it would have a negative impact on small and medium sector banks in terms of their market share and incremental deposit growth. Large public sector banks would also suffer loss of market share in payments transactions and Government transfers.

Kohil and Patel (2016) were of the view that though credit is important, payments and savings are also central to efficient financial system. Payments Bank would help in channelizing savings of unbanked population by providing last mile connectivity in rural areas where physical access is difficult. Such savings could be used for productive purposes which would contribute to the growth of the economy. Its profitability is directly linked to economies of scale and identified the following factors as essential for it to succeed: designing right products, patient capital with adequate levels of investment, strong marketing and well managed distribution networks.

## OBJECTIVES OF THE STUDY

1. Need and objects of India Post Payments Bank
2. State of financial inclusion so far
3. India Post Payments Bank – suitability in achieving financial inclusion objective
4. Prospective challenges and problems in achieving financial inclusion

5. Suggestions for overcoming challenges

**METHODOLOGY**

The study is descriptive in nature. It examines the regulatory framework, potentiality in promoting financial inclusion, possible challenges in promoting financial inclusion and provides suggestions for overcoming those. The study is based on secondary data collected from published sources such as reports published by RBI, Department of Posts, World Bank, News Paper reports, etc. The data collected is analysed and presented to provide a simple and lucid narrative.

**NEED AND OBJECTIVES OF INDIAPOST PAYMENTS BANK**

India post payments bank is established with a corpus of Rs. 800 crore contributed by the Government of India and is expected to be professionally run with a chief executive at the helm. It is to become operational with 650 branches and 5000 ATMs and has a potential to generate employment to 3500 banking professionals. Grameen daksevak in rural post offices would be given handheld devices for digital connectivity<sup>1</sup>. It is expected to use the already established network of post offices by India post or Department of Posts for extending services along with mobile banking, internet banking, etc. It is established with the objective of bringing large number of individuals and small businesses under the ambit of formal financial banking institutions by offering the following:

- i. Demand Deposits-Savings account of upto Rs. 1 lakh and Current Accounts with special focus on Micro Small and Medium Enterprises (MSMEs), small entrepreneurs, village panchayats, Self Help Groups (SHGs) etc
- ii. Direct Benefits Transfer (DBT) of social security payments to beneficiaries
- iii. Utility bill payments for electricity, water, telephone, gas etc
- iv. Payments of various Central and State Government and Municipal dues and fees of various Universities / educational institutions
- v. Person to Person remittances both domestic and cross-border with special focus on migrant labourers, low income households
- vi. Distribution of third party financial products such as insurance, mutual funds, pension and credit products

By establishing Payments Bank, India post is expected to accelerate its financial inclusion efforts and actively contribute to extending the reach of banking institutions among vast majority of unbanked and under banked segments of population.

**STATE OF FINANCIAL INCLUSION IN INDIA**

Financial Inclusion refers to providing access of basic financial products and services to all segments of economy including low income households, small businesses, rural and migrant population, etc. There are around 2 Billion people worldwide lacking access to basic financial products and services<sup>2</sup>. With several studies establishing the link between financial access to and use of financial services and socio-economic development, financial inclusion has become a goal for majority of the countries of the World.

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<sup>1</sup>Dhirendra Kumar. (2016, June 3.) Get all 650 India Post Payments Bank Branches working in 1 year: Modi. *Millennium post*, New Delhi.

<sup>2</sup>Demirguc-Kunt, Klapper, Singer & Van Oudheusden, (2015). The Global Findex Database 2014: Measuring Financial Inclusion around the World. Policy Research Working Paper 7255, World Bank

The Government of India and the Reserve Bank of India adopted a bank-led approach to financial inclusion. Several measures were adopted over the last decade such as opening of 'no frill bank accounts or basic saving bank deposit accounts with minimum or nil balance, relaxing know your customer norms, etc. Commercial banks were required to open 25% of the new branches in rural and remote areas and specific area targets were given to them. However, the progress on financial inclusion is far from satisfactory and much needs to be done to achieve the target of financial inclusion.

The World Bank Findex Survey states that on an average, only 35 per cent of the target population in India has at least one bank account. Further, only 45 per cent of the urban population and 32 per cent of the rural population has bank accounts<sup>3</sup>.

Access to bank branches, business correspondent locations, ATMs, enables people to deposit and withdraw cash from their bank accounts, transfer balances from one bank account to another, in a secure environment. It was observed that on an average, 89 per cent of districts in urban areas have 25 or more payment access points per 10,000 population, while only 3 per cent of districts in rural areas have access points indicating low availability of banking facilities in rural areas<sup>4</sup>.

Financial inclusion goals of providing universal access to banking services is being pursued with Commercial Banks using bank branches and intermediaries to provide remittance and credit facilities, savings products. However, the cost of providing basic saving and payment services is becoming an unviable option through bank branches if the volume of transactions is low and of small value. It was observed that for loans less than Rs.5 lakh in value, the bank-branches have shown themselves to be an extremely high cost and high-risk credit channel<sup>5</sup>. Moreover, as branches operate in fixed working hours, anytime access of facilities is not made available to customers.

Banks are permitted to employ agents or intermediaries referred to as Business Correspondents (BC) to extend the reach of banking services and to reduce cost of providing such services. Various studies reveal that the number of BCs in rural India is large and has grown both in rural and urban areas. As of March 2013, there were 2,21,341 business correspondents engaged by banks, showing a growth rate of 548 per cent since 2010. However, very few of them are active, particularly in rural areas and low-income urban areas, where alternative channels such as ATMs are not available. Field research by College of Agricultural Banking, CGAP, and MicroSave suggest that over 75 per cent of the accounts opened and over 25 per cent of BCs are dormant. This has resulted in an absence of financial viability and several have now started to shut down<sup>6</sup>.

## **SUITABILITY OF INDIA POST PAYMENTS BANK IN PROMOTING FINANCIAL INCLUSION**

Providing access to banking services and promoting their usage has been the goal of financial inclusion programme undertaken by the Government of India since the last several decades. With limited success of mainstream banking institutions in this area, there is a need to explore multiple options and channels for extending banking facilities. Post offices all over the world have actively contributed to financial inclusion. Out of total global population of 5.4 billion, 1.5 billion or 28% have access to financial services through post offices<sup>7</sup>. Post Banks set up by post offices have been successful in several countries, notable among them are Post Banks in Japan, New Zealand, Switzerland, France, China, South Korea, South Africa, Morocco<sup>8</sup>.

<sup>3</sup>Dr. Mor, N. (2013). Report of the Committee on comprehensive financial services for small businesses and low income households.

<sup>4</sup> Ibid., p.32

<sup>5</sup> Ibid., p.64

<sup>6</sup> Ibid., p. 66

<sup>7</sup>Ansón&Toledano, (2010).Between Financial Inclusion and Postal Banking: Is the Survival of Posts Also There?UPU

<sup>8</sup> <https://www.indiapost.gov.in/financial/pages/content/ippb.aspx>

Department of Posts or India Post is one of the oldest establishments in the country and dates back to as early as the year 1727. It has established a large network of postal services in the World with 1,54,910 post offices in the country. 89.7% of the post offices or 1,38,955 are located in rural areas. It serves an average of 8,364 people in rural areas and 26,553 in urban areas. A post office serves approximately an area of 21.22 square km. Payments Bank promoted by India Post is expected to use the existing physical network of post offices as the main customer touch points for providing bank services. It is likely to be the most accessible banking service in rural and unbanked areas of the country.

Department of Posts is involved in Financial Services through the operation of Post Office Savings Bank and various savings schemes on behalf of Ministry of Finance. The Post Office Savings Bank (POSB) has more than 400.05 million account holders as on 31.03.2016. The National Savings Schemes and Savings Certificates have an outstanding balance of over Rs.639254.06 crore as on 31.03.2016. The Payments Bank can utilize the experience of the Department of Posts in devising simple, diverse and growth oriented savings products and provide an affordable and convenient banking option to majority of population.

Money remittance service which enables customers to transfer money from any Post Office is provided by the Department of Posts through Instant Money Order and Electronic Money Order Service. Under this service, a person can send an amount from Rs. 1,000 up to Rs. 50,000 in one transaction. Electronic Money Order service, introduced in 2008 provides for transfer of money electronically. It has the advantage of sending money to the door step of the payee and it can be tracked through India. Since payment and remittance service is one of the principal activities of the Payments Bank, it can leverage the cash management expertise of the Department of Posts, devise and deliver cash remittance services most effectively through digital platform as well as through post offices, being interconnected with other banks and entire payments network.

India Post Payments Bank has been promoted primarily for improving Direct Benefit Transfer of various subsidies. Post Office is already transferring various social security benefits to Post Office Savings Bank Account holders. Various Government sponsored social security schemes like the Mahatma Gandhi National Rural Employment Guarantee Scheme (MGNREGS), Indira Gandhi National Old Age Pension Scheme (IGNOAPS) & other pension schemes for social welfare are being implemented. These benefits can now be directly transferred to the account holders of Post Office Payments Bank.

Under Digital India Programme, launched by Government of India in 2014 with the objective of transforming India into a digitally empowered society the post offices are required to work as multi service centres, play a major role in facilitating financial inclusion through disseminating information about government policies and disbursement of social security benefits. Post offices are connected with Core Banking Solution (CBS) Project, to provide facilities of ATM banking, Internet and Mobile banking to its Post Offices Savings Bank (POSB) customers, along with fund transfer facilities using National Electronic Fund Transfer (NEFT) and RTGS. Establishment of Payments Bank is a continuation of the transformation of Post Offices and makes them more relevant<sup>9</sup>.

## **PROSPECTIVE CHALLENGES AND PROBLEMS IN OPERATION OF INDIA POST PAYMENTS BANK**

1. As India Post Payment Bank is not allowed to extend credit, it will not be able to earn income by way of Interest spread. It can earn fee income by way of investment of 75% of its demand and time liabilities in government securities and treasury bills, 25% as demand/time liabilities with other scheduled commercial banks. Hence, it might take a long time for it to breakeven.

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<sup>9</sup>Dept. of Posts. (2017). *Annual Report 2016-17*. Dept. of Posts, Ministry of Communications, Govt. of India, New Delhi.

2. It will not be able to meet the credit requirements of rural population and they might be forced to turn towards money lenders. This defeats the entire purpose of financial inclusion.
3. It is expected to provide services through the application of mobile technology and other forms of digital technology. However, though there is wide spread proliferation of mobile services and mobile phone usage in rural areas, mobile banking has not caught on due to several reasons such as cash preference of customers, security concerns, illiteracy, lack of knowledge about technology products and services. Educating and convincing people to use mobile phones to access banking services could be an uphill task.
4. Since IPPB intends to use existing infrastructure in terms of the already established network of post offices and postal employees in providing payment bank services, it faces the huge task of training staff in around 1,30,000 rural post offices so that they can adequately use digital technology and deliver quality of service. It might have to recruit new staff with adequate banking experience to handle Payments Bank activities.
5. All the post offices are not completely computerized, though IT modernization project was in operation since 2012. Similarly Core Banking Solution connectivity is available in few post offices only. It is necessary to ensure that IT modernization project is successfully completed so as to automate the back end and front end operations of post offices and thereby reduce the cost of providing service. Project Arrow which aims to improve the working conditions in post offices is also in complete.
6. Changing the orientation of postal departmental staff towards banking culture would be another challenge<sup>10</sup>.
7. Though the number of unbanked is quite high, there is Increase in competition from banking and institutions such as Scheduled Commercial Banks, Mobile Service providers. The number of mobile subscribers is on the rise and more so in rural areas where there is lack of traditional bank branches. Though mobile banking has not caught on, if payment and remittances are made available at low cost through mobile phones, mobile banking would see a substantial increase.

### **SUGGESTIONS TO OVERCOME THE CHALLENGES**

1. India Post Payments Bank must work in close collaboration with the Department of Postal Services so as to use its vast network of post offices and the trust that the post office enjoys among the target population. According to Global FINDEX report, 2014 around 43% of unbanked population is living in rural areas<sup>11</sup>. Hence, access to postal network which made inroads in rural areas is very important in reaching the unbanked in rural areas.
2. India post already has amassed experience in mobilizing small savings, management of cash, distribution of social security benefits through its network of post offices. It has been operating small savings schemes on behalf of the Ministry of Finance, Government of India. It also disbursed MGNREGA wages amounting to Rs. 6,943 crores to 697 crore beneficiaries as on 31st March 2016<sup>12</sup>. Its experience in handling large volumes of low margin products can be leveraged to efficiently run the Payment Bank.

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<sup>10</sup>Dhirendra Kumar. (2016, June 3.) Get all 650 India Post Payments Bank Branches working in 1 year: Modi. *Millennium post*, New Delhi.

<sup>11</sup>Nils Clotteau., BsratMeasho. (2016) Global panorama on Postal Financial Inclusion 2016. Universal Postal Union. Switzerland. P 35.

<sup>12</sup>Dept. of Posts. (2017). *Annual Report 2016-17*. Dept. of Posts, Ministry of Communications, Govt. of India, New Delhi.

3. In a study by World Bank in 2013, it was observed that Post offices have a greater chance of reaching out to financially excluded customers than traditional financial institutions<sup>13</sup>. Unlike commercial banks, the focus of payments bank run by India post would be customer service orientation and hence it would be able to reach out to poor, illiterate, marginalized customers. It would be an effective medium to service large volume of small value transactions.
4. In order to handle competition for providing financial services, the payments bank needs to offer the services at low cost to its customers. For this purpose, it is necessary to digitize its operations. Digitization is also required to improve the quality of service to the customer. The IT Modernisation project, which was started in 2012 was able to automate operations and achieve connectivity to electronic network in around 25,000 post offices out of a total of 156000 post offices. The connectivity rate is 16% while the world average is 58%<sup>14</sup>. This has to be accelerated so that post offices at all levels are enabled to extend uniform service to act as main customer touch points.
5. It must effectively create customer awareness about the products and services that it offers. It must develop products which are innovative, which meet the cash flow pattern and other requirements of the customers and then bring it to the notice of customers through door to door campaigning.
6. Postal staff is in direct contact with the customers and they enjoy the trust of customers. They must be trained to handle banking operations involving multiple delivery channels such as internet banking, mobile banking and so on. India post has developed a comprehensive mechanism for training the employees at all levels in various aspects of banking and computer literacy.
7. Payments Bank must be used as a medium for Direct Benefit Transfer of social security wages and pensions. This encourages people to open accounts and hence becomes an effective medium of financial inclusion.
8. Though Payments Bank cannot directly extend credit, it can offer credit facilities by tying up or in partnership with commercial banks.

## CONCLUSION

Payments Bank established by the Department of Posts has the potential to be the most accessible banking network in the country. With the postal delivery system combined with digital platform such as mobile, internet banking, prepaid instruments, debit cards, ATMs, point of sale devices, Payments bank is set to be the face of transformation of post offices and be major drivers in financial inclusion initiative of the Government of India. However, to realize its potential, it is necessary to undertake modernization of post offices so as to provide uniform service. As post man is to be interface between the bank and the customer, he should be adequately trained to provide banking services. Products should be tailored to the requirements of customers and high level of awareness should be created about them. Once it succeeds in being an effective channel for providing savings, payments and remittance facilities, its activities can be extended to encompass extension of credit as well.

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<sup>13</sup>Ansón, Berthaud, Klapper& Singer.(2013).Financial Inclusion and the Role of the Post Office. Policy Research Working Paper 6630, World Bank

<sup>14</sup> Nils Clotteau., BsratMeasho. (2016) Global panorama on Postal Financial Inclusion 2016.Universal Postal Union. Switzerland. P 38

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