The evolution of neobanks in India

Impact on the financial ecosystem

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Fintech Convergence Council

Message from PwC

Vivek Belgavi
Partner, FinTech, and Alliances
and Ecosystem Leader
PwC India

Neobanks have evolved and grown significantly worldwide as well as in India despite their relatively recent entry into the larger FinTech segment. The definition of neobanks has changed as they are differentiating themselves from online banking services and moving away from being centred only around digital banking to focus on providing a superior customer experience.

Technological advancements, innovative models and niche customer-focused approach have helped neobanks in creating novel, technology-based platforms and agile business models, and delivering innovative financial services. Such advancements are providing neobanks with the ability to reach unserved and underserved segments of society and provide them with customised portfolios of services that are targeted to meet their financial needs, both across retail as well as business segments.

Neobanks and most of their product offerings are not directly regulated in India. However, they are subject to indirect regulations (through their partnerships with regulated entities), ensuring that their product offerings are in adherence to the regulatory norms. It is critical that regulations evolve gradually in line with the advancement of the sector to ensure that the sector matures further. As the neobanking space becomes more stabilised with the introduction of new business models/ products, the segment may require standalone regulations which will monitor the market.

This report aims to provide incumbent banks, new-age neobanks, regulators and other stakeholders with a comprehensive view of India's neobanking landscape and will help to identify key focus segments, business models, drivers and enablers of the ecosystem. I would like to thank the Internet and Mobile Association of India (IAMAI) for taking the initiative of conducting relevant research to prepare this report and inviting PwC India to be a knowledge partner to share our point of view on this emerging sector which is expected to play a critical role in achieving greater financial independence across the country.

Message from FCC

Jitendra Gupta
Chairman, Neobanking Committee,
Fintech Convergence Council (FCC),
and Founder and CEO, Jupiter Money

The Indian financial services sector, especially banking, is on a transformational path with the advent of the increasing number of neobanks in the country in the past couple of years. The constant challenges pertaining to last-mile connectivity, bringing millennials in the ambit of the banking domain, facilitating branchless banking, providing seamless banking experiences, etc., faced by the Indian banking sector are soon turning out to be a thing of the past as the core business model of neobanks addresses these issues right at the outset. With the tie-ups between financial institutions and neobanks proliferating with every passing day, a transition from a customer-led to a customer-centric financial services offering is evident. It is heartening to witness this shift and how financial institutions are seamlessly adapting to the evolving technological and digital needs of customers by collaborating with neobanks.

The disruptive and innovative technologies, digital-only presence, conducive regulatory environment, etc., are some of the apparent contributors to the growth story of neobanks in India which syncs with their global growth as well. With the current momentum, neobanks are likely to leapfrog in the coming years and become a financial services behemoth, and have a positive impact on the overall growth of the financial services sector in India. And while this evolution takes place, it will be interesting to see how the roles and approaches of various stakeholders will evolve and shape the future of neobanks in India.

On the one hand, with neobanks not being directly regulated currently for some of their activities, the regulators will have to keep up with the pace of innovations and operations of the former to assess the right time to holistically regulate them. On the other hand, neobanks will have to continually navigate the critical requirements such as data privacy, cyber security and regulatory compliances to gain confidence of the regulators. Amidst these developments, financial institutions will have to ensure that they strike a fair balance between growth, compliance, customer services and their overall ethos.

Through this report, we intend to enable the incumbent and aspiring neobanks to comprehend the global and Indian neobanking landscape from a business and regulatory standpoint, and also engage with regulators and other stakeholders on the proposed regulatory regime for neobanks in the country.

I would like to thank PwC and my co-members of FCC's Neobanking Committee such as Open, RazorpayX, NiYo, Fi, One Card, and InstantPay for their contribution to this report.

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Neobanking: The next banking revolution

The definition of a neobank has evolved despite its relatively recent entry into the larger FinTech segment. Originally, a neobank was defined as a bank that had no physical presence and functions completely online while interacting directly with the consumer. A neobank does not aim to be just another bank but one that provides a better digital banking experience.

This definition has evolved as neobanks have tried to differentiate themselves from online banking services offered by incumbents and shifted from being centred only around digital banking to focusing on providing a superior customer experience.

This shift is not new or unique to the neobank subsegment. The larger FinTech industry has always focused on digital technologies and customer delight as its two key cornerstone policies. However, there has been a subtle shift in neobanking policies. For example, \alternative lenders now tend to focus on embedded finance and use-case centred lending as opposed to only pure-play lending platforms and marketplaces. The same strategy has emerged in other FinTech segments as well, as players look to seamlessly integrate financial services within larger customer needs to develop more sustainable demand and product innovation. Digitisation of the whole banking and transactions journey, upgrading legacy systems and ways of serving customers, and being the enablers of transactions at source are leading to the large-scale development and adoption of embedded finance. Banking is evolving rapidly as a part of embedded finance to focus on customer delight.

Neobanks are flourishing by addressing the primary needs of end consumers

Neobanks have shifted their focus towards providing superior customer experience. Therefore, it is useful to identify the needs of such target customers which in turn have fuelled and sustained the growth of neobanking in India and worldwide.

Access

- Access to financial services continues to be a core need of retail and micro, small and medium enterprise (MSME) customers alike. Neobanks have found untapped opportunities in various customer segments, including tier-2 and 3 rural areas as well as digital millennials. While banks in India are mandated by regulatory bodies to focus on the unbanked/underbanked population (about 58.4%)[1] and do so primarily in tier-2 and 3 rural segments, millennials who also constitute a large part of the unbanked/underbanked population receive limited attention. Neobanks play a pivotal role in addressing their needs as they are digitally savvy and have showed interest in accessing financial products in the recent past.
- A majority of MSMEs in India still rely on informal financial services for accessing credit. MSMEs owe a total of INR 69.3 lakh crore in debt of which INR 58.4 lakh crore[2] is from informal sources.
- The overreliance on informal credit sources is perpetuated by the rigidities and inefficiencies of traditional bank distribution models with higher acquisition costs that make certain customer segments unviable for traditional banks.

Aligned financial products

- Customers today require products that can be customised to more specific needs in terms of quantum/ticket size, tenure and cost.
- Such product innovations require dynamic technology and delivery solutions that enable start-ups to effectively manage unit economics flexibly while offering a variety of products in terms of quantum and pricing (e.g. micro ticket-size loans/investments and short-tenure credit). Traditional banking models are usually unable to offer such flexible financial products given the rigid cost structures they operate under.

Convenience

- Customers today can experience superior facilities across different service lines – from commerce and purchasing to logistics and travel – and these have led to similar expectations of convenience from financial services.
- Core service tenets of instant access to information, easier capture of data and requests, and customised points of service delivery (e.g. credit line at point of sale [POS] terminals) have become more commonplace and are expected from financial services delivery channels as well.

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1 https://www.rbi.org.in/Scripts/PublicationReportDetails.aspx?UrlPage=&ID=924#CH2

2 https://www.ifc.org/wps/wcm/connect/dcf9d09d-68ad-4e54-b9b7-614c143735fb/Financing+India%E2%80%99s+MSMEs+-+Estimation+of+Debt+Requirement+of+MSMEs+in+India.pdf?MOD=AJPERES&CVID=my3Cmzl

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Non-financial services synergies

- An offshoot of seamless customer service is the amalgamation of financial services offerings within a larger customer experience flow. Strategies such as embedded finance are seeing traction as end customers prefer a frictionless journey to the point of consumption.
- Service needs such as e-commerce, individual tax and personal finance management (PFM) services, digital commerce platforms, GST filing, accounts receivable (AR)/accounts payable (AP) tracking and reporting services for MSME customers are requirements that have elements of financial services embedded within a larger need.

These customer needs and the gap in current traditional banking services are the primary drivers for sustained growth of neobanks as they have been able to operate in this gap to capture the market and carve out revenue streams.

Secondary need – incumbents' collaboration

Incumbents continue to realise the limitations of their existing modes of operation and accept the benefits of collaboration to facilitate faster go-to-market strategies. Their needs for developing streamlined and low-cost acquisition and distribution models, and providing superior customer experience have become secondary drivers for neobank growth. This has led to the emergence of banking as a service (BaaS).

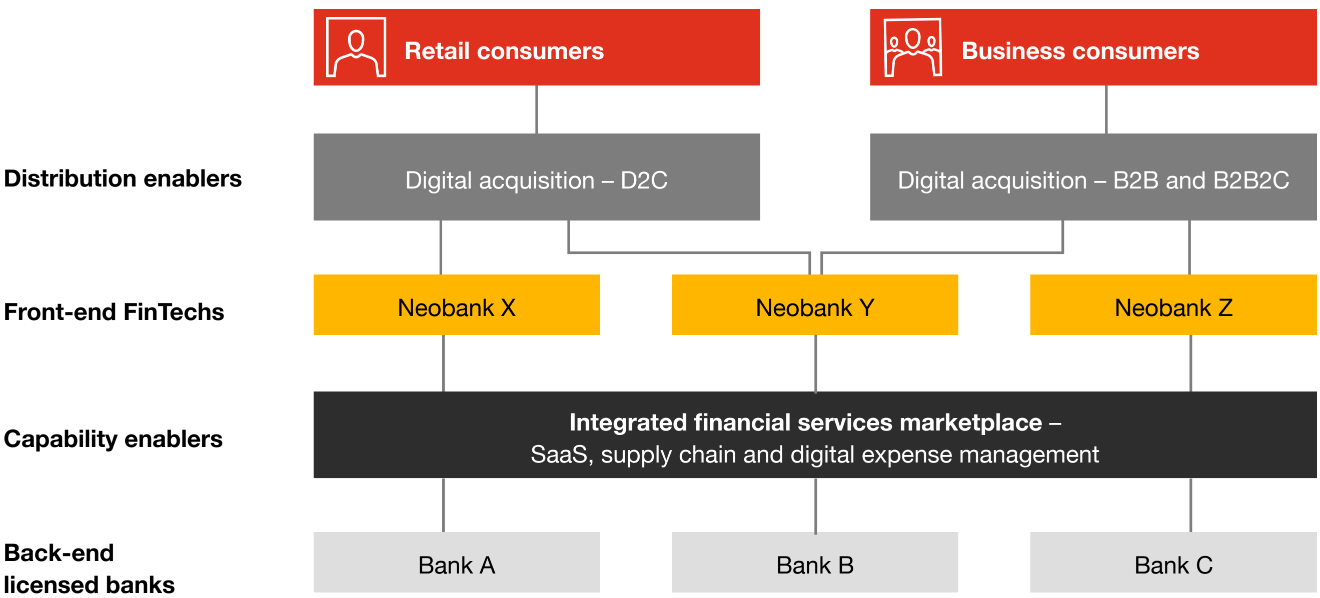
BaaS helps FinTechs to use application programming interfaces (APIs) to connect with banks, enabling them to build their financial services on top of the regulated infrastructure. Neobanks use the BaaS APIs to provide customer-initiated onboarding, account funding and other banking activities.

Banks can opt to **deliver banking services** (focus on risk management and build financial infrastructure) and allow distribution and customer interaction to be managed by other parties, i.e., FinTech companies, software-as-a-service (SaaS) players and marketplaces.

Ease of use is of significant appeal for customers. For example, a small business can get open bank account using its accounting software or avail loans directly on a logistics platform.

Today, organisations of all types with varied levels of maturity, including marketplaces, BigTechs and software companies, and logistics firms are offering embedded financial services to serve retail customers and small businesses.

Operational architecture of neobanks



Source: PwC analysis

This unique positioning of neobanks has led to the emergence of the following subcategories:

- **Pure-play neobanks** – players that are primarily digital in terms of their operations and customer-interaction models, and offer core banking (liabilities products) and relevant value-added services.
- **Incumbent digital subsidiaries** – existing traditional banks that started off with a brick-and-mortar approach and have significantly redesigned their complementary digital offerings for end consumers.
- **Enabling adjacency** – players that are not yet in the banking space but have either:
  - been able to develop a strong customer base, are strong distribution enablers for existing banks and neobanks, and are poised to pivot into a neobanking model, or
  - developed capabilities and offerings that are strong capability enablers and would significantly expand the core offerings of banks.

1.1. Evolution of the global neobanking landscape

The neobanking space has witnessed strong growth across North and South America, the UK, Europe as well as the Asia-Pacific (APAC) region.

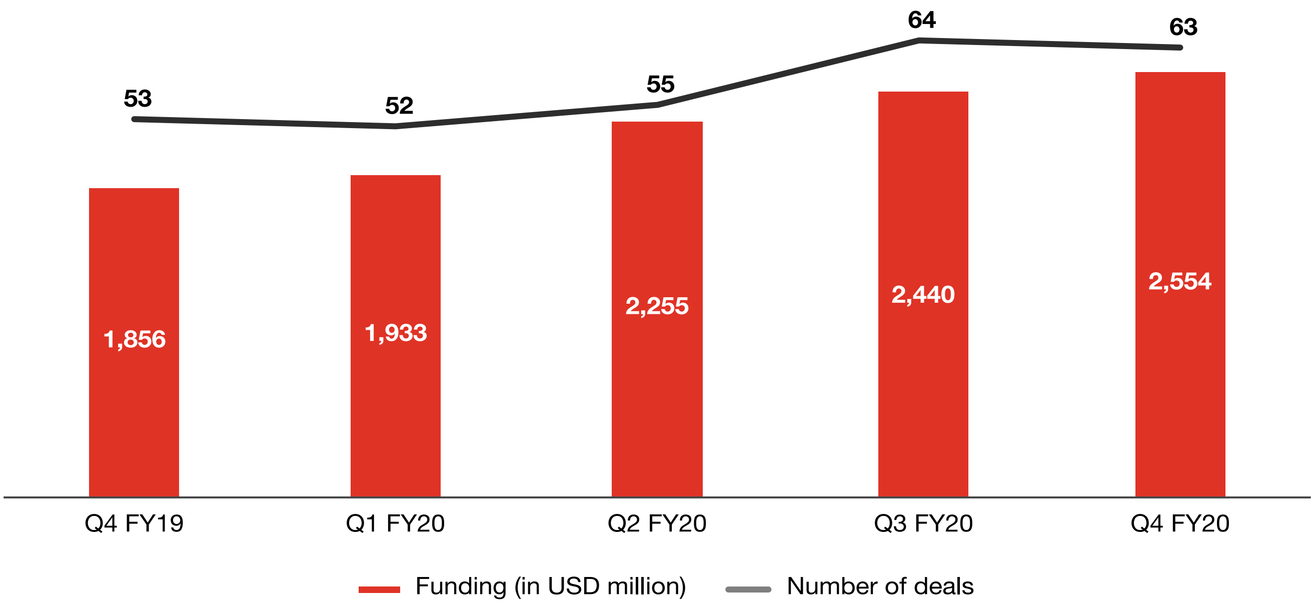
The UK has had a head start in neobanking due to the early introduction of common banking guidelines for the entire European Union (EU). FinTechs used APIs for developing open banking platforms that are tailor-made to form partnerships with banks to serve niche customer segments. This propelled the growth of neobanks in the UK and they went on an acquiring spree while complying with the regulations.

The first set of neobanks emerged from Europe. They were regulated by the original Payment Services Directive (PSD), an EU directive to regulate payments services and service providers, which helped increase industry transparency and provided easier access to new entrants. This was followed by PSD2 which mandated third-party access to the APIs of banks. This open data-sharing landscape resulted in the growth of neobanking FinTech firms as they were able to securely access customer account data and build digital-only banks. The US, Canada and several EU countries followed suit, leading to the prominence of neobanking players with a few having presence across multiple jurisdictions.

The funding received by neobanks and the number of deals closed in this segment reflect the increased interest in this sector. Neobanks witnessed consistent deal activity throughout 2020 despite the pandemic and in some cases, buoyed by the pandemic. Investors realised the potential that neobanks bring to the larger financial services industry.

The figure below analyses the global venture capital (VC) backed banking financing trends for Q4 FY19–20.

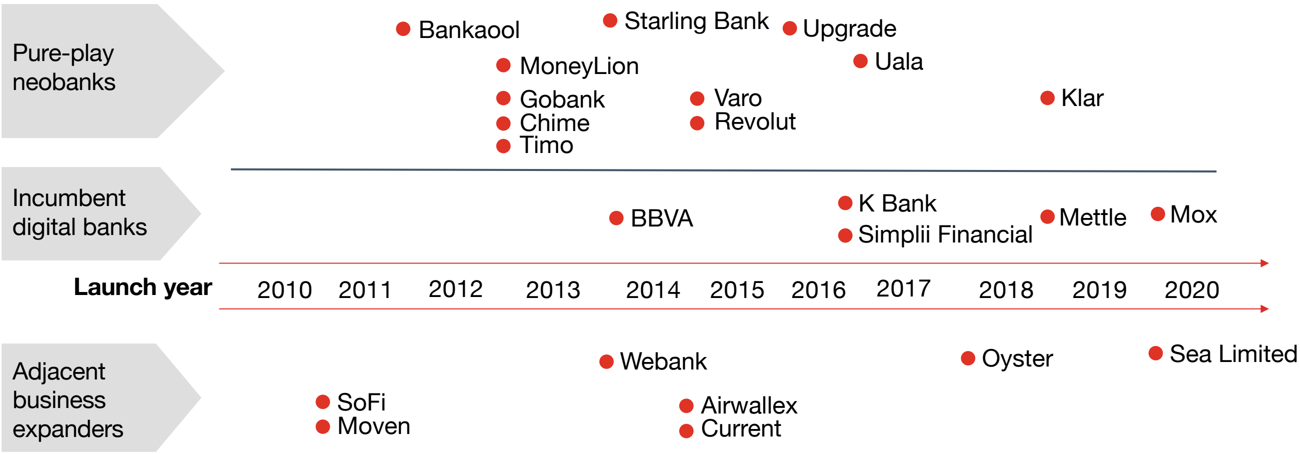
Global digital bank funding (VC based)



Source: CB Insights

Apart from the pure-play neobank segment, several digital bank offerings helped many incumbent banks to grow strongly in Q4 FY19–20. Many adjacent business expanders have also shown signs of pivoting into the neobank space. This growth has been achieved due to a combination of innovative customer-segment and product strategies as well as facilitative regulatory steps and practices.

Types of players entering the neobank space



Note: For illustration purposes only. Not intended to be an exhaustive list

Source: PwC analysis

It would be interesting to look at the different strategies adopted by financial services players for entering the neobanking space.

One such strategy is to start with a gateway financial service to attract customers and then provide additional services. For example, a leading UK-based neobank started off as a money transfer and exchange platform before expanding into a global, multiproduct player. Another example would be the CEO and co-founder of a leading Brazilian neobank describing how it launched credit cards as its first offering when entering into a new market to let customers get accustomed to digital-only banking, before offering other debit products.

An equally interesting strategy is the emergence of several non-financial services players with established customer bases who are venturing into the neobanking space. This is particularly evident from the neobank licences that have been issued to players recently, particularly in the APAC region. Telecom players, ride-hailing and delivery apps, e-commerce platforms, and social media messaging and digital entertainment players have entered into the neobanking space. There is a clear and visible trend of organisations with large consumer bases identifying strong monetisation opportunities through financial services pivots.

Regardless of the strategy adopted to enter the neobanking space, players must utilise digital channels and innovative incentive strategies to develop a strong customer base before offering diversified financial services.

Types of customer segments

While the customer segments that global players are catering to are quite aligned with the trends witnessed for their Indian counterparts (retail and business segments with specific subsegment focus), the customer acquisition and product strategies adopted are distinct and interesting.

Retail customer segment

Neobanks catering to the retail segment have focused on combining basic banking at competitive and affordable prices with strong value-added services and acquisition strategies.

- Apart from deposit accounts, reduced transaction fees and waived ATM withdrawal charges, some global players build on spends analytics offerings to help users plan their goals and expenses.
- A UK-based neobank has combined its spend analytics offerings with special sub-accounts to help users develop customised and automated savings plans and behaviours. It also caters to children through special accounts and prepaid cards.
- A US-based neobank specifically targets new-to-credit customers and allows them to develop their credit history through special credit cards that are initially backed by cash deposits. It reports the transactional behaviour to credit bureaus, thereby helping customers build their credit history.
- A Singapore-based neobank specifically focuses on young travellers and millennials by offering a multi-currency travel wallet.
- Some neobanks have expanded to allow investment options for their customers. A popular product is the 'round-up' service that rounds up transaction amounts to the nearest 10/100 and deposits the extra value into a savings/investment account. A leading neobank also allows its customers to invest in various asset classes, including gold, cryptocurrency, commodities and shares.
- A leading global neobank provides tailored insurance products such as customised travel insurance, car rental insurance, mobility insurance for shared vehicles, phone insurance and winter sports insurance to its consumers.
- The super app approach is another strategy being adopted by neobanks worldwide. A leading Russian neobank offers a host of mobile apps that can be used for paying traffic fines and taxes other than usual banking activities. It also facilitates e-commerce purchases as well as booking flight, rail and movie tickets.

Business customer segment

- Apart from the more standard business accounts, lending and cross-border payments offerings, some neobanks offer value-added services such as open APIs and seamless integration with business apps (accounting and business communication apps) to embed financial services offerings within their larger business framework. A leading neobank offers business customers with website building options, invoicing, AR tracking and online bookkeeping services.
- Other neobanks have looked at helping with business incorporation and set-up as a value-added service.
- From an acquisition perspective, some neobanks are leveraging digitised supply chains for faster customer access. A leading Chinese neobank has tapped into the 5,000-strong distributor ecosystem of a Chinese food manufacturing company to provide banking services.

Other banks as a customer segment

Several global players are offering their capabilities as services that other banks can utilise. This strategy is particularly relevant to the Indian ecosystem where neobanks must currently partner with traditional banks and develop offerings that their partner banks can benefit from.

- Some players have developed personal finance management and credit scoring offerings that can be utilised by traditional banks to provide their end retail customers with value-added services.
- A few players offer credit assessment modules and loan portfolio management capabilities for banks to access and consume.

1.2. Evolution of neobanking in India

The Indian neobanking landscape has grown exponentially over the last two years. Even with over 18 players[3] vying to scale up their businesses, aspects like distinct product offerings and target customer segments of each neobank ensure substantial growth potential for them in the coming years. The journey of financial services in India is evolving with upgraded banking infrastructure, new banks and regulatory mandates, and technologically advanced FinTechs, with an increased focus on customer needs. Additionally, factors like incumbent banks looking for strategic partnerships with neobanks and interest from private equity players[4] are adding to the growth story of India's neobanking space.

The Indian neobank ecosystem landscape

Start-up neo-banks are growing year on year (YoY) and building a competitive digital banking landscape. Indian neobanks are yet to receive specific licences or regulatory approvals. Hence, digital banks/challenger banks don't exist in the country unlike in some foreign countries. Banking partnerships form the core of neobanks in India and this is a major difference between the global and Indian neobanking models.

3 PwC analysis

4 Total funding to this segment stood at USD 163 million as of Q1 2021 with some traction being witnessed in the initial months of 2021.

The table below compares the Indian and global neobanking business models:

Particulars	**Global model –** licensed digital banks	**Indian model –** partnerships with licensed banks
Regulated	The financial regulators of some countries, especially developed nations, issue licences to neobanks and regulate them.	Indian neobanks are FinTech companies which are not directly regulated by the Reserve Bank of India (RBI). They partner with licensed banks, NBFCs and other financial institutions to provide financial services through their digital platforms.
Branches	Globally, neobanks usually do not operate as traditional banks and hence have zero or minimal physical branches as required by the prevailing laws.	Neobanks in India do not have a physical presence given the nature of their business model and the absence of regulatory requirements. They primarily interact with customers through digital platforms. However, customers can still access physical branches of partner banks/financial institutions.
Scope of services	The primary role of neobanks globally is to deliver banking services through the internet or other electronic channels instead of physical branches. The more mature neobanks provide the whole gamut of financial services.	Neobanks provide a range of financial services in partnerships with other regulated entities. These services include: • opening of bank accounts • loan/credit facilities • prepaid card services • investment advisory services • insurance services, etc. Some of the neobanks which target and serve MSMEs and other non-retail segments also provide white-label solutions such as expense management, preparation of invoices and vendor payment management.
Permissibility	The digital banking business model is regulatorily permissible across the UK, US, Canada, Singapore and Hong Kong.	These types of partnership business models are prevalent in India with no specific restrictions on operations.
Compliances	Digital banks must comply with the relevant frameworks and regulations issued by the regulatory authorities.	Neobanks in India are not directly subjected to complying with the RBI due to the absence of a prevailing licensing regime. Typically, the partnerships with regulated entities are governed by the RBI's Outsourcing Regulations, Business Correspondent Guidelines and Master Directions on Digital Payment Security Controls, and applicable to the partnering regulated entities. The applicability of these guidelines is driven by the nature of services offered by neobanks.

Framework for analysing neobanking strategies – global vs India

Based on the key strategies witnessed in the neobanking space across the globe, we have identified key strategic levers neobanks are adopting to differentiate themselves from traditional banks and build their services portfolio.

Indian neobanks have adopted strategies similar to their global counterparts in terms of customer segment focus and services. As there is no official licensing route for such players yet, the primary strategy for providing core banking services has been achieved by partnering with incumbent banks. This has in turn defined the service offerings and strategic levers that Indian neobanks focus on.

Key strategic levers for neobanks

Strategy	Levers		
Customer	Customer segment targeting	Customer acquisition	Customer experience
Product and process	Financial services product innovation	Non-financial services product synergies	Process and channel
Partnerships	Manufacturer strategy		

- Understanding a specific strategy of a neobank would require understanding how uniquely it is applying specific levers
- The availability of a banking licence has a distinct effect on the strategic levers chosen:
  - Neobanks with bank licences would focus on customer experience and superior financial services product innovation
  - Non-licensed neobanks would focus on customer segment, acquisition and non-financial services product synergies

Source: PwC analysis

Global and Indian neobanks are evolving rapidly along the lines of these strategies and levers that are influenced by market dynamics and opportunities. Global and Indian neobank archetypes are compared in the table in the following pages using the above framework.

Parameters	Levers	Global	India
Customer	Customer segment targeting	• Global neobanks continue to focus on both individuals and MSMEs. • Focus on niche segments such as teenagers, families and millennials is rising significantly. • There is an upsurge in the number of neobanks across the US and Europe that are focusing on customers in the age group of 10–20 years.	• Similarly, Indian neobanks are focusing on retail and MSME segments. • There is an increased focus on providing services to the underserved segments such as teenagers, gig economy workers, blue-collar workers and SMEs. • Multiple neobanks are coming up with service offerings targeted towards small businesses by providing them with a portfolio of financial services. • Some examples of customer segments focused on by neobanks are: — a Bengaluru-based neobank is providing teenager-focused services — another Bengaluru-based neobank has launched a digitally enabled platform for SMEs.
	Customer acquisition	• Major acquisition channels of neobanks are online, driven by them and their partner platforms.	A mix of offline and online acquisition channels that vary as per the target customer. • A Delhi-based neobank focused on providing services to the underserved and small businesses by offering a host of payments and booking services via its app and network of offline agents. • A newly launched start-up is focusing on services for teenagers on a digital-only platform.
	Customer experience	• Agile and innovative best practices are followed in terms of flexibility, self-service capabilities, customer needs and personalisation.	Neobanks are focusing significantly on customer experience as they cannot serve them directly due to the absence of standalone licences. Hence, they are looking to provide integrated financial services. • A Bengaluru-based neobank focusing on millennials and salaried individuals offers a portfolio of services such as forex cards, mutual fund investments, current account savings account (CASA), expense management, among others. • Multiple neobanks targeted towards teenagers are offering solutions such as expense management, split-money options and financial education platforms in addition to financial services.

<table>
<tr><th>Parameters</th><th>Levers</th><th>Global</th><th>India</th></tr>
<tr><td rowspan="3">Product and processes</td><td>Financial services product innovation</td><td>Neobanks across multiple countries are operating with their own banking licences and offering a number of core banking services. They are also innovating these core banking services to enhance customer experience.
• For example, a US-based neobank enables its customers to have automatic savings. Whenever a customer uses a debit card to make a purchase, the amount charged to the account is rounded up and the round-up is transferred from the spending account to the savings account.
Some neobanks are also adopting a partnership-driven model to offer a financial services marketplace to their customers that helps them with:
• wealth management
• lending
• insurance.</td><td>• Neobanks in India are dependent on traditional banks to offer basic banking services. Hence, the expansion in services is driven by offering other financial services of their own:
— A Bengaluru-based neobank merged with a tax advisory services start-up to provide tax filing and PFM services to gig economy workers.
— Another Bengaluru-based neobank acquired a mutual funds focused platform to provide investment services to millennial customers as a part of its wealth portfolio.</td></tr>
<tr><td>Non-financial services product synergies</td><td>• Multiple non-financial services players are expanding into the neobanking space.
— A ride-hailing company has partnered with a telecom company to launch a neobank in Singapore.
— An airline company has announced its plan to launch a neobank in Malaysia.</td><td>Driven by the same rationale of bank-partner dependency, Indian neobanks are also expanding to create an ecosystem of services across:
• job search platforms
• e-commerce platforms
• travel booking facilities.
Non-FinTech players in India with a substantial retail and MSME customer base can expand their offerings towards neobanking.</td></tr>
<tr><td>Process and channel</td><td>• Digital is the primary channel for most global neobanks.</td><td>• Indian neobanks continue to use an offline + online model based on customer segments.</td></tr>
<tr><td>Partnership</td><td>Manufacturer strategy</td><td>• A number of global economies have announced separate digital banking licences for neobanks.
• Multiple neobanks operating on a standalone basis with their own CASA services have achieved significant scale.</td><td>• Indian neobanks do not have the licence to offer CASA services. Hence, partnerships with traditional banks form a core part of their operations.</td></tr>
</table>

The different models and strategies adopted by Indian neobanks are analysed in detail in the following section.

1.2.1. Retail neobanks

Retail neobanks are FinTechs which target individual retail customers such as blue-collar and gig economy workers, teenagers, and students.

The number of Indian retail neobanks has grown significantly over the last few years, with each of them coming up with their own version of product offerings catering to niche retail segments.

For example, a Bengaluru-based neobank launched in December 2020 is providing front-end banking solutions to migrants moving from India to the US and vice versa. The company aims to expand its services to remittances, loyalty-based solutions, cryptocurrency, insurance and credit through partnership networks in the future.

Another neobank launched in October 2020 focuses on children under the age of 18 and lets them make digital and physical purchases. It allows parents to control smart cards through an app wherein they can create in-app chore lists and tie them with perks.

The following are some key customer segments and focus areas that retail neobanks are targeting:

1. Blue- and grey-collar workers: This segment accounts for approximately 250 million[5] of India's population and is significantly underserved by traditional banking players due to their low ticket size and volume of transactions. Neobanks are targeting these segments via a combination of online and offline models, and providing services such as savings accounts, sachet loans, insurance and payments.

2. Gig economy workers: Gig economy workers, including people who work on short-term and on-demand contracts, account for nearly 15 million[6] of India's population. Neobanks can tap into this segment for providing financial services. The recent surge in organisations adopting gig-tech models for certain tasks has provided an opportunity for formalising this customer segment and digitising their relevant transactional data that can be utilised by financial services players for providing customised products.

3. Teenager-focused neobanks: India is home to over 250 million[7] teenagers and this large number is becoming a strong base for the financial services ecosystem. This segment presents neobanks with a significant untapped opportunity as teenagers are growing up in an on-demand world with preferences for digital transactions and e-commerce. As per a survey conducted by a neobank exclusively for Indian teenagers, 84%[8] of them shop online for both big-ticket (gadgets) and small-ticket items (food, clothes and digital subscriptions). Multiple neobanks are providing account services that are focused on this segment, including PFM, imparting financial knowledge and payments services.

4. Digital millennials: Millennials comprise the largest age group in India's population (approximately 400 million).[9] They could be a huge potential customer base for neobanks. These digitally connected individuals are driving the growth of many digitally driven consumer-facing businesses.

Overall, retail neobanks exhibit several characteristics that allow them to carve out a niche space for themselves:

- **Seamless account opening:** Neobanks provide simplified online processes for opening accounts and onboarding customers, thus addressing a major pain point for incumbents.
- **Convenient interface:** Some neobanks provide a 360-degree view to their customers with unified dashboards which are easy to understand and provide key insights such as expenses incurred, due bills and bank statements.
- **Transparent service fees/charges:** Most neobanks have a transparent fees and charges policy as a differentiator and do not impose hidden fees/charges on their customers.
- **Value-added services:** Neobanks provide several supplementary services such as budgeting, curated e-commerce, tax filing and automated accounting which enhance customer engagement.
- **Robust infrastructure:** The product/service offerings of neobanks are protected by robust information technology and security infrastructure.

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5 https://www.businessinsider.in/business/startups/news/this-startup-a-linkedin-like-platform-for-indias-blue-collar-workers-gets-more-funds-from-lightspeed-and-sequoia/articleshow/77866010.cms

6 https://www.thehindubusinessline.com/opinion/indias-gig-workforce-is-on-the-ascent/article33300755.ece

7 hhttps://www.unicef.org/india/what-we-do/adolescent-development-participation

8 https://indianexpress.com/article/parenting/events-things-to-do/how-teenagers-shop-survey-reveals-online-shopping-patterns-in-lockdown-6757773/

9 https://www.morganstanley.com/ideas/India-millennials-growth-sectors#:~:text=India%20is%20on%20track%20to,and%2046%25%20of%20its%20workforce.

Neobanks are able to offer the above-mentioned customised services while maintaining a robust information security architecture and complying with the data security norms of their bank partners.

The table below further summarises some of the core services that neobanks have focused on for some niche retail customer segments.

	Teenagers	Digital millennials	Blue-/grey-collar workers	Gig economy workers/freelancers
Non-financial services	• E-commerce • Educational platform	• E-commerce • Forex services • Booking facilities for travel (hotels, flights and trains)	• Job search platform • Skill enhancement platform	• Assisted e-commerce • Booking facilities for travel (trains and buses)
Non-banking financial services	• Money transfer (UPI) and mobile recharges • Personal finance management	• Money transfer (UPI), mobile recharges, bill payments (BBPS) • Personal finance management	• Money transfer (DMT and AePS) and bill payments	• Money transfer (DMT and AePS), bill payments and recharges
Banking services	• Prepaid card services • Sachet loans	• Savings account • Credit • Investment • Insurance	• Savings account • Credit on tap • Sachet insurance	• Savings account • Credit • Micro investments

Customer segments

Source: PwC analysis

Case study #1

A two-year old Bengaluru-based neobank is targeting salaried individuals aged between 25–35 years and focusing on providing wealth creation and lending services.

We briefly look at the different strategies adopted by the neobank:

Customer segment targeting: It is focusing on digital millennials to provide them with savings services. When it comes to saving money, the average household savings rate is witnessing a decline as more avenues to spend money open up. As individuals are inclining towards purchasing/buying more, the neobank is focusing on providing them with solutions on managing the three key aspects of their money – know, organise and grow your money.

Partner strategy: It is looking to combine organic and partnership-led growth to provide customers with a range of finance management services. It has also has partnered with an upcoming bank.

Financial services: It is currently providing offerings such as savings account, lending and investment solutions and looking to expand into mutual fund distribution and stockbroking.

Non-banking financial services: It allows customers to link all their bank accounts in a single platform and provides a dashboard to track transactions simultaneously. It also uses an artificial intelligence (AI) driven data model to recommend budgets based on the spending habits of customers.

As per the neobank, the Indian financial services market is at a point where digital banking is increasingly becoming commonplace. Though digitisation is still an important aspect, strategies are being directed towards focusing on the consumer segment and creating solutions specifically for them. Traditional banks operate with a one-app-for-all model, providing standardised services to a broad range of customer segments. In contrast, neobanks are looking to develop universal solutions and focusing on the consumer segment to provide the best curated and specific experiences.

1.2.2. MSME neobanks

MSME neobanks in India have recently started gaining traction. These FinTechs are targeting MSME customers who have faced issues in accessing formal credit. Even though India's MSME sector accounts for 29%[10] of the country's GDP, it has been largely ignored by the traditional banking sector due to high acquiring and servicing costs.

MSME sector overview, contribution to GDP, exports and NPA

Annual turnover	Segment	Contribution to GDP	Contribution to exports	Overall credit exposure (in INR lakh crore)	NPA
>INR 250 crore	Large	71.1%	51%	46.7	18.7%
INR 75–250 crore	Medium			4.7	18.1%
INR 5–75 crore	Small	28.9%	49%	8.9	10.8%
<INR 5 crore	Micro			4.6	8.9%

Source: MSME annual report and Transunion CIBIL MSME report

The figure below depicts why MSMEs have remained unserved/underserved by traditional banks.

Lack of customised offerings

MSMEs generally have limited collateral, improper documentation, incomplete tax returns, inadequate accounting etc., making them ineligible for availing traditional asset-backed loans offered by banks. Neobanks are offering integrated invoice generation and tax-filing services which help them provide customised cash flow based loans and invoice discounting suitable for small enterprises.

High cost of acquisition limiting eligible MSMEs

With a relatively low turnover, lower-rung MSMEs tend to be a low priority for banks due to the high cost of acquisition. By providing digital onboarding even in remote locations, FinTechs have a wider market to access. They are also reaching out to the lower-earning and unorganised employees of MSMEs through individual tie-ups with employers. This has increased the revenue potential for neobanks.

High cost of servicing

Low digitisation of MSMEs leads to high cost of servicing and cumbersome document collection processes for banks who find it difficult to service them. Neobanks are increasing the number of channels for interacting with end customers through alternative data models, smart partnerships and digital technologies.

Source: PwC analysis

10 IBEF report MSME industry in India, 2021

Neobanks with digital cores are able to offer solutions to overcome these issues. They are tying up with traditional banks and offering a set of value-added services by bridging the data gap between banking, payments and accountancy, and making rapid inroads into the underserved MSME market.

MSMEs are using neobanking services for the following reasons:

- **Seamless onboarding:** Opening a neobank account is a less cumbersome process and MSMEs can open virtual accounts with less paperwork and within a short time period.
- **Intuitive customer platforms:** Neobanks are offering cleaner user interfaces and creating intuitive user experiences such as regional language support and integrations with accounting and expenses systems.
- **One-tap availability:** They are embedding into existing user processes by offering financial products at the point of consumption by using alternative data such as cash flow based credit and invoice insurance.
- **Transparency and data insights:** Neobanks are doing away with payment penalties, limited ATM withdrawals and account balance charges, and offering more transparent pricing to their business customers. Additionally, most neobanks are also providing dashboards and visualisation analysis which provide useful analytics on accounting, payments, receivables, etc., helping business owners keep track of payments/receivables outstanding, invoices pending, spends analysis and other relevant financial activities.
- **Consolidation of financial and non-financial services:** MSMEs are benefiting from the convergence of financial and non-financial services into a blended ecosystem. For example, several neobanks are providing MSMEs with digital tools that enable them to connect with customers and suppliers via digital platforms. These players are providing neobanks with an opportunity to embed financial services with non-financial services such as loans for purchase, pre-shipment loans and payment gateway facilities.

Case study #2

A four-year-old Bengaluru-based neobank, having powered more than one million MSMEs and start-ups, is focusing on providing them with tools across the four basic business verticals of banking, payments, accounting and compliance.

The neobank's strategic decisions are analysed below:

Products and process: It is consolidating all tools and functionalities that help businesses in taking care of these core pillars. It is using digital current account opening to acquire customers and then providing them with an integrated set of services like automated bookkeeping, reconciliation, GST filing and payments. It has also built a predictive dashboard that can be used by customers for the visibility of cash flows. This data helps the neobank in providing cash flow, lending and wealth management services to these businesses.

Partnerships: It also aims to integrate with packers and movers, travel agencies, legal services, financial services, office security services, printing and publishing, digital marketing, public relations and event management, etc. The platform also provides business growth tools, including a marketplace as well as a rich app store with various business essential services required for small businesses like insurance, accounting plug-in, among others.

02

Evolution of neobank-related regulations in Asia

Neobanking has witnessed increasing traction, and regulators across multiple markets have also implemented a number of regulations specifically designed for neobanks. This practice of regulating neobanks started with the developed markets, but a few Asian countries have also issued licensing regulations over time to bring neobanks under regulatory frameworks. In the recent past, regulators in developing Asian economies have started to explore ways of governing digital and neobanks. The Monetary Authority of Singapore (MAS), Financial Supervisory Commission Republic of China (FSC Taiwan), Bank Negara Malaysia (BNM), Bangko Sentral ng Pilipinas and Hong Kong Monetary Authority (HKMA) are the regulators who have issued digital banking frameworks and commenced granting digital banking licences. On the other hand, the Bank of Thailand (BoT) has inclined towards regulating the digital banking space while Bank Indonesia has issued the guidelines for digital banks just a few weeks ago. A few specific details on these developments for some of the Asian countries are outlined in the following page:

MAS

The MAS released guidelines for issuing a digital bank licence on 28 June 2019. It aims to enable non-bank players with strong value propositions and innovative digital business models to offer digital banking services. Digital full banks (DFBs) will provide a wide range of financial services and take deposits from retail customers, while digital wholesale banks (DWBs) will focus on serving SMEs and other non-retail segments.

It has awarded four new digital bank licences in December 2020 – two DFB and two DWBs.[11]

FSC Taiwan

FSC Taiwan issued internet-only bank guidelines on 26 April 2018.[12] The scope of business of these banks is the same as that of a conventional commercial bank in Taiwan.

As of February 2021, FSC Taiwan issued two internet-only bank licenses.[13]

HKMA

The HKMA issued revised virtual bank guidelines on 30 May 2018.

The scope of a virtual bank is to primarily deliver retail banking services through the internet or other forms of electronic channels instead of physical branches.

It has issued a total of eight virtual banking licences as of 31 December 2020.[14]

BNM

BNM issued a framework[15] on licensing digital banks on 31 December 2020, clearly charting out the eligibility criteria, application procedure, etc., for an applicant intending to carry on digital banking business or Islamic digital banking business.

As of June 2021, BNM has received 29 applications, out of which only five licenses are proposed to be granted.[16]

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11 https://www.mas.gov.sg/news/media-releases/2020/mas-announces-successful-applicants-of-licences-to-operate-new-digital-banks-in-singapore

12 https://www.fsc.gov.tw/en/home.jsp?id=473&parentpath=0%2C4

13 https://www.moodysanalytics.com/regulatory-news/feb-09-21-fsc-taiwan-grants-license-to-internet-only-banks-in-taiwan

14 https://www.hkma.gov.hk/eng/key-functions/banking/banking-regulatory-and-supervisory-regime/virtual-banks/

15 https://www.bnm.gov.my/documents/20124/938039/20201231_Licensing+Framework+for+Digital+Banks.pdf

16 https://www.bnm.gov.my/-/bnm-receives-29-applications-for-digital-bank-licenses

03

Indian neobanking regulatory landscape

The Indian banking sector is one of the most heavily regulated sectors in the country. Banks in India deploy considerable resources (time, manpower and money) to ensure compliance with applicable regulations. Indian banks have also adapted to the new realities of the digital era and adopted state-of-the-art technologies and systems to remain compliant with the constantly changing regulatory landscape.

Over the last decade, there has been an increase in the use of cutting-edge, tech-enabled solutions in the banking sector. These tech-enabled solutions have also given rise to neobanking business models in the country. These neobanks have brought superior technology to financial services and enriched customer experience while leveraging the regulatory infrastructure and core systems of existing banks.

Business models

In countries where neobanking business models are regulated (termed as either digital banks or neobanks), the governing regulations in such jurisdictions typically do not require such entities to establish physical branches. As a result, these neo/digital banks completely operate on a digital-based banking model with no physical presence. In contrast, the Indian FinTech ecosystem has witnessed two different types of business models for catering to the banking and financial services needs of the population through digital modes. The broad characteristics of these two models are described in the following page.

Description	Licensed banks: Fully digital banking unit requiring physical presence	Licensed bank + FinTech partnership model
Overview	These are existing Indian banks which facilitate complete digital banking services under their own brand name.	These are usually FinTech entities that tie up with multiple banks and other partners to provide a wide range of financial services.
Objective	They are typically established to compete with FinTechs and keep up with new-age technology in the financial services sector.	These FinTechs are naturally established with the goal of becoming a financial services regulated entity in the near future.
Authorisation	These entities are authorised by the RBI to undertake banking and financial services activities.	In India, banks/financial service providers are regulated entities who co-brand/partner with FinTechs (unregulated entities) to offer various regulated products to customers. Such co-branding/partnership is governed by regulations on business correspondents (BCs), outsourcing and digital payment security controls.
Products offerings	• Bank account • Remittance • Utility bill payments • Credit cards • Insurance • Investments • Loans	• Small and medium enterprise (SME) and individual banking • Insurance • Prepaid cards/wallets • Remittance • Utility bill payments • Investments • Loans • Value-added services — Expense management — Automated accounting and invoicing — Integrated payment gateway — White-label solutions

Regulatory framework

Currently, neobanks offer products that cut across all the three financial regulators, namely, the RBI, Securities Exchange Board of India (SEBI) and the Insurance and Regulatory Development Authority of India (IRDAI). While some of the product offerings require neobanks to seek a licence/approval from the concerned regulator, some others (primarily RBI governed) – for which the applicable regulatory regime is indirect – do not.

Furthermore, in the context of the applicability of regulations and requirements to seek licences from the RBI, the governing factor will be whether such neobanks partner with existing financial institutions (banks, non-banking financial companies, prepaid instruments (PPI) issuers, etc.) or directly become the issuers of products, take credit risks in their own books, etc.

Neobanks also offer investment advisory services to their customers (for investing in mutual funds, stocks, insurance policies, fixed deposits, etc.), and in such a case, depending on the exact role of the neobanking entity, licences/approvals from SEBI and the IRDAI may be required.

In areas where the regulatory framework does not apply to neobanks directly, the below mentioned outsourcing and business correspondent guidelines (issued by the respective regulators and listed below) typically apply to neobanks.

- RBI - Guidelines for engaging Business Correspondents (BCs) under Master Circular on Branch Authorisation dated 1 July 2014
- RBI - Framework for Outsourcing of Payment and Settlement-related Activities by Payment System Operators dated 3 August 2021
- RBI - Guidelines on Managing Risks and Code of Conduct in Outsourcing of Financial Services by Banks dated 11 March 2015
- RBI - Master Direction on Digital Payment Security Controls dated 18 February 2021
- RBI - Directions on Managing Risks and Code of Conduct in Outsourcing of Financial Services by NBFCs dated 9 November 2017
- SEBI - Guidelines on Outsourcing of Activities by Intermediaries dated 15 December 2011
- IRDAI - IRDAI (Outsourcing of activities by Indian Insurers) Regulations dated 20 April 2017

Thus, the implications of regulations flow down to neobanks contractually from their regulated partners. The legal agreements which are executed between neobanks and regulated entities are the key governing terms for providing a wide range of products and services. Such contracts are signed by neobanks with different regulated entities as appropriate to their business operations.

In the event that the regulatory framework becomes directly applicable to neobanks by virtue of offering products on its own books or the roles and responsibilities with respect to a particular product come within the ambit of the regulatory domain, the regulations from which authorisation requirements for such typically offered products derive are listed in the table below:

Products	Indicative regulations
— Banking services — Credit/loans — Domestic money transfers — Utility bill payments — Prepaid card services	Extant RBI regulations pertaining to licensing of banks RBI Master Directions on Prepaid Payment Instruments dated 27 August 2021 RBI Non-Deposit taking NBFC Master Directions (Systemically Important and Non-Systemically Important NBFCs) dated 1 September 2016 (updated as on 17 February 2020) Guidelines on Regulation of Payment Aggregators and Payment Gateways dated 17 March 2020
Investment advisory products — investment in stock markets — investment in mutual funds — investment in IPO — investment in gold	— SEBI (Investment Adviser) Regulations, 2020 (updated as on 3 August 2021) — AMFI Code of Conduct for distribution of mutual fund products
— Corporate agents — Insurance web aggregator — Insurance policy	— IRDAI (Registration of Corporate Agents) Regulations, 2015 — IRDAI (Insurance Web Aggregators) Regulations, 2017

RBI | SEBI | IRDAI

Neobanks, as a part of their arrangement with regulated entities (banks, NBFCs, payments companies, etc.), perform varied roles, including that of technology service providers, marketing and distribution agents and business correspondent. Neobanking services typically start with the opening of a savings or current account. Once customers are onboarded, they have integrated access to a range of other financial products and services which are offered through tie-ups with multiple regulated entities. The opening of a preliminary bank account (with the bank that the neobank has tied up with for this purpose) is generally mandatory for customers to gain access to the financial services provided by neobanks in India.

Some key operational processes of the neobanking business model are discussed below.

- **Customer onboarding process**

  Neobanks have their own strategies for acquiring customers, varying from running rewards campaigns to cashback/value point programmes. These offers, along with a superior online banking experience, attract customers.

  Neobanks act as the front-end customer interface, while most of the regulatory compliance is taken care of by the regulated entities. In the case of a conventional bank partnering with a FinTech, the customer acquisition aspect for the purpose of opening a bank account and availing banking services is usually executed by these FinTech entities. They assist the bank and other back-end regulated entities in complying with KYC/AML requirements. While the documentation part or operational KYC-related aspects are supported by these neobanks, the final decision to validate and approve/reject the KYC of any customer lies with the regulated entities. These critical KYC-related aspects are adequately covered in extant agreements between neobanks and the regulated entity.

  The neobank's obligation is limited to providing technology support for sharing of KYC documents with the regulated entity. Due to regulatory constraints, neobanks cannot and do not store the KYC documents of customers. Additionally, when customers opt for a particular product from a regulated entity, neobanks make extensive disclosures (through terms and conditions, agreements, etc.) to them regarding the regulated entity. The journey of a customer with a neobank is analysed in the figure below.

- **Implementation of grievance redressal mechanism and fair practice code**

  Given that neobanks interface with customers, they are required to put in place an appropriate and comprehensive customer grievance redressal mechanism. Even though the ownership of customers (who avail several financial products and services) is with the regulated entity – that is, the back-end partner of the neobank – the customer grievance process must be easily accessible on the neobank's website or mobile application platform. The grievance redressal process is required to clearly outline the procedure for lodging the complaints along with a detailed escalation matrix. Additionally, it should include contact details of the nodal officer of the regulated entity, so that in case a customer is not satisfied with the resolution provided by the neobank, they may reach out to the respective regulated entity for resolution.

  In addition to providing customers with standard options (telephone, emails, etc.) for lodging complaints, neobanks also leverage technology and use cost-efficient customer service chatbots that assist customers round the clock. These chatbots are seamless as they are tech-driven and capable of providing instant resolution to several queries and concerns.

  Apart from providing round-the-clock customer support through digital modes, neobanks are also required to follow fair practices while rendering financial services to their customers.

The financial services offered by neobanks cannot be combined with the sale of any product/services offered by them. Additionally, neobanks disclose the terms and conditions and service fees/charges applicable for availing products and services on their platforms to their customers. Though neobanks are not regulated entities, they are required to be extremely mindful of the regulatory regimes which are indirectly applicable to them via their partner regulated entity. In India, the RBI has also issued an Ombudsman Scheme for Digital Transactions in January 2019 (the Scheme) which requires payment system providers (PSPs) to redress customer complaints arising out of deficiency in services while undertaking digital transactions as defined under the scheme. The obligations arising out of this scheme may be encapsulated by the PSPs in their arrangements with the neobanks. These obligations needs to be factored in while assessing the direct and indirect regulations applicable to neobanks.

- **Data privacy and security**

  By virtue of the business model put in place by neobanks, they have access (either independently or through partnering financial institutions) to substantial customer data. It is important that such data is appropriately accessed, stored and shared by neobanks by following stringent data security standards. Even currently, neobanks adopt various technical standards – namely International Organization for Standardization (ISO), Payment Card Industry Data Security Standard (PCI-DSS), etc., as may be applicable – to safeguard customer data. This is in addition to the data standards that may be imposed by regulated entities on the same set of customer data.

  A recent speech by the RBI Deputy Governor M. Rajeshwar Rao delivered in the context of data protection suggested that large-scale adoption of open banking[17] frameworks should ideally be preceded by strong data protection and privacy laws.

  India has already embarked upon the same with the introduction of The Personal Data Protection Bill, 2019, in the Parliament. The bill seeks to protect individual personal data and establish a data protection authority for the same. Neobanks will have to take into account the provisions of this bill while accessing, storing and sharing customer data once it becomes a legislation.

17 https://m.rbi.org.in/scripts/BS_SpeechesView.aspx?Id=1107

04

Way forward

The Indian financial sector is primarily regulated by the RBI, SEBI and IRDAI. These regulators have introduced various initiatives and regulations for increased, consistent, seamless and safe accessibility to financial products through digital modes. The tremendous efforts put in by all the regulators to make regulations commensurate with the ever-changing technological developments and innovations in the financial ecosystem is laudable. For example, the Regulatory Sandbox initiative that all the regulators introduced in the recent years enables them to live test new products/services in a regulatory environment. Initiatives like Video KYC, establishment of the Reserve Bank Innovation Hub and introduction of the Account Aggregator framework are equally remarkable in the current context. If this dynamic approach of the regulators continues, the already burgeoning neobanking sector is expected to grow rapidly in the future.

As indicated above, in view of the current role played by neobanks, most of their product offerings are not directly regulated. However, being subjected to regulations indirectly (through their partnership with regulated entities) has ensured that their product offerings are in adherence to the regulatory norms. This, in turn, has helped these entities gain customer confidence and offer a host of financial products to the masses.

However, the sector is yet to mature and it is therefore critical that regulations evolve gradually in line with its advancement. In a few years from now, the neobanking space is expected to stabilise with new business models/ products, and Indian regulators, like their global counterparts, may look at directly regulating neobanks. However, Indian regulators could consider the following approaches for paving the way for digital banking set-ups:

Phase 1 – necessary to update existing regulations: Currently, unlike neobanks, the regulatory regime does not envisage a completely digital method of offering financial products. It is extremely critical that the current indirect regulations are relooked at in light of the digital offerings of neobanks and their relationship with financial entities. For example, the business correspondents (BCs) guidelines are quite dated and do not factor in the change in relationships between financial institutions and their BCs as well as the manner in which the latter can operate now. The concept of a BC has transformed from that of an entity offering financial products through purely physical channels to digital ones. Also, the scope of the product offerings by these BCs has expanded considerably. A regulatory framework that enables functions such as settlements and fund management to be undertaken by a regulated entity and technology interface and user experience to be undertaken by a FinTech partner needs to be considered.

Additionally, a similar change is required in the RBI's Branch Authorisation guidelines which currently define 'branch' only as full-fledged branches, specialised branches, satellite offices, mobile branch extension counters, off-site ATMs, administrative offices, controlling offices, service branches (back office or processing centre), etc. This definition currently does not take into account the digital set-up of neobanks. Furthermore, the mobile banking guidelines issued by the RBI enables banks only with a physical presence to offer mobile banking services to customers.

To ensure that neobanks have a regulatory framework that is free from ambiguity, the regulators need to revisit the relevant regulations and develop supporting regulations for the aspiring neobanking industry while ensuring customer protection measures.

Phase 2 – niche banking licence: Based on an assessment of the way in which the neobanking space is expected to evolve over the next few years, the RBI could carve out regulations that are niche to neobanks, similar to those created for small finance banks and payments banks in the past. Thus, a specific regime for the establishment of digital banks needs to be explored. The case for such a regime is made below:

- **Branches no longer the pivotal point for customer handling:** Existing regulations make the business branch the pivotal point for customer handling, comprising customer onboarding, servicing and grievance redressal. The RBI Master Circular on Customer Service in Banks dated 1 July 2015[18] makes this explicit. It has been suggested that digital banks adopt the notion of virtual branches, but the compliance requirements in the RBI's master circular are so stringent that this would require branch managers and supporting branch teams to be in place for the bank to remain compliant. If these represent humans, the cost savings that arise from a digital bank would be lost, and the business model would become unviable. Instead, if there are to be virtual branch managers and branch teams, it would become much simpler to centralise the automation of customer handling. Regulations would therefore need to protect customer interests differently from the manner presently specified, not relying on branches.
- **Implications of absence of branches for geographical dispersion:** As per the RBI circular on Rationalisation of Branch Authorisation Policy - Revision of Guidelines dated 18 May 2017,[19] geographical dispersion of customers is presently mandated by the RBI through branch locations, with six locational tiers. Tier-1 centres have a branch strength not exceeding that of centres in all other tiers put together, with a quarter of all branches being in unbanked locations and with incentives for expanding into underbanked locations. As a digital bank will have no business branches, geographical dispersion would instead need to be guided by fresh regulations based on depositor locations.

18 https://m.rbi.org.in/scripts/BS_ViewMasCirculardetails.aspx?id=9862

19 https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10972&Mode=0

05

Future trajectory of growth

Given their technological prowess and innovative business models, neobanks have the potential for further value addition and growth.

For instance, by working in tandem with the government, they can play a vital role in expanding the reach of financial services, operationalising measures undertaken to solve the challenges of financial inclusion and providing a bundled portfolio of necessary financial services. Services ranging from opening of bank accounts for immigrants, facilitated via innovative onboarding procedures, to providing instant credit facilities to MSMEs which are not based on traditional methods of underwriting could assist in realising the larger financial inclusion vision.

Key attributes and offerings such as accessibility, cost-effectiveness, access to financial and non-financial functionalities under one platform, and customer-centric approaches are some of the factors driving the success of neobanks globally.

Moreover, neobanks are building niche solutions focused on specific groups of customers, and this characteristic continues to make them vital in the larger financial services ecosystem.

Although neobanks are gaining momentum and have significant potential to disrupt the banking and financial services arena, their operational model is yet to show sustained profitability.

While neobanks are innovating with revenue streams, there is potential for regulatory support through the opening up of further lucrative financial services revenue streams through targeted regulations. Further, there is merit in neobanks taking a leaf out of the larger ecosystem platform strategy, which is to create even more comprehensive, common service platforms that aggregate multiple ecosystem partner service offerings for greater customer engagement, pool and utilise ecosystem partner strengths in customer onboarding, and give rise to further revenue stream opportunities. This is already apparent in the super-app trend that is being seen in multiple geographies.

Another revenue stream neobanks are exploring is offering banking as a service via APIs. Having already established their own technology and offerings, these players are abstracting these solutions for use by other players as building blocks and platforms. For example, a leading global technology player is offering digital banking APIs to players such as FinTechs, start-ups and corporates to build their own financial solutions in the form of embedded finance or neobanking applications.

With competition increasing among players in the financial services domain, including traditional banks, new-age FinTechs, technology firms and non-banking entrants, it is yet to be seen whether the market is deep enough for neobanks to grow sustainably and equitably. Addressing critical impediments such as regulation and compliance, data and cyber security, seamless API integration and expansion of products and services will play a fundamental role in determining their success.

About FCC

FCC is formed under Internet and Mobile Association of India (IAMAI) and represents the FinTech industry. The purpose of the council is to encourage collaboration, seek complementarities and build synergy between the FinTech ecosystem. The council has worked towards interpreting the regulatory and legal framework, aggregating the concerns and feedback of the various players and communicating it to lawmakers and organizing gatherings of the industry participants.

About FCC's Neobanking Committee

Out of the various sectors that FCC represents, Neo-Banking is one of them. The goal of this FCC's Neo Banking committee is to become one mature voice of the neo banking industry since it's at a nascent stage and evolving and also assist the regulator or government for any proposed regulations pertaining to the sector. The neo-banking committee represents players such as RazorpayX, Open Financial, NIYO, FPL Technologies, EpiFi Technologies, Jupiter, Instantpay India, etc.

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Contact us

IAMAI

Gaurav Chopra
Vice President
gaurav@iamai.in

Neha Bajaj
Assistant Vice President
neha@iamai.in

PwC

Vivek Belgavi
Partner, FinTech, and Alliances and Ecosystem Leader
PwC India
vivek.belgavi@pwc.com

Authors

Sanjana Agarwal
Tanvi Vakil
Avneesh Narang

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