NEO Bank- Revolution in Indian Banking Sector- A Critical Analysis

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ABSTRACT

A bank is a place where all kind of financial transaction takes place, where people save their money or make investments through it. In the age of digital India, we are focusing on digitalization of everything then why not banks also. Neo banking is a concept where we do not have any physical bank because it will provide services entirely through online mode. Neo banking is an entirely different concept where customer can avail all the service of physical banks even without having any physical bank-like money transfer, money lending, investments and many more. These neo banks are completely based on the “Information Technology” and “Artificial Intelligence” but still they do not have bank license as Reserve Bank of India keep a strict check on banking services. Thus, these neo banks depend on the bank partners to provide them with banking service license. Today it has become very important for every business to meet the requirement of the customers and their level of satisfaction if they want to survive in the market, but somehow traditional banking approach are unable to fulfill that which neo banking is trying to fill that gap between the customer and traditional bank.

In this research paper, the author will firstly explain the concept of neo banking, functionality of neo banking than the author will focus on the regulation of the neo banking and their reorganization in Indian banking sector. The paper will further emphasize on the working aspect of the neo banking means services provided by them to their customers. Thereafter, the author will put light on scope of neo banking in India and at the end; the paper will also contain a comparative study of working neo banking in India and in other countries.

Keywords: Neo banking, online transaction, customer satisfaction, Reserve Bank of India, Information Technology, Artificial Intelligence.

I. INTRODUCTION

Neo bank is a new concept emerging in Indian Banking Sector, which will be operated completely through online mode using “Information technology” and “Artificial Intelligence”

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and there will be no specific location for such neo banks. Neo banks can be called as fin-tech firm.

Neo banks are coming up with more customer satisfaction, customer convenience, speedy customer service and transparency. Neo banks are mainly non-banking service provider providing banking services with an ultimate safeguard to their customers. Neo banks are considered as non-banking service provider because Reserve Bank of India has not allowed 100% of their online banking services and they have to provide services through traditional bank partners only.

Neo banks provides with fast opening of accounts, cloud storage, ease of making and receiving payments, transfers and remittance solutions and many more, it also provides for creditworthiness to attract MSMEs.

In the time of digitalization, the concept of neo banks by fin-tech firm can prove as a great opportunity for the growth in an Indian market because of their “low-cost business model”.

An establishment of neo banks in India is not so easy because in back 2018, A Reserve bank of India had restricted the trade in crypto currency in all form stating the reason that it is a “threat to security” which result in a temporary halt in coming of neo banking in India. Later, in 2019 Reserve Bank of India has passed circular allowing fin-tech firms to enter in an Indian banking market in a restricted ecosystem with the concept of neo banks.

Anish Achuthan has said that “for traditional banks it would be difficult for them to change their legacy technology for which they have already spend a lot. Neo- banks on the other hand, are small and nimble. They can use latest technology and offer solution to customers banking problems. He further stated an example that all traditional banks offer transaction through UPI (Unified Payment Interface). Customer prefers to use non-banking app such as Google Pay or PhonePe, which offer the service in partnership with traditional banks.”

II. RESEARCH METHODOLOGY

The author has done descriptive research using qualitative and quantitative research for which the author has relied upon different sources of secondary data that are published in various journals on which the author has done content analysis to come on conclusion. The author has

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2 Vartika Rawat & Ishan Shah, “Neobanks are democratizing services for SMEs” dated October 11, 2019, available at: https://cfo.economictimes.indiatimes.com/news/neobanks-are-democratising-services-for-smes/71540302
3 Anish Achuthan, CEO and Co-Founder of Open Financial Technologies Pvt. Ltd.

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also used comparative method to analysis the situation of neo banks in India and in other countries.

III. OBJECTIVE OF STUDY

India is a developing country where a bank plays an important role in the development of economy. Banks not only keep customers money safe but also help in increasing the value of money by giving interest on it. It also helps customers by giving them loan for the purpose of expanding their business. But in the age of digitalization there is no difference between day and night because with the help of technology anything can be done at anytime. But traditional banks somehow fail to fill this gap. Even though they provide UPI but customers prefer to use neo banks payment interface because it is convenient. Traditional banks also provide E-Banking and M-Banking but that is also in very limited sense as NEFT/RTGS can be done through e-banking only in bank hours which is again a problem. So to analyze how neo banks are overcoming with all these short comes of traditional banks.

IV. LITERATURE REVIEW

1. Tinesh Bhasin in his article “What do neo banks offer and should you try them?” has stated that neo bank is coming up with a new concept to ease the banking services with the help of information technology and artificial intelligence. He has also included in his article about the companies taking initiative to come in India. He further mentioned the services they offer, mode of offering services. Thus, the author finds this paper as a useful material for conducting research on the given topic.

2. Advait Rao Palepu in his article “India’s Neo-Banks: What’s So ‘Neo’ About Them?” has done quantitative research where he has mentioned about the global approach of the neo banks in terms of capital investment and global reach. This paper also takes about regulatory framework for neo banks in India and also stated reasons for the restrictions imposed by RBI on certain aspects where neo banks cannot deal in. He also mentioned in his paper that neo banks have great opportunity in India because they have targeted customer segment with digital services which they are providing is much more than what traditional banks are providing. This paper has also mention in his paper about such companies showing interest in doing business in India and their market analysis. So the author has taken reference

5 Tinesh Bhasin, “What do neo banks offer and should you try them?” dated June 01, 2020, Available at: https://www.livemint.com/money/personal-finance/what-do-neo-banks-offer-and-should-you-try-them-11591032340062.html

6 Advait rao Palepu, “India’s Neo Bank: What’s So Neo About Them?”, Dated: December 04, 2019, Available at: https://www.bloombergquint.com/business/fintech-news-indias-neo-banks-whats-so-neo-about-them
from this paper in terms of quantitative research done by the author and the market analysis of selected companies referred in this paper.

3. **Vanita D’souza** in her article “5 Neo Banks that are changing the way India Does banking” has included the report published by ‘Allied Market Research’ which states the growth rate of neo banks from year 2017 to 2020, the research also mention about the view of the customer and their preference in respect of neo bank. This article also states that neo bank has a great opportunity in Indian market and can be proved beneficial for MSMEs in terms of loan advancement, ease of payment method, creditworthiness. Thus, the author has taken reference of this article for the purpose of analyzing the market condition and in what ways MSMEs can be benefited from neo banks.

4. **Raghav Agarwal and Avneesh Singh Nagar** in their article “Neo Banks and the next banking revolution” they have mentioned about how the business of banking is changing rapidly. They have further differentiated between digital bank and neo bank with a case study of e-KYC and UIDIA. They have pointed out certain advantages of neo bank and the challenges and shortfalls of neo bank. Later they have discussed about the structure of neo banks like their core infrastructure, B2C/B2B Modules. Thus, from this article the author has taken reference of structure of neo banks that how they channelize end to end service, then author has also referred the advantage and shortfalls of neo bank from this article.

5. **Gabriel Hopkinson, Romeo V. Turcam, Diana Klarova and Valeria Gulieva** in their article “How neo banks business models challenge traditional banks”. They have mentioned about the revolution that has been brought by the neo banks in the banking sector and have also stated the reason for such a great revolution i.e. transparency, Low-cost structure, end to end customer services, 24*7 customer support, money management tools etc. They have also mentioned about how neo banks have made investment easy for everyone. Now everyone can invest into mutual funds without any difficulty. Neo bank also provide them with the flexibility of anytime switch in or switch out which is widely attracting customer for investments through neo banks, not only this but customer also get higher rate of interest than what they get through traditional banks. They have also focused in this article about the future of banking sector. However, the author has only taken the reference of future of banking sector as a relevant part for the purpose of research.

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6. **Vinod Kothari** is his book “Banking Law and Practice in India”\(^9\) has talked about various functions performed by commercial bank in order to provide services to its customer. Though this book does not talk about the function of a neo bank or a fin-tech firm but it will help the author to compare the functions of a commercial bank with that of a neo bank is providing to its customers and what other functions does a neo bank can provide in future.

7. **Michael Magrath** is his article “Top Regulatory Consideration for Neo Bank”\(^10\) has mentioned about the various challenges face by the neo banks in providing services to its customers mainly in respect with privacy of data. He said that most of the customers are having same concern that whether their data and money will be safe in neo bank.” So he has given certain way to overcome these challenges. He said in his article that the layering of security is very important in order to protect customer’s privacy. The author has used this article as reference for the purpose of writing challenges faced by neo banks.

V. **NEO BANKS AND TRADITIONAL BANKS OR DIGITAL BANK**

1. Neo bank is completely an online process where all the transaction takes place through online mode via mobile application or through web service; they do not any physical setup for the purpose of providing any services. Whereas traditional have physical setup for providing services.

2. Neo bank is a virtual bank were customer and the banker does not deal face to face but through a medium mainly through application where as in traditional bank the deal take place through physical meeting.

3. Neo banks is a cheaper way to make transaction as compared to traditional bank like there is no monthly charge levied by the neo bank unlike traditional bank. For instance, if a customer asks his bank to issue a cheque book or debit card then he has to pay certain amount for the particular services. But it is not in the case of neo bank as they do not charge any amount from the customers for keeping money in e-wallet.

4. The major difference between neo bank and traditional bank is that traditional banks have their own license where as neo banks do not have their own license as of now. They have to rely on some licensed partner for providing their services.

5. An approval process like loan sanction or any service request in traditional bank usually takes longer time than a neo bank.


6. Neo bank is completely based on Information Technology and Artificial Intelligence which make the transaction seamless and also keep a watch on customer activity over application like the kind of services he is availing or has been frequently checking those services, it help the customer by providing information related to those services via different mode of communication which cannot be seen in the case of traditional banks.

7. Neo bank’s services can be availed at any time of the day without any interruption but it is not same with traditional banks because they have time duration even if using their digital portal. For example: if a person want to transfer certain amount of money using digital bank or through bank branch then he can do so between 10am to 4pm but in neo bank he can transfer money at any point of time even if its midnight.

8. If we analysis these two terms that is neo bank and digital bank they both look very similar to each other in their activities, in such a way as they both are giving online services to their customer. But there is a slight difference between neo bank and digital bank that is digital bank is an online medium of the traditional bank for providing services whereas neo bank is completely different and entirely based on IT and Artificial Intelligence.

VI. STRUCTURE OF NEO BANK

Neo bank is fully digitally operated bank using Information technology and Artificial Intelligence which create an innovative infrastructure for the customer which make the banking service seamless. Neo bank is a based-on Application Programming Interface (API) which is a computer bases programming which help in connecting the one software to the another in order to provide services. API helps the banks in order to open their system so that the third party can provide banking services through their inbuilt infrastructure.

API for open bank or neo bank is in a restricted manner because it allows only to those who are having partnership with the licensed banks\textsuperscript{11}. For example, Yono is a kind of open bank or Paytm Payment Bank.

In India, neo bank is not independently functional; they must have to rely their partner. Thus, API help neo bank in inheriting users and expanding customer base over third party platform.

Neo bank is a platform centric rather than product centric. It is so because neo bank is being preferred only for its platform based. It has a high community engagement with the numerous

\textsuperscript{11} Adait Rao Palepu, “The New baking Lexicon For the 2020s” Dated: 18\textsuperscript{th} January, 2020, Available at: https://www.bloombergquint.com/economy-finance/the-new-banking-lexicon-for-the-2020s
services with open technological architecture which also allow external developer. It provides with real time management facility and instant service and has customer centric focus.

The neo bank structure is divided into three major parts:

1. Core Infrastructure:
   This layer mainly works in backend, as there are multiple bank partners allowing neo banks to render their services. They have payment gateway associated with traditional bank partners.

2. B2B/ B2C Modules:
   This is the front-end service of a neo bank. It shows the list of services provided by the neo banks to their customers.

3. Customers:
   Neo banks have larger customer base which under B2B module includes IT Outsourcing Company, Travel Industry, Marketplaces, E-Commerce Sellers, NGOs and Education etc.

VII. SERVICE TO CUSTOMER BY NEO BANKS

Neo banks are known as open bank using Artificial Intelligence and API which allow customers to avail number of banking activity. These neo banks allow customer to open an account at no cost and the benefit of having neo bank account is that it can be accessible from anywhere with its login credentials. They allow customer to manage their money in a systematic way and provide them with various investment option. These banks have wallet

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12 Raghav Aggarwal and Anveesh Singh Narang, “Neo bank and the next banking revolution”, Available at: https://www.pwc.in/consulting/financial-services/fintech/fintech-insights/neobanks-and-the-next-banking-revolution.html

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facility which also helps in keeping the customers money safe as it is in a digital form that cannot be stolen by anyone. As it is very well known that neo bank completely work on AI and API which also allow these banks to keep a track record of the transaction pattern, credibility and other financial data and accordingly recommend related services to their customers. These neo banks have loan facility at a very minimum rate of interest.

For example: Paytm Payment Bank provides loan up to ₹2 L to small or medium entity for a limited time period at low interest rate. Paytm Payment Bank is a neo bank which makes the loan process easy as the customer need not visit branch of its respective bank with lots of documents.\textsuperscript{13}

Neo bank also allows their customers to check their statement and manage their money. They have the option to put limit on their expenditure. These banks also have their blogs which make the customer aware of their services, financial education and different investment policy.

\textbf{VIII. REGULATORY FRAMEWORK FOR NEO BANK}

In India, majority of banks are having physical workplace with e-banking services that is digital banks. As we have already discussed the difference between neo banks and traditional banks or digital bank, there is a different regulation for neo-bank as they are not licensed bank. They can render there services only through some licensed partner bank. In 2014, the RBI in its annual report said that its RBI does not recognize payment banks under the term ‘banking’\textsuperscript{14}, in virtual and branchless banks\textsuperscript{15}. Thus, RBI is not issuing a separate virtual banking license to these neo banks.

A report was submitted to RBI for licensing the virtual banks because they are not just payment banks but much more than that.\textsuperscript{16} Again in 2018, RBI has imposed complete restriction on trading in crypto currency stating that it may be threat to national security. This move by RBI has also restricted the entering of neo bank in India. Later in 2019, RBI has somehow allowed the neo banks in India in a very restrictive ecosystem for marketing.

\textsuperscript{13} Paytm for Business, Blog by Paytm on “Working Capital Loans for Your Business”, Dated: May 2\textsuperscript{nd}, 2020, Available at: https://business.paytm.com/blog/introducing-paytmloan/

\textsuperscript{14} S 5(b), The Banking Regulation Act, 1949, Act No. (10 of 1949)

\textsuperscript{15} Raghav Aggarwal and Anveesh Singh Narang, “Neo bank and the next banking revolution”, Available at: https://www.pwc.in/consulting/financial-services/fintech/fintech-insights/neobanks-and-the-next-banking-revolution.html

\textsuperscript{16} Suman Gandham, Founder and CEO of Finin.
IX. ADVANTAGES OF NEO BANKS

1. A Neo bank provides services at a very low cost as it do not ask from the customer to maintain minimum balance and there is no extra hidden.

2. Neo bank pays higher rate of return on saving account and interest on fixed deposit than the traditional bank.

3. Neo banks do not have any physical branch, it is completely technological driven and give greater banking experience to its customer.

4. It is time efficient as it provide almost real time services without much documentation.

5. It also encourages investment facility and also provides investment education.

6. It provides round the clock services i.e. 24*7 and in case of any dispute or issue it can be resolved seamless through automated messaging system or Artificial Intelligence.

7. The primary business of neo bank is to provide banking services and apart for this they also provide near real time accounting and reconciliation services for bookkeeping, balance sheets, profit and loss statement and certain taxation services like invoicing, GST compliance, payment of tax etc.

8. Neo bank ensures complete transparency of services, charges, and complete details of every transaction and notifications.

9. Neo bank ensures high security feature for account and debit card with blocking feature within application or over call.

10. Neo bank allows customer to manage their other accounts which are either partner or associated banks with them.

X. CHALLENGES FOR NEO BANKS

1. Neo bank is in banking service tough not completely as they are not providing all the services that a traditional bank is providing.

2. The biggest challenge in front of neo bank is there separate licensing. We have seen in regulation of neo bank that neo bank is not recognized as virtual bank in India as of now which stands as a hurdle in their development because they have to depend on other partner bank for licensing. Thus, it results in lack of satisfaction among the promoter of neo bank because they have to agree on all the terms and condition of the partner bank for the sake licensing.
3. Another challenge for neo bank is lack of technological knowledge among the customers. Thus, they are unable to make best use of it.

4. Due to branchless concept of neo bank, it creates a trust issue among people as they think their money is not safe.

   For Example: Recently Google has removed Paytm from the Play Store because of violation of gambling policy, thus the Paytm customers are in a great dilemma that whether their money in Paytm wallet is safe? After that Paytm replied that the customer money in wallet is completely safe.

   Though in such cases customer lose their trust in neo banks.

5. Another major challenge for neo bank is no regulatory framework which et rules and regulations for the neo banks in order completely authorized them for providing services.

6. The neo bank offers considerable services to the customer though they don’t fully satisfy all the needs.

**XI. NEO BANK IN INDIA AND IN OTHER COUNTRY**

In the era of digitalization, banking sector is also in its way to give complete online solution to its customers. RBI is also now planning to recognize neo ban as ‘banks. There are currently 5 major neo banks providing services in India are:

**NiYO**

NiYO is a neo bank which mainly provides services to the customer who are salary based employees. NiYO claims that it has more than 5 Lakh customers and has tie-up with 3000 corporate sectors in order to provide services to their employees. NiYO has recently launched a “Global Card” which makes the foreign transaction much easier for that customer who goes for a foreign trip. It is so because now customers need not to take a forex card.

NiYO also provide technology based financial assistance and advise to its customers of various investment schemes and strategies. The Co-Founder of NiYO has said that “Financial inclusion has always been at the core of our business. We believe this will go a long way in helping booth our existing and new customers manage their short-term and long-term financial needs”.

NiYO bank claims that they provide instant opening of bank account with up to 7 percent of
interest rate on saving account and also with no ATM transaction chargers.  

811 BY KOTAK
Kotak Mahindra Bank has also taken initiative for establishing an online platform to ease the banking business. 811 by Kotak is a kind of neo bank which provide a digital platform to their customer in order to avail maximum service without visiting bank branch.

811 by Kotak provides virtual bank account which give approx 6 percent of interest rate on saving account and also have virtual card facility to fast payment process.

OPEN
OPEN is another neo bank which has its main focus on Small and Medium Enterprises.
OPEN was launched 2017 and has partnered with ICICI bank in order to provide services to its customer and at present there are almost 11 bank that has came into partnership with OPEN. Recently, OPEN has crossed around $ 4 billion of analyzed transaction revenues on the platform.

Anish Achuthan founder of OPEN said “Neo-banking is not just about financial inclusion, it’s also about bundling services with other financial services. So in India, neo banking can work as an extension to solve or the financial inclusion challenges. Secondly, we are seeing fintech start-up build niche solutions focusing on blue collar jobs and that’s the way forward”.

YONO BY SBI
YONO is most familiar neo banking service among us as State Bank of India has launched YONO in Nov. 2017 for establishing online platform. YONO not only provide banking services but also allow customers to explore lifestyle services such as online shopping, cab services etc.

YONO has card less withdrawal of cash from SBI ATM, YONO is using API method which create a reference number whenever you want to withdraw cash. In such case customer just need to visit nearest SBI ATM enable with YONO Cash and enter the reference number and

17 NiYO Bank, About Us, Available at: https://www.goniyo.com/
18 Vanita D’souza, “Neo Banks that are changing the way India does banking”, Date: 16th April, 2019, Available at: https://www.entrepreneur.com/article/332315
19 Vanita D’souza, “Neo Banks that are changing the way India does banking”, Date: 16th April, 2019, Available at: https://www.entrepreneur.com/article/332315
will be able to withdraw cash.\textsuperscript{20}

**INSTANTPAY**

InstantPay has launched its neo banking service in FY2020 mainly focusing on Small and Medium Enterprise in order to ease the business transaction much easier such as payment, settlement, financial requirement etc.

Shailendra Agarwal, CEO of InstantPay, said in a statement said “Driven by favourable government policies and flexible banking institutions, SMEs are increasingly contributing to the development of our country as well as offering employment. Our banking solution is designed to address the unique requirements of SMEs. It does away with the hassles of traditional banking process & policies and provides a seamless and user-friendly experience”\textsuperscript{21}.

**XII. FUTURE OF NEO BANK IN INDIA**

Neo bank provides ease of doing banking activities with the help of API, it also ensures fast payment and collection method, financial assistance, investment schemes, cashless environment etc. and it mainly focus on SMEs as they are proving themselves as a business of new era by using technology for doing their business.

Neo bank overcomes the challenges faced by the individual in transacting with traditional banks such as clearance of cheque, money deposit, other services like bank statement for current account, lengthy documentation for loan processing. Neo bank eliminates all these difficulty by providing near real time services to its customer. Neo banks not only helping the businessmen but also to customers in different way. Neo bank also provides more interest rate on saving account or in investment fund than that of traditional banks. Neo bank also ensure fast opening of account in neo bank though are certain areas in which neo bank does not deal in which traditional banks do.

If we analysis the current we can say that neo banks are having a great future in India. Today, they don’t have their own separate banking license but RBI is considering to recognize neo banks as ‘bank. Neo bank has great potential in building a new age of banking services in

\textsuperscript{20} Navneet Dubey, “YONO cash withdrawal from SBI ATM”, ET Online, Date: April 05, 2019, Available at: https://economictimes.indiatimes.com/wealth/save/how-to-withdraw-cash-from-sbi-atm-without-using-debit-card-or-sbi-yono-app/articleshow/68722123.cms?from=mdr

order to provide seamless and swift customer experiences.

XIII. CONCLUSION

Neo bank is the future of banking sector. It enables the seamless banking with various services that eliminate the gap between traditional banks and customers. It is very much essential to convert traditional banks into neo bank in the age of digitalization because now everyone wants that their work should be done at just one click without being waiting for long day. It also help in reducing the corruption because of transparency in working process. It will also help in cutting the additional transaction cost such as processing charge and other charges.

Neo bank is introduction lots of new user data with user friendly interface in order to provide hassle free transaction. Neo bank will also help in creating funds and allocating the funds in proper account and government can have proper check on it.

Neo bank targets SMEs because they are focusing on development of the country at minimum cost. Therefore, neo bank can we suitable banking option for fast payment and collection process and for tax compliances as most of the neo bank also allow customers to file their GST return and other indirect taxes.

According to Digital Evolution Index, “India is among the top nation that has huge potential for digital payment. Cashless society is required and we will be able to achieve it. The aim must go from a cash economy to a less cash economy”.

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