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Neo Banks in India: A Study of Services, Challenges, Opportunities, and Regulation

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ABSTRACT

Neo banks, or digital-only banks, are transforming the financial landscape by offering a seamless, user-friendly alternative to traditional banking. This study explores the rise of neo banks in India, examining their services, target demographics, regulatory framework, and growth challenges. Using a descriptive research design, it highlights customer preferences, operational models, and the fintech ecosystem that supports these banks. The analysis also identifies key barriers such as cyber security risks and regulatory limitations while uncovering opportunities in financial inclusion and digital innovation. The findings provide a detailed overview of how neo banks are reshaping financial access and convenience for digitally active users in India.

Keywords: Neo banks, Digital banking, Fintech, Financial inclusion

Introduction

The global banking sector is witnessing a rapid shift from conventional branch-based banking to technology-enabled financial solutions. At the forefront of this transformation are neo banks, also known as digital-only or challenger banks. These institutions leverage digital platforms to offer comprehensive financial services without maintaining a physical presence. In light of changing customer preferences and technological advancements, this study sets out to analyze why neo banks are gaining traction, the demographics they serve, and the hurdles and prospects they face in today's competitive financial environment.

Functions of Neo Banks

Neo banks in India perform a range of innovative, tech-driven functions aimed at improving the customer banking experience. These include:

- **Technology-Driven Services:** The core function of neo banks is to offer fully digital banking solutions via intuitive mobile and web platforms.
- **Customer Engagement and App Management:** Neo banks focus on client satisfaction, seamless product delivery, and user-friendly app interfaces for efficient banking experiences.
- **Partnership with Traditional Banks:** They collaborate with conventional banks to offer cutting-edge banking features, leveraging secure backend systems and regulatory support.
- **Data-Driven Personalization:** By collecting and analyzing user data, neo banks tailor financial services to better match consumer behavior and needs.
- **Lending and Financial Inclusion:** Neo banks often provide no-fee accounts and small loans, particularly targeting students and first-time earners aiming to build credit.
- **Quick and Easy Account Setup:** Opening an account typically takes just 3 to 10 minutes, involving a simple digital form and a brief video-based KYC process.
- **Global and Crypto Services:** Many neo banks offer free international debit card usage with live forex rates, and some even allow users to open cryptocurrency wallets.
- **Expense Management Tools:** Users can monitor monthly spending and budget more effectively using built-in expense tracking features.

- **Instant Debit Card Control:** Customers receive a free debit card which can be instantly managed, blocked, or updated directly through the app.

These functions make neo banks highly attractive to digitally inclined customers who seek convenience, speed, and financial control.

Operating Procedure of Neo Banks in India

Neobanks in India operate through a digital-first model, providing banking services entirely via mobile apps and web platforms without any physical branches. These fintech-driven entities do not possess their own banking licenses; instead, they collaborate with licensed traditional banks to deliver services such as savings accounts, fund transfers, debit cards, and financial planning tools.

The customer onboarding process is fully digital, typically involving a quick e-KYC process using Aadhaar and PAN. Once registered, users can seamlessly manage their finances with real-time updates, spend analytics, and personalized recommendations powered by AI and data analytics.

Since the Reserve Bank of India (RBI) does not currently permit full-stack digital banks, neobanks function under the regulatory framework of their partner banks, ensuring customer funds are secure and operations remain compliant. This model allows neobanks to offer a streamlined, tech-savvy experience targeted at digitally literate individuals and small businesses seeking convenience, transparency, and control over their finances.

List of Prominent Neo Banks in India

Below is a list of some leading neo banks in India along with their year of launch, key functions, operating revenue and overall progress:

Table 1: leading neo banks in India

Neo Bank	Year of Launch	Key Functions	Operating Revenue (FY 2023)	Progress & Highlights
Niyo	2015	Forex cards, digital savings, expense tracking	₹45 crore	Expanded overseas partnerships, over 4 million users
Open	2017	Business banking, invoicing, payments, bookkeeping	₹90 crore	Serves 2.3 million SMEs, RBI licensed NBFC partner
RazorpayX	2019	Business current accounts, payouts, payroll management	₹170 crore	Part of Razorpay suite, rapid growth among startups
Jupiter	2019	Personal banking, smart budgeting, UPI, mutual funds	₹50 crore	Targeting salaried youth, 2 million+ downloads
Fi Money	2021	Salary accounts, smart financial insights, investments	₹22 crore	Focused on young professionals, app-based ecosystem
Zolve	2020	Banking for students/professionals going abroad	Not disclosed	Operating in US-India corridor, growing cross-border

Sources: Razorpay financials report.

These neo banks are helping reshape digital finance in India by offering specialized services for individuals and businesses, focusing on convenience, speed, and low cost. They continue to grow in partnership with licensed banks and fintech enablers, aiming to reach both urban and semi-urban markets effectively.

Literature Review

Research on neo banks highlights their disruptive role in the banking industry. According to Deloitte (2020), neo banks focus on customer-centric models by leveraging technology to deliver faster and more efficient services. A study by PwC (2021) found that Millennials and Gen Z are more inclined toward digital banking due to mobile accessibility and real-time service features. Kapoor and Goyal (2022) observed that trust and data privacy remain significant barriers for wider adoption of neo banks in India. Furthermore, Sharma (2023) pointed out the role of neo banks in financial inclusion, especially among underserved populations.

Objectives of the Study

1. To examine the key services and digital functionalities that differentiates neo banks from traditional banks.
2. To assess customer preferences, usage patterns, and satisfaction levels with neo bank platforms across demographic segments.
3. To identify the major operational challenges and regulatory constraints impacting the growth of neo banks in India.

Research Methodology

This study adopts a descriptive research design to explore the preferences, challenges, and opportunities associated with neo banks. Primary data was collected through an online structured questionnaire distributed among 250 respondents across urban, semi-urban, and rural areas in India. The sampling method used was purposive sampling, targeting digitally active individuals aged 18 and above.

Secondary data was sourced from industry reports, academic journals, and official publications such as RBI guidelines, Deloitte and PwC reports, and fintech market research databases. Quantitative data was analyzed using basic statistical tools including percentages and frequency distributions to identify patterns in service usage and demographic variations.

The scope of the study is limited to Indian users of neo banking platforms, and responses were gathered over a two-month period in 2025. Ethical considerations, including informed consent and data privacy, were maintained throughout the research process.

Key differences between Neobank and Traditional Bank

Category	Neobank Characteristics	Traditional Bank Characteristics
Physical Presence	Online-only, no physical branches	Physical branches and ATMs
Fees/Rates	Lower or no fees for basic services; higher interest rates on deposits	Fees for services like account maintenance; lower interest rates on deposits
Product/Service Range	Basic banking (Checking, Savings, Payments, Microloans, Secured Credit Cards); agile in niche offerings	Comprehensive (Loans, Mortgages, Investments, Business Accounts, Wealth Management); wider range of complex products
Customer Service Model	Virtual support only (chat, email, phone); AI-driven chatbots for 24/7 service	In-person, phone, and online support; caters to preference for face-to-face interaction
Technological Innovation	Mobile-first, rapid innovation (AI, biometrics, real-time updates, PFM tools); user-friendly interfaces	Slower to adopt new technologies due to legacy systems; increasingly investing in AI for efficiency and customer service
Deposit Insurance	Partner-insured (rely on FDIC-insured partner banks)	Directly FDIC-insured

Regulatory Considerations for Neo Banks in India

Neo banks in India operate under a hybrid regulatory environment, as the Reserve Bank of India (RBI) does not yet issue full banking licenses to digital-only entities. Instead, these fintech players partner with licensed traditional banks or NBFCs (Non-Banking Financial Companies) to offer financial services. This partnership model ensures that the neo bank's activities remain compliant under the regulatory umbrella of their partner institutions.

Key regulatory considerations include:

- **No Independent License:** Neo banks are not recognized as standalone licensed banks in India. They must operate in collaboration with existing licensed financial institutions.
- **RBI Oversight Through Partner Banks:** All banking operations are subject to RBI norms through the licensed bank, which is ultimately responsible for customer deposits and compliance.
- **KYC and AML Regulations:** Neo banks must adhere to strict Know Your Customer (KYC) and Anti-Money Laundering (AML) standards. Most conduct e-KYC using Aadhaar and PAN integration.
- **Data Security and Privacy:** Neo banks must comply with the Information Technology Act and RBI's guidelines on digital payments, cybersecurity, and data protection.

- **Third-Party Risk Management:** Since many operations are tech-driven or outsourced, RBI expects robust third-party vendor risk frameworks from partner institutions.

As the digital finance space grows, policymakers are closely monitoring neo banks. There is ongoing discussion about developing a regulatory framework that specifically recognizes and governs neo banks as distinct entities. Until such a framework is formalized, neo banks will continue operating as extensions of traditional banks, blending innovation with compliance.

Data analysis

Table2 . Services Preferred by Neo Bank Users

Service Category	Percentage of Users (%)
Digital payments	85%
Instant fund transfers	78%
Expense tracking tools	65%
Automated savings	60%
Customer support chat	55%

The table presents the preferences of neo bank users regarding various digital services. A significant 85% of users favor digital payments, making it the most popular service. Instant fund transfers follow closely with 78%, reflecting demand for speed and convenience. Expense tracking tools are used by 65%, while 60% rely on automated savings. Additionally, 55% of users appreciate customer support chat, emphasizing the importance of responsive and efficient assistance in digital banking.

Table 3.Usage Patterns Across Demographics

Demographic Group	Neo Bank Usage (%)
Age 18-25 (Gen Z)	72%
Age 26-40 (Millennials)	68%
Age 41-60 (Middle-aged)	35%
Age 60+ (Seniors)	15%
Urban Residents	70%
Semi-urban	45%
Rural	20%

The table illustrates neo bank usage across different demographic groups. Gen Z (18–25) shows the highest adoption at 72%, followed by Millennials (26–40) at 68%, indicating strong digital affinity among younger users. Middle-aged individuals (41–60) show moderate usage at 35%, while seniors (60+) lag behind at 15%. Usage is also location-dependent, with 70% of urban residents using neo banks, compared to 45% in semi-urban and 20% in rural areas.

Challenges Faced by Neo Banks

Neo banks face several critical challenges despite their digital-first appeal:

- **Limited Regulatory Autonomy:** Many neo banks are not fully licensed and instead operate through partnerships with traditional banks. This restricts their freedom to offer independent financial products and limits innovation.
- **Cybersecurity Risks:** Operating entirely online makes neo banks vulnerable to cyber threats such as data breaches, identity theft, and hacking, requiring significant investment in digital security.

- **Lack of Physical Infrastructure:** The absence of physical branches makes it difficult to build trust with customers who prefer face-to-face service, especially older generations and rural users.
- **Customer Trust Issues:** Neo banks are relatively new, and the lack of legacy reputation or brand visibility often leads to skepticism among potential customers.

These challenges hinder the scalability of neo banks and emphasize the need for stronger regulatory frameworks, secure platforms, and effective branding strategies to gain long-term consumer trust.

5. Opportunities for Neo Banks

Neo banks, on the other hand, are well-positioned to take advantage of several opportunities:

- **Low-Cost Operations:** Without the expense of maintaining physical branches, neo banks can provide more affordable services, attract cost-conscious consumers, and remain financially sustainable.
- **Financial Inclusion:** They can reach unbanked and underserved populations in rural and semi-urban areas by offering simplified digital onboarding processes and mobile-based services.
- **Personalized Services:** With access to real-time customer data, neo banks can offer customized financial products such as tailored budgeting tools, expense trackers, and goal-based savings accounts.
- **Technological Partnerships:** Collaborations with fintech companies and traditional banks enable neo banks to expand their service offerings, scale faster, and increase customer credibility.

By leveraging these opportunities, neo banks can reshape the banking landscape, particularly for digital-first users, while also contributing to inclusive economic growth and financial innovation.

Conclusion

The rise of neo banks signifies a broader transformation in the financial services industry. Driven by customer demand for convenience, cost-effectiveness, and innovation, neo banks challenge traditional models and push for a more inclusive, tech-driven approach to banking. However, for sustained growth, they must navigate regulatory frameworks, bolster cyber security, and build customer trust. As this study reveals, the strategic use of services, demographic targeting, and forward-looking innovation will determine the future trajectory of neo banks in the global financial ecosystem.

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