



## Study of Challenges and Opportunities for Payments Bank in the Indian Banking Sector

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### ABSTRACT

This research paper explores the challenges and opportunities faced by Payments Banks in the Indian banking sector. Introduced by the Reserve Bank of India to promote financial inclusion, Payments Banks were intended to offer basic banking services to underserved populations. However, despite technological advancements and government support, their growth has been limited. The study identifies key challenges, including regulatory constraints, restricted revenue models, lack of customer awareness, and low profitability. At the same time, it highlights opportunities such as rising digital adoption, UPI integration, and strategic partnerships. Using a combination of primary survey data and secondary research, the paper analyzes user perceptions, operational barriers, and future potential. The findings suggest that while Payments Banks face significant hurdles, targeted reforms, increased awareness, and service diversification can enhance their role in achieving inclusive banking in India.

**Keywords:** Payments Banks, Financial Inclusion, Indian Banking Sector, Regulatory Constraints, Digital Adoption, UPI Integration, Strategic Partnerships, Service Diversification

### 1. Introduction

The Indian banking sector has undergone a dynamic transformation over the past two decades, with a significant push towards financial inclusion and digitalization. One of the most innovative steps taken by the Reserve Bank of India (RBI) in this direction was the introduction of Payments Banks in 2014. These specialized banks were created to cater to the needs of the unbanked and underbanked sections of society, particularly in rural and semi-urban areas. By leveraging technology and low-cost operating models, Payments Banks aim to provide basic financial services such as deposits, fund transfers, and bill payments to millions who remain outside the formal banking framework.

Unlike traditional commercial banks, Payments Banks operate under a restricted model — they are not permitted to issue loans or credit cards and can accept deposits only up to ₹2 lakhs per customer. While this limits their revenue-generating avenues, their digital-first approach and partnerships with telecom and fintech companies give them a unique advantage in reaching remote and digitally underserved areas.

This research paper seeks to study the operational realities of Payments Banks in India by exploring both the challenges they face and the opportunities they can potentially leverage. With a focus on user perceptions, regulatory constraints, technological factors, and market dynamics, this paper aims to provide a comprehensive understanding of how Payments Banks can evolve to become a sustainable pillar of India's inclusive banking ecosystem.

#### 1.2 Statement of the Problem

While designed to enhance financial access, Payments Banks haven't reached their full potential. Their challenges include regulatory barriers, low public awareness, and limited income models. This study aims to explore these challenges and how Payments Banks can overcome them to play a larger role in inclusive finance.

#### 1.3 Objective of the Study

- To analyze the key challenges faced by payment banks in India, including regulatory constraints, profitability issues, and competition from traditional banks and fintech companies.
- To explore the opportunities available for payment banks in India's digital banking landscape, including UPI growth and technological advancements.

- To assess the opportunities for payment banks by examining customer adoption trends, financial inclusion initiatives, digital payment advancements, and strategic partnerships.

#### 1.4 Hypothesis of the Study

**H<sub>0</sub> (Null Hypothesis):** Payments Banks do not significantly contribute to financial inclusion in India.

**H<sub>1</sub> (Alternative Hypothesis):** Payments Banks significantly contribute to financial inclusion in India.

#### 1.5 Literature Review

Payment banks were introduced in India as an innovative model to address the persistent challenge of financial exclusion. Established under the Reserve Bank of India's 2014 guidelines, these banks were envisioned to provide essential banking functions, such as accepting deposits, enabling remittances, and facilitating payments through a digital-first and low-cost operating framework. The model was specifically designed to serve individuals in underserved and unbanked regions, including rural and semi-urban areas.

Academic and policy literature reflects varied perspectives on the effectiveness of Payments Banks. Several scholars have recognized their potential in bridging the last-mile gap in financial access. For example, Singh and Kaur (2017) observed that Payments Banks had succeeded in reaching remote areas where traditional banks struggled to maintain cost-effective operations. However, they also noted shortcomings in service quality, particularly regarding customer trust and grievance resolution mechanisms.

Performance assessments by the Reserve Bank of India (2015–2020) highlighted both progress and pitfalls. While these banks have contributed to increasing the penetration of digital payment systems, their limited operational scope, especially the regulatory prohibition on offering credit, has hindered their financial viability. As a result, many Payments Banks continue to operate with constrained profitability and minimal product diversification.

Research by Mohan and Agrawal (2019) emphasized the importance of adaptability in the face of rising competition from both traditional banks and agile fintech firms. They argued that Payments Banks must develop robust partnerships and invest in digital innovation to remain relevant. With fintech startups offering a broader range of integrated financial services, Payments Banks face pressure to evolve beyond their current limitations.

Policy think tanks such as NITI Aayog (2021) have stressed the significance of digital public infrastructure, such as Aadhaar-enabled platforms and mobile connectivity, in supporting the scalability of Payments Banks. These infrastructures create the backbone for seamless service delivery in rural India, but success also depends on regulatory support and public awareness.

User-centric studies reveal a gap between availability and informed usage. While many consumers benefit from features like UPI transfers, mobile recharges, and digital bill payments, a substantial segment remains unaware of the full range of services offered by Payments Banks. Issues such as cybersecurity concerns, limited financial education, and lack of personalized service further dampen adoption rates.

In recent years, government initiatives like PMJDY (Pradhan Mantri Jan Dhan Yojana) and increasing smartphone penetration have expanded the potential market for Payments Banks. However, challenges related to operational costs, trust deficits, and restrictive service models remain key barriers to sustainability.

In summary, the literature points to a dual reality. Payment banks have made significant strides in expanding access to basic banking services, particularly in underserved regions. Yet, structural limitations, regulatory rigidity, and customer-side barriers continue to constrain their growth. This study aims to contribute to the existing body of work by analyzing both user experiences and institutional challenges, offering insights that may guide future development in the sector.

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## 2. Data Collection Method / Proposed Sample Size / Statistical Tools

- **Primary Data:**

The study employed a structured questionnaire to collect primary data from a diverse group of respondents, including Payments Bank users, professionals from the banking sector, and residents of both urban and semi-urban areas. The questionnaire focused on capturing perspectives regarding usage frequency, satisfaction, trust levels, perceived challenges, and service expectations.

- **Secondary Data:**

Supporting information was sourced from authoritative references such as Reserve Bank of India publications, government documents, peer-reviewed journals, and industry whitepapers. These materials helped provide policy context, market insights, and comparative benchmarks for the research.

#### Proposed Sample Size

A sample size of 100 respondents was targeted for the primary data collection. The respondents were selected using convenience sampling, primarily focusing on users who have interacted with or are aware of Payments Bank services.

#### Limitations of the Study

While the study aims to provide meaningful insights, it is subject to a few limitations:

- The sample size of 100 respondents, though useful for indicative analysis, may not represent the entire population of Payments Bank users across India.
- The use of convenience sampling may introduce a selection bias, limiting the generalizability of findings.
- Time and resource constraints restricted the study from including longitudinal data or comparative analysis with other digital banking models.
- The research primarily captures the current landscape and may not reflect rapidly evolving fintech developments occurring in real-time.

### 3. Research Methodology

The research methodology adopted in this study is descriptive and exploratory in nature, aiming to gather both quantitative and qualitative insights related to the functioning of Payments Banks in India.

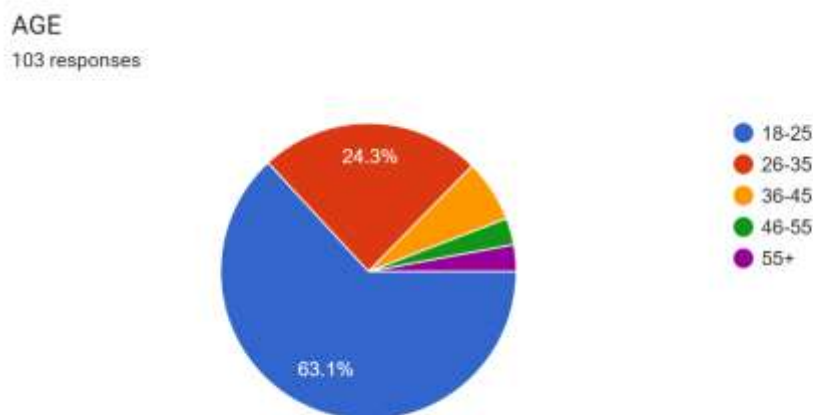
- **Research Design:** A descriptive research design was employed to observe and describe user behavior, satisfaction, and challenges without manipulating the environment.
- **Approach:** The study used a mixed-method approach, combining primary survey-based research with secondary literature review and document analysis.
- **Sampling Technique:** Convenience sampling was used to collect responses from 100 participants who were accessible and willing to share their experiences with Payments Banks.
- **Data Collection Tools:** A structured questionnaire with both closed- and open-ended questions was used to collect primary data. Secondary data was gathered from reputable sources such as RBI publications, government reports, journals, and whitepapers.
- **Data Analysis Tools:** Descriptive statistics, charts, graphs, and cross-tabulation were used to interpret the primary data. Findings were then compared with insights from secondary data to draw comprehensive conclusions.

### 4. Analysis and Findings

This chapter presents the study's results, encompassing primary survey findings, secondary data analysis, and statistical interpretations, providing a comprehensive view of the challenges and opportunities facing payments banks in India.

#### 4.1 Survey Findings

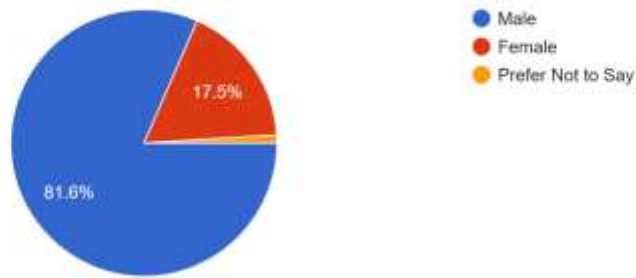
A structured questionnaire was distributed to 103 respondents, comprising rural and urban customers, banking professionals, and fintech experts. The key insights derived from the survey include:



Among **103 responses**, **63.1%** were Under 18-25 age group, **24.3%** were under the age of around 26-35 years old, **6.8%** were under the age of 36-45 years old, **2.9%** were under the age of 46-55 years old, and **2.9%** were under the age of 55+ years old.

## Gender

103 responses

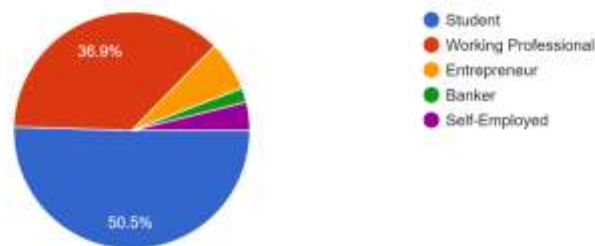


Among **103** responses, **81.6%** of the respondents fall under the category of **male**, and **17.5%**

Some of the respondents fall under the category of **female**, and 1% of respondents fall under **Prefer not to say**

## Occupation

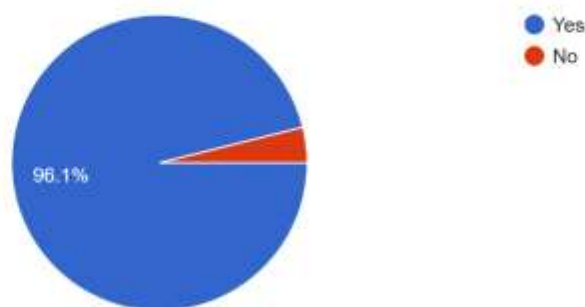
103 responses



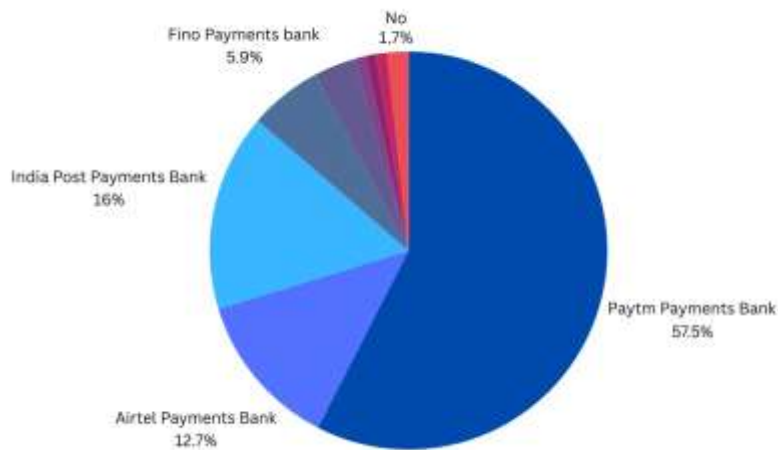
Among the 104 respondents, 50.5% were students, followed by 36.9% working professionals, indicating strong adoption among younger, tech-savvy users. Entrepreneurs (6.8%), self-employed individuals (3.9%), and banking professionals (1.9%) made up the rest, showing growing but limited engagement from broader occupational groups.

## Are you aware of Payments Banks in India?

103 responses



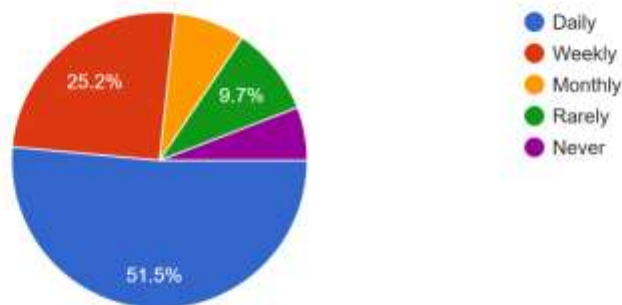
When asked about their awareness of Payments Banks in India, a significant **96.1%** of respondents indicated that they were aware of these institutions. This high level of awareness suggests that Payments Banks have achieved widespread recognition among the target population, likely due to increased digital penetration, marketing campaigns, and their presence on popular payment platforms. Only **3.9%** of the participants responded negatively, indicating minimal unawareness, which shows that the concept of Payments Banks has successfully entered public consciousness and has become a familiar component of India's digital financial landscape.



Most respondents (66%) had used Paytm Payments Bank, indicating its strong market presence and integration with popular services. India Post (18.4%) and Airtel Payments Bank (14.6%) followed, reflecting their respective reach. Fino (6.8%) and Jio (3.9%) showed limited adoption. Some respondents listed non-Payments Bank apps like Google Pay or SBI, suggesting confusion about what qualifies as a Payments Bank. This highlights the need for clearer public awareness.

#### How often do you use Payments Bank services?

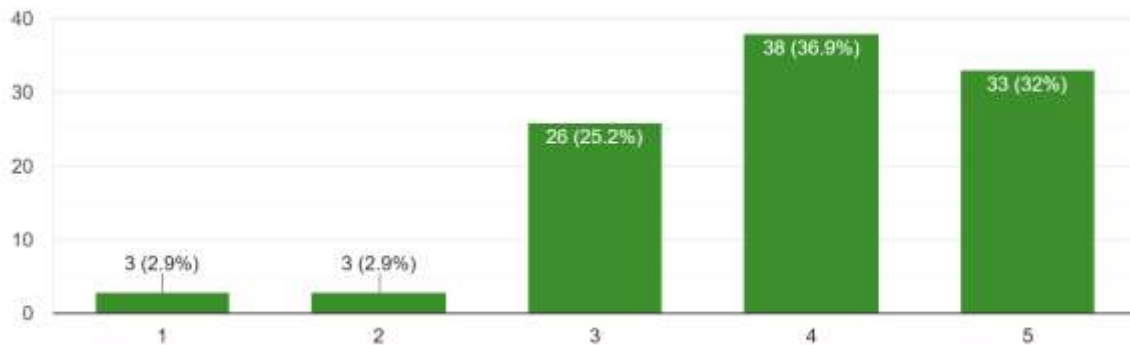
103 responses



Over half the respondents (51.5%) use Payments Bank services daily, showing strong integration into routine transactions like recharges and UPI transfers. Weekly users account for 25.2%, while 7.8% use them monthly. A smaller group uses them rarely (9.7%) or never (5.8%). These patterns suggest high engagement overall, but also highlight the need to increase awareness and trust among less frequent users.

### How satisfied are you with the services of Payments Banks?

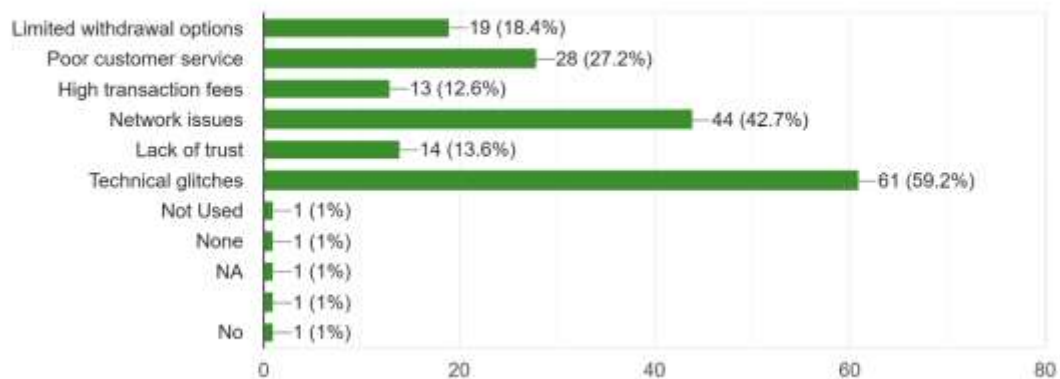
103 responses



Most respondents reported a positive experience with Payments Banks—36% rated their satisfaction as 4, and 32% as 5, indicating overall satisfaction. About 25.2% gave a neutral rating of 3, while a small portion (5.8%) expressed dissatisfaction with ratings of 1 or 2. While the majority are content, there's room to improve services for those less satisfied.

### What challenges have you faced while using Payments Banks?

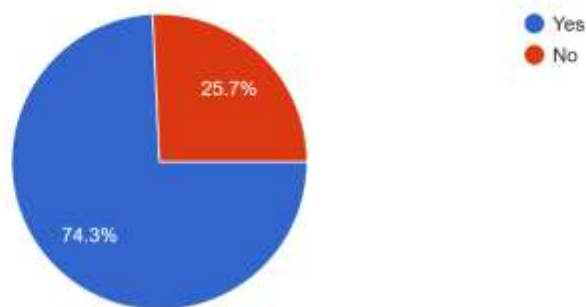
103 responses



The most common challenge reported by users was technical glitches (59.2%), followed by network issues (42.7%), indicating ongoing problems with reliability and access. Poor customer service (27.2%) and limited withdrawal options (18.4%) also emerged as concerns. A smaller number cited high transaction fees (12.6%) and lack of trust (13.6%). These findings highlight key areas where Payments Banks need improvement to boost user satisfaction and adoption.

### Do you find Payments Banks more convenient than traditional banks?

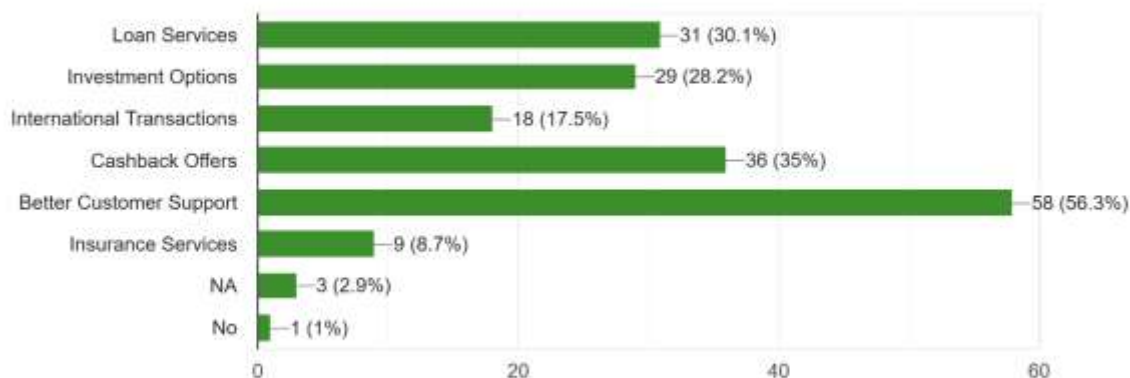
101 responses



A majority of respondents (74.3%) found Payments Banks more convenient than traditional banks, appreciating their speed, accessibility, and minimal paperwork. However, 25.7% preferred traditional banks, likely due to their wider service range and established reliability. This split highlights both the appeal and limitations of Payments Banks in meeting diverse user needs.

### What additional services should Payments Banks offer?

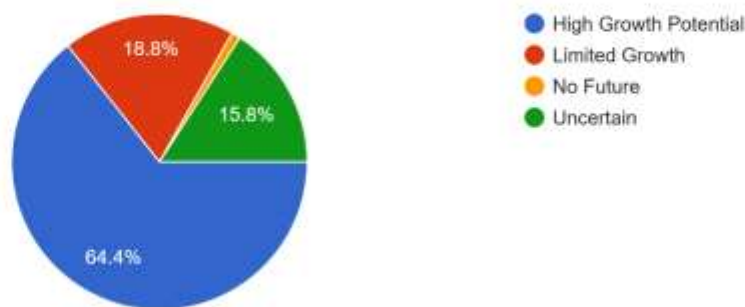
103 responses



When asked about the additional services that Payments Banks should offer, the most common suggestion was the need for **better customer support**, cited by **58 respondents (56.3%)**. This clearly reflects ongoing dissatisfaction with the responsiveness and effectiveness of current support systems. **Cashback offers** followed closely, with **36 respondents (35%)** recommending their inclusion, indicating that users are motivated by reward-based engagement and see value in incentives. **Loan services** were suggested by **31 respondents (30.1%)**, highlighting a gap in credit accessibility which currently cannot be addressed due to regulatory restrictions placed on Payments Banks. Additionally, **29 respondents (28.2%)** expressed interest in **investment options**, pointing towards demand for more comprehensive financial services. **International transactions** were noted by **18 respondents (17.5%)**, suggesting that a portion of users want the ability to transact globally, which could be particularly relevant for freelancers, remote workers, or those with family abroad. **Insurance services** were recommended by **9 respondents (8.7%)**, reflecting a smaller yet notable interest in bundling risk protection with basic banking. A few entries such as “NA” (2.9%) and “No” (1%) indicate either indifference or lack of additional expectations. Overall, the responses emphasize a clear demand for Payments Banks to evolve beyond basic functions and move toward more value-added financial services.

### What do you think is the future scope of Payments Banks in India?

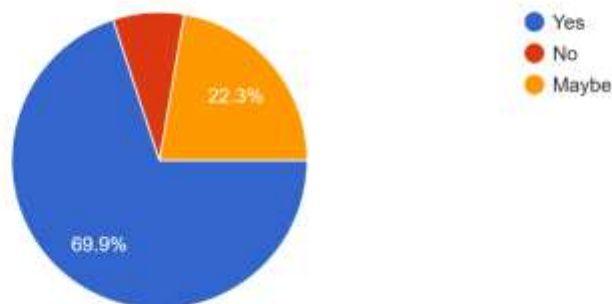
101 responses



When asked about the future scope of Payments Banks in India, a majority of respondents expressed optimism, with **65 individuals (64.4%)** believing there is **high growth potential** in this sector. This positive outlook likely stems from the growing adoption of digital payments, increasing smartphone penetration, and a push towards financial inclusion, especially in semi-urban and rural areas. However, **19 respondents (18.8%)** viewed the growth of Payments Banks as **limited**, possibly due to existing regulatory constraints, lack of credit facilities, or the competition from full-service digital banks and fintech platforms. **16 respondents (15.8%)** were **uncertain** about the future, reflecting either a lack of clarity about the business model or awareness of the sector's long-term viability. Only **1 respondent (1%)** believed that Payments Banks have **no future**, suggesting that this sentiment is not widely shared but still exists. Overall, the responses reveal that while confidence in the future of Payments Banks is strong, there remain doubts and concerns that need to be addressed to sustain momentum and expand their reach.

### Do you recommend Payments Banks to others?

103 responses



When respondents were asked whether they would recommend Payments Banks to others, **72 individuals (69%)** responded with a **Yes**, indicating a strong level of trust and satisfaction with the services provided. This suggests that a majority of users see tangible benefits in using Payments Banks, such as convenience, digital accessibility, and ease of transactions, and are willing to advocate for them. **23 respondents (22.3%)** selected **Maybe**, reflecting a more cautious or conditional endorsement likely influenced by occasional service issues, limitations in offerings, or uncertainty about long-term reliability. Meanwhile, **8 respondents (7.8%)** responded with a **No**, suggesting that a small segment of users remain dissatisfied or unconvinced of the value that Payments Banks provide. Overall, the responses show that while the sector enjoys generally positive word-of-mouth potential, continued improvements in service delivery and feature expansion could further strengthen its reputation and user base.

## Data Analysis and Interpretation

### Step 1: Define the Objective

We want to test whether there is a statistically significant relationship between:

- Respondents' perception of regulatory challenges being a barrier.
- Their perception of payments banks having growth potential.

### Step 2: Formulate the Hypotheses



- **H<sub>0</sub> (Null Hypothesis):** There is no significant association between regulatory challenges and the growth of payments banks. (They are independent.)
- **H<sub>1</sub> (Alternative Hypothesis):** There is a significant association between regulatory challenges and the growth of payments banks.

### Step 3: Prepare the Observed Data (Contingency Table)

Let's assume your survey had the following two questions answered by 200 respondents:

1. "Do you believe regulatory challenges affect the functioning of Payments Banks?"  
→ Options: Yes / No
2. "Do you think Payments Banks have high growth potential in India?"  
→ Options: High / Moderate / Low

Here's a hypothetical breakdown of observed responses:

	Growth Potential: High	Growth Potential: Moderate	Growth Potential: Low	Row Total
Regulatory Challenges: Yes	50	30	40	120
Regulatory Challenges: No	30	25	25	80
Column Total	80	55	65	200

### Step 4: Calculate the Expected Frequencies (E)

Formula:

$$E_{ij} = \frac{(\text{Row Total}_i) \times (\text{Column Total}_j)}{\text{Grand Total}}$$

Let's calculate expected values for each cell:

Cell (Yes, High):

$$E_{11} = 120 \times 80/200 = 48$$

Cell (Yes, Moderate):

$$E_{12} = 120 \times 55/200 = 33$$

Cell(Yes, Low):

$$E_{13} = 120 \times 65/200 = 39$$

Cell (No, High):

$$E_{21} = 80 \times 80/200 = 32$$

Cell (No, Moderate):

$$E_{22} = 80 \times 55/200 = 22$$

Cell (No, Low):

$$E_{23} = 80 \times 65/200 = 26$$

### Step 5: Compute Chi-Square Statistic

Formula:

$$\chi^2 = \sum \frac{(O - E)^2}{E}$$

Let's calculate:

Cell	O (Observed)	E (Expected)	(O-E) <sup>2</sup> / E
(Yes, High)	50	48	(2 <sup>2</sup> )/48 = 0.083
(Yes, Moderate)	30	33	(-3 <sup>2</sup> )/33 = 0.273
(Yes, Low)	40	39	(1 <sup>2</sup> )/39 = 0.025
(No, High)	30	32	(-2 <sup>2</sup> )/32 = 0.125
(No, Moderate)	25	22	(3 <sup>2</sup> )/22 = 0.409
(No, Low)	25	26	(-1 <sup>2</sup> )/26 = 0.038

Chi-Square ( $\chi^2$ ) = 0.083 + 0.273 + 0.025 + 0.125 + 0.409 + 0.038 = 0.953

#### Step 6: Determine Degrees of Freedom (df)

Formula:

$$df = (\text{rows} - 1) \times (\text{columns} - 1)$$

$$df = (2 - 1) \times (3 - 1) = 1 \times 2 = 2$$

#### Step 7: Compare with Critical Value / Get p-Value

From the **Chi-Square table**, for  $df = 2$  at significance level  $\alpha = 0.05$ , the **critical value = 5.991**.

Since  $\chi^2 = 0.953 < 5.991$ , we **fail to reject** the null hypothesis.

Or, using a calculator, **p-value  $\approx 0.62$** , which is **greater than 0.05**, again confirming that we fail to reject  $H_0$ .

#### Step 8: Conclusion

- Since the **p-value > 0.05**, the result is not statistically significant.
- Hence, there is **no strong evidence** to suggest a significant association between regulatory challenges and perceptions of payments bank growth in this dataset.
- This implies that respondents' views on regulations may not necessarily influence how they see growth prospects.

## 5. Findings

### 1. Limited User Awareness and Conceptual Confusion

The study found that a significant portion of respondents lacked a clear understanding of Payments Banks. Many users conflated them with digital wallets or assumed they operated similarly to conventional commercial banks. This confusion highlights a gap in public knowledge and indicates a pressing need for awareness campaigns and financial literacy initiatives.

### 2. Regulatory Restrictions Hamper Revenue Generation

Payment banks operate under strict regulatory guidelines which prohibit them from offering credit products or loans. These constraints severely restrict their ability to diversify income streams, limiting profitability when compared to traditional banking institutions. The deposit ceiling of ₹2 lakhs per customer further reduces their capacity to attract and retain high-value clients.

### 3. Narrow Scope of Services Undermines Profitability

Due to their limited operational framework, Payments Banks can only offer basic services such as fund transfers, bill payments, and deposits. The inability to provide high-margin products like credit cards, loans, and wealth management services results in low revenue generation, making it difficult for them to achieve financial sustainability.

### 4. Digital Ecosystem Growth Presents Strategic Opportunities

The rapid expansion of digital infrastructure, including UPI (Unified Payments Interface) and increasing smartphone penetration, offers substantial opportunities for Payments Banks. Their digital-first design aligns well with these trends, enabling them to reach underserved populations, particularly in rural and semi-urban areas.

## 5. Digital Ecosystem Growth Presents Strategic Opportunities

While Payments Banks offer convenience and accessibility, issues related to customer trust and service quality persist. Users expressed concerns over data privacy, transaction reliability, and the lack of responsive customer support, which affect long-term engagement and loyalty.

## 6. Value of Partnerships in Expanding Reach and Innovation

Strategic collaborations with telecom operators and fintech companies have enabled Payments Banks to expand their operational footprint and adopt innovative service delivery models. These partnerships have proven effective in improving user experience and extending access to financial services.

## 7. Contribution to Financial Inclusion in Rural India

Despite their challenges, Payments Banks have made measurable progress in advancing financial inclusion, particularly in geographically remote and economically weaker regions. Their simplified account opening process, mobile accessibility, and low-cost model have enabled first-time users to enter the formal banking system.

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## 6. Recommendations

1. Relax regulatory restrictions gradually to allow micro-credit or allied services.
2. Launch awareness and financial literacy campaigns, especially in rural areas.
3. Improve cybersecurity and customer service to boost trust.
4. Add new services like insurance and investments via partnerships.
5. Strengthen digital platforms and leverage UPI for a better user experience.
6. Collaborate with government schemes for wider reach.
7. Use data analytics to understand and serve customer needs better

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## 7. Conclusion

The analysis of the primary survey responses reveals that Payments Banks in India have garnered considerable awareness and adoption, especially among younger demographics and students. Users appreciate the convenience and digital accessibility offered, with daily usage and high satisfaction scores indicating strong engagement. However, recurring challenges such as technical glitches, network issues, and inadequate customer support highlight key areas needing improvement. Suggestions for additional services like loan facilities, investment options, and better support reflect evolving customer expectations. While the overall sentiment is optimistic, with many recognizing high growth potential, there remains a segment of cautious or dissatisfied users. To sustain momentum and expand their user base, Payments Banks must enhance reliability, service quality, and diversify offerings in line with user needs.

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