Role of digital banking in furthering financial inclusion
Banking the unbanked

Several macroeconomic factors indicate that the basic ingredients for successful creation of a digital ecosystem are rapidly falling in place, far exceeding the supply side capabilities that support the Indian government’s agenda of financial inclusion. For instance, digital banking offers numerous advantages that work towards improving the same, largely lying on the fact that Indian consumers have shown tremendous preference for digital technologies, with growth rates for e-commerce as well as mobile phone adoption far outstripping rates in developed economies.

The Reserve Bank of India broadly defines financial inclusion as providing access to a ‘wide range of financial services at a reasonable cost’. This provision of access to banking services to nearly 47 per cent of the reportedly unbanked population in India has the potential to unfold huge growth opportunities for financial services players.

In this context, digital platforms are likely to deliver financial services to both the unbanked and the underbanked population, especially in rural/remote regions, at a low cost, and subsequently increase digital financial access to provide high quality, affordable financial services. By using digital channels, transaction costs could be lower than those incurred through traditional channels by as much as 90 per cent, thereby bringing down break even costs.

As banking becomes much less reliant on physical distribution, particularly as cash needs decline and video-based advice becomes more common; it is believed that the time has come for digital banking players to gear up the launch of digital products and services for their customers. This is expected to lead to future benefits from lower operating costs, along with increased business volumes, while also driving financial inclusion.

Banks should target previously underbanked and financially excluded segments with the help of technology; this could provide the necessary traction on new demand, as urban markets are crowded with a large number of players. It could also give banks an opportunity to spread the costs or investments in technology over a much larger base, and increase the utilisation of existing technology.

Further, government initiatives, regulatory support and active participation of public as well as private participants could be key levers for enabling a successful transition to a financially inclusive economy.

Why technology is likely to drive financial inclusion

India’s financial inclusion status is more likely to improve through technological interventions as:

- Brick and mortar businesses are proving to be an unfeasible proposition for banks in rural or remote areas
- There are distribution challenges due to localised constraints
- Conventional banking models are not feasible for low ticket size of transactions, deposits, loans, etc. in such regions
- Several accounts are no-frills in nature
- There is a lack of awareness of financial products
- There is a high requirement of skilled and trained manpower

Unbanked economies have tapped the potential of digital technology, particularly in the mobile space, to gauge the impact of technology-driven inclusion. In Kenya, nearly two-thirds of all adults are active customers of a mobile phone-based money transfer and payments service. While over 20 per cent of the population in Bangladesh uses mobile financial services, 50 per cent of mobile phone owners in Tanzania actively use mobile money systems.

In comparison, India, with its unbanked population of approximately 47 per cent and 900 million mobile subscriber base, sees only 1 to 1.5 per cent of mobile subscribers using mobile money actively. However, demand side drivers and the emerging digital ecosystem in the country still hold the key to promote financial inclusion, using digital channels.

Government initiatives for an inclusive growth

Financial inclusion is likely to remain high on the government’s agenda over the next decade. Over the last several years, many initiatives have been progressively launched for its propagation.

‘Digital India’

The ‘Digital India’ initiative, coupled with a payments infrastructure, is laying the cornerstone for a digital economy, keeping in mind the increasing willingness of people to use the internet, and the rising data traffic in the country. (Refer to graphs below)

The vision of the initiative, as outlined by the Government of India, focusses on the provision of infrastructure as a utility to every citizen, digital empowerment, services on demand and governance.

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02. Refers to unbanked population as on 2014; this unbanked population for 2015 might be lower post the rollout of Pradhan Mantri Jan Dhan Yojana that reportedly added around 16 crore more accounts (http://pmjdy.gov.in/account-statistics-country.aspx accessed 30 June 2015)

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The impact of ‘Digital India’ by 2019, as envisaged in the vision document published by GoI, has so far led to:  
- An investment of USD18.4 billion to provide last mile internet connectivity, better access to government services, and development of IT skills  
- Setting up of a pan India fibre-optic network by June 2016  
- Provision of Wi-Fi services in cities with a population of more than one million, as well as major tourist centres  
- Provision of broadband internet access to 250,000 village clusters by 2019 at a cost of about USD5.9 billion  
- Availability of ‘digital lockers’ to each citizen, allowing them to store all their original identification documents and records  
- Development of 100 smart cities in India, for which USD1.2 billion has been allocated  
- Universal phone connectivity  
- Setting up of 400,000 internet access points  
- Digital inclusion targeting job creation for nearly 1.7 crore people trained in IT, telecom and electronics  
- Creation of at least 8.5 crore indirect jobs related to IT  
- Focus on moving towards automation in delivery of government services  
- Achievement of a leadership position in IT towards betterment of health, education and banking services  
- Widened internet access and an enabled use of shareable private space on a public cloud model in order to empower citizens digitally.

**‘Aadhar’ card**

The technology-levered ‘Aadhar’ programme is likely to be the biggest disruptor in financial inclusion delivery, as innovations leveraging the ‘Aadhar’ card are expected to assist in broad-basing the access and acceptance by financially excluded segments.

An ‘Aadhar’ card provides a 12-digit individual identification number, issued by the Unique Identification Authority of India (UIDAI), to serve as a proof of identity and address. This card is based on biometrics technology. In addition, the ‘Aadhar’ Enabled Payment System (AEPS), an open platform which is a bank-led model, allows online interoperable financial inclusion transaction at points of sale (MicroATM) through the business correspondent of any bank using ‘Aadhar’ authentication.

Over 880 million ‘Aadhar’ cards have been issued as on 21 July 2015. The programme aims to achieve 100 per cent coverage by 2016. Following are some innovative initiatives based on demand side drivers that the ‘Aadhar’ programme is expected to propel:

**Direct benefits transfer (DBT)**

The scheme was initiated to facilitate disbursements of government entitlements such as those under the National Rural Employee Guarantee Act (NREGA), social security pension scheme, handicapped old age pension scheme, etc. of any central or state government bodies, using ‘Aadhar’ and authentication thereof, as supported by UIDAI.

**Retail banking**

The provision of these services is expected to encourage electronic retail payments and facilitate inter-operability across banks in a safe and secured manner.

**Creation of a commercially viable rural banking and financial inclusion model**

This is likely to provide a cost-effective model for dispensing last mile access by leveraging AEPS for biometric identification, using bank technology interfaces for smooth delivery of services.

**Analytics**

‘Aadhar’ data is likely to create a huge opportunity for leveraging analytics for customising services and offerings.

The ‘Pradhan Mantri Jan Dhan Yojana’ (PMJDY), ‘Pradhan Mantri Bima Yojana’ (PMBY), the launch of ‘Pradhan Mantri’ Micro Units Development and Refinance Agency Ltd (‘MUDRA Bank’) focussing on SME financing needs, launch of Differentiated Banking Licence (which also includes payments banks) as well as common service centres are other prominent initiatives that have generated a lot of interest from market participants and have delivered on several fronts. For instance, while 10.21 crore rural accounts and 6.71 crore urban accounts have been opened as on 21 July 2015 under PMJDY, there has been a roll-out of 1,33,847 common service centres (e-governance centres) in the country as on 31 March 2014.  

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2. Global Findex (Global Financial Inclusion Database) accessed 30 June 2015  
Digitisation trends and opportunities

Consumer behaviour is changing towards rapid adoption of digitisation
As the market has been exposed to innovative digital-based services that have been disruptive in nature (e-commerce players and e-governance services), it is now betting on changing client preferences to move from pricing (discounts) to convenience and service.

Demographic dividend is likely to create a large digital savvy customer segment
India’s demographic dividend is well suited to switch to digital behaviour, considering that the median age of an Indian is expected to be 29 years by 2020, with 900 million of the population falling in the age group of 16-60 years by 2025.

The unpenetrated or financially excluded, along with GoI initiatives, offer natural growth opportunities
Around 50 per cent of the unbanked population is being aggressively targeted to be brought under the banking umbrella. Progressing towards this goal, around 160 million accounts have been opened under PMJDY, while INR500 billion has been targeted to be transferred directly under DBT.

Increasing mobile penetration and smartphone usage
Mobile penetration of around 90 per cent is likely to drive financial literacy as well as inclusion, as players are betting on mobile-based financial services. An increased smartphone proliferation, projected at 50 per cent by 2020, and falling handset costs are likely to increase acceptance, better servicing as well as security.

Leveraging mobile phone and smartphone penetration
Mobile phones are likely to lead digital growth in India, considering the expected level of penetration. Innovations that use mobile penetration and payments banks to their advantage are likely to further financial inclusion.

Number of mobile internet users (in million)

Smartphone penetration (in per cent)

India’s mobile-banking opportunity

Mobile banking user forecasts (in per cent)


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The road ahead

Despite the huge potential and well-established promise of digital financial services to drive financial inclusion, multiple challenges remain in making these sustainable. Banks need to focus on developing compelling products that proliferate active customer adoption. As the unbanked pool reduces over the next few years, due to both physical as well as digital initiatives, the next wave of growth is expected to come by focussing on the underbanked.

Banks may also need to invest in creating user readiness on several counts to benefit from the growth of this segment for:

- Supporting platforms for e-KYC, based on ‘Aadhar’
- Supporting mobile platforms and analytics to understand customer segments and needs
- Innovating distribution models that go beyond the brick and mortar and manpower intensive operating models
- Making available customer service models like multi-lingual, voice based interaction, simplified service offerings

- Enhancing quality of service that is aligned to target customer ecosystem and needs
- Basing innovation needs on already existing technological initiatives that are scalable and capable of integration with emerging disruptive technologies and models such as Prepaid Instruments (PPI), Point of Sale (PoS), kiosks, mobiles, payment banks, etc.

There is a need for players to adopt a holistic approach on going digital and integrating business strategy with all constituents of their operating model ecosystem to create a remarkable customer experience. Given the constraints on capital and internal capabilities, players may need to make strategic choices around the digital model as well as the transition path they may need to take, in the short to medium term.

Following are some movements, owing to increased mobile penetration and use of mobile internet, that reflect the shift towards financial inclusion:

- Multiple models and partnerships have been forged between banks, telecom operators and technology players, e.g. the National Payments Corporation of India launched a national unified Unstructured Supplementary Service Data (USSD) code and gateway, which is device, operator and bank independent; a solution for the masses in India who have basic feature phones (Refer to the graph below to know the utility levels of mobile with respect to complexity)

- Mobile-based pre-paid instruments (wallets) is driving adoption of cashless transactions - remittances and commerce for the un/under banked.

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Source: KPMG in India analysis, 2015

Maturity of mobile usage

Source: KPMG in India analysis, 2015

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