

# Bank licences on tap but hardly anyone to tap

By [Saloni Shukla](#), [Shilpy Sinha](#), ET Bureau | Feb 01, 2017, 12.06 AM IST

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*In the US, there are more than 20,000 banks for a population of 400 million, while for India's 1.3 billion people, there are only 40 scheduled commercial banks and 1,574 urban co-operative banks with many of them being dysfunctional.*

before the question of value was explored in depth by economists, Adam Smith was confounded by the problem why diamond with hardly any use was more valuable than essential water. Something similar is happening in Indian banking as to when licence was rationed, there was a scramble, but when it went on tap, hardly anyone is tapping.

When dozens queued up to get a licence either to start a payments bank or a small finance bank, nearly half of the Indian population of 130 crore being unbanked was touted as an opportunity. In February 2015, 113 scrambled to get a licence. A status check after two years shows: 21 got the licence, three have dropped out of the race and nearly a dozen are nowhere near commencing the business.

RBI approved 11 applicants in August 2015 to set up [payments banks](#) with a stipulation that they commence operations by February 2017. And 10 were granted license to start a small finance bank with a string that they begin business by March 2017.

Equitas, Suryodaya, Local Capital Area Bank and Utkarsh have already started their small finance banks, while [Airtel](#) and India Post have launched payments banks. [Paytm](#) has received a final go ahead from the regulator to launch a payments bank. It is not just those with licences being hesitant to begin operations, but the on-tap bank licence offer that was hailed as a revolution in regulatory approach may also be fizzling out.

Six months since on-tap licensing was announced as a parting gift from Raghuram Rajan, there is not a single applicant. "Those who want to apply haven't figured out how to make money yet. Traditionally, banking in India has made money primarily from low competition," says Krishnamurthy Subramanian, assistant professor of finance at the Indian School of Business.

"Name one Indian product that is globally competitive? Whether it is Windows or Starbucks, it's all American. Except for Yoga, there isn't a single Indian product acceptable worldwide. Because our corporates are not innovative enough, that is why they are at a loss. "



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In the US, with a population of 400 million, there are more than 20,000 banks, many of which are community and local banks. India with a population of 1.3 billion people has only 40 scheduled commercial banks and 1,574 urban co-operative banks with many of them being dysfunctional.

Tough conditions like high capital requirement of Rs 500 crore and large industrial houses with such resources being barred from bidding for licences themselves could be deterrents.

"The reason that there are no applicants is that it is a difficult market to get in for people which are not industrial houses," says TT Ram Mohan, professor, IIM Ahmedabad.

"The only ones who can enter this market are people with deep pockets and the RBI doesn't seem very receptive to them." But the lukewarm response is not necessarily a reflection on the potential for making money in financial services where many models exist. One of them is non-banking finance company which is a better model for profits, especially when interest rates are headed lower.

"People take time to understand that banking makes money only over a long period of time, so you have to be willing to take that call," said Deepak Gupta, joint managing director, [Kotak Mahindra Bank](#). "For the first five years, banking is an inferior model than an NBFC and banks have a problem of bureaucratic costs like compliance, and risk which is significantly higher than an NBFC, plus branches and ATMs."

Gupta, whose bank was an NBFC before converting into a bank, says that while typical operating cost of a bank was anywhere between 2% and 2.5% of its total assets, for an NBFC it is less than 1%. The dynamics of the industry are fast changing and the mushrooming of financial technology companies are threatening even established banks' bread and butter business.

"Licences on on-tap basis doesn't put pressure on anyone to apply for a bank licence in a limited time period, but only after doing detailed viability analysis," said PN Vasudevan, MD, Equitas. "No applicant for a licence shows that people do not want to just rush in which is a good sign."

When mobile wallet companies are challenging the likes of the [State Bank of India](#) and [HDFC Bank](#), the new entrants are not sure about what they are getting into. "There is a huge question mark on payments bank viability once you move to the UPI interface," says Mohan of IIM-Ahmedabad.

"There is no reason for you to go to a payments bank when your existing bank can give you all the facilities. The small finance banks look promising because they are getting into areas which are not of great interest to the universal banks."

Big banks which have been hobbled by regulations fear that they might end up being a specialised bank for corporates as innovations can take away their retail customers who are looking more for convenience than complicated products that big banks bring to them.

"One doesn't know how digital shapes up," says Gupta. "For example, for an universal bank, retail tends to be one-third of total business. Will that retail move straight to the payments bank? Who knows? So the corporate piece may remain but the retail piece may just go away."

[Mobikwik](#), a fintech firm which was one of the 72 applicants for payments bank licence, believes that regulations are lagging behind the emerging reality.

"I am looking for being an internet-only bank," said Mrinal Sinha, chief operating officer of Mobikwik. "If I am able to service the customer, I should have the right to choose the business model. This is world 2.0. Our policy making needs to evolve to say that there is a huge segment of India which doesn't want anything to do with branches."

Non-banking finance companies which are quasi banks may look to gain by converting into a full-fledged bank as they could access lower cost current and savings account deposits, but many without vibrant financial services who looked to flip licence for a profit may struggle.

There are examples in the insurance industry like Bharti and the Future group which are struggling to make a mark and it won't be anything different with banking which is even tougher due to higher costs of compliance.

"If these aspirants want to do banking, the way it's been done then there isn't much to do because it will be another me too kind of bank," said Subramanian.

"A lot of corporates in India have made money either by their proximity to the government or by reverse engineering global products. If this has to work we can't be only talking about 'jugaad' innovation anymore."