Incidental paper: 01

Account inactivity in India—is there a problem? [1]

Akhand J Tiwari and Graham AN Wright

The scope and scale: Bank accounts and inactivity

The latest Findex data on account inactivity has pushed India to rethink its efforts to improve financial inclusion (figure 1). Findex defines inactivity as **"The percentage of respondents who report neither a deposit into nor a withdrawal from their account in the past year. This also includes making or receiving any digital payment."**

What does this number mean in the Indian context? About 273 million adult Indians did not use their bank accounts in the past year.[2]

In this note, we decode the reasons for account inactivity.

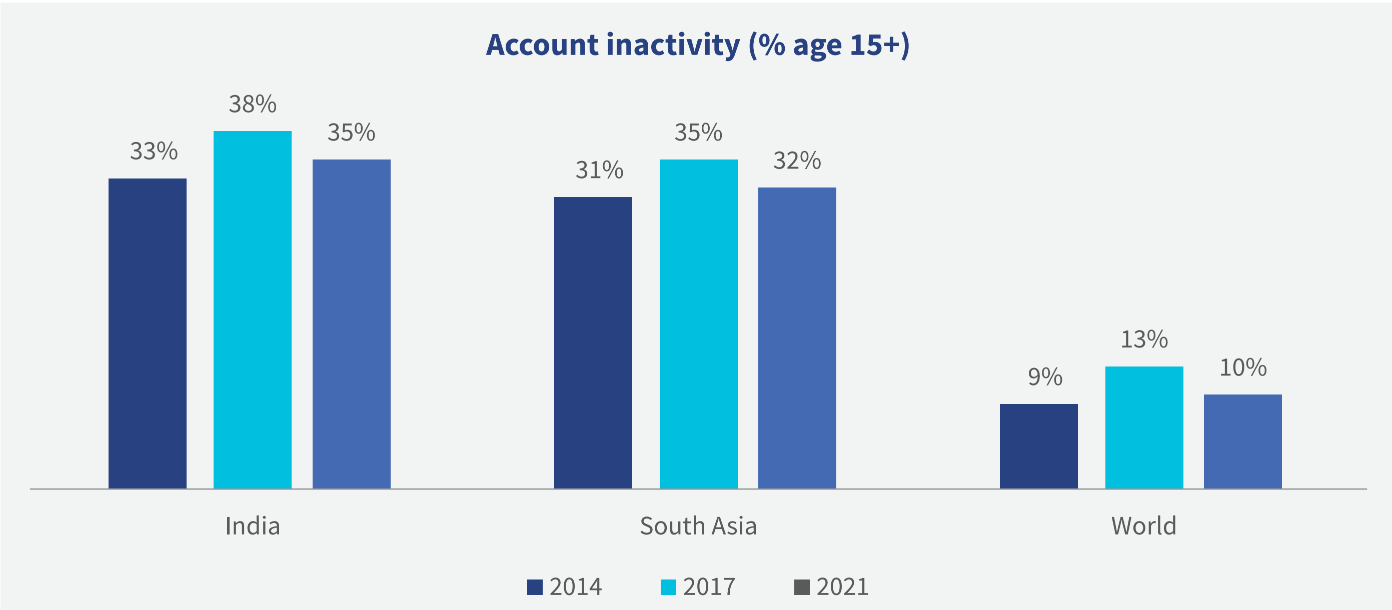

Figure 1: Account inactivity in India, Findex 2021

[1] The authors thank MSC colleagues Kanishkaa, Rahul, Monica, Mimansa, and Nikhita for their support

[2] Out of 1.4 billion (2022, current estimates) Indians, 67% are 15 to 64 years of age, and 7% are above 65. This corresponds to 1 billion adults (74%). As per Findex 2021, 78% of adults (=780 million) have accounts and 35% of these (=273 million) accounts are inactive.

PMJDY accounts and their dormancy: Some context, history, and myth busting

Some may assume that inactive PMJDY accounts primarily drive these numbers, as many new accounts opened between 2014 and 2016 after the PMJDY scheme was announced in 2014.[3] Yet, while the large number of new accounts opened initially may explain the higher inactivity in 2017, it does not explain the account inactivity at present.

NFA and PMJDY

In 2011, five years after the Reserve Bank of India (RBI) introduced no-frills accounts (NFAs), the precursor to PMJDY accounts, MSC assessed why many of them were dormant. Our research concluded, "Despite an impressive number of NFA account openings, approximately 50.6 million with balances of INR 53,860 million—too many are used only for withdrawing government benefits and wages, such as NREGA. The majority often remain inactive or dormant. In most areas, only 20% or fewer use their accounts for small savings, which was the original objective of launching these accounts. As a result, banks lose money on these accounts, which cost INR 13.4 per transaction and INR 50.45 for account opening, or INR 250 total to open and maintain accounts. Not surprisingly, bank service is often unsatisfactory—and less than encouraging for customers to continue NFA use."

We also noted that "adoption ultimately comes down to three deterrents: proximity, convenience, and security. These deterrents magnify if money is involved. They are magnified further if small amounts of precious money are involved. Any initiative to change customer behavior must address these concerns. So far, our research indicates no-frills accounts have failed to achieve this.

Too often, NFA customers live too far from branches to use their accounts more than once or twice a month. Too much effort and expense are needed for simple transactions, and almost no aspect of banking services is "convenient" for NFA customers. Finally, while both customers' sense of security and confidence improved because banks inspire both, they are insufficient to overcome the discouraging barriers imposed by distance and difficulty. So the majority do not use their NFAs, or use them only to withdraw money unavailable through other channels."

[3] *Pradhan Mantri Jan-Dhan Yojana* (PMJDY) In 2014, the Government of India launched the PMJDY financial inclusion scheme to provide banking to all households without access to the formal financial system. PMJDY provides debit cards, insurance, pension facilities, and overdraft to beneficiaries.

What changed with PMJDY accounts?

In this note, MSC documented how PMJDY accounts were different. The core of this change was how a bank account was at the center of delivering financial services (figure 2). The Government of India modified the scheme design regularly to add new features and onboard more users. While the total number of accounts decreased from 2017 by 2% in India (Findex 2021), likely due to a decrease in non-PMJDY accounts, the number of PMJDY accounts has increased consistently.[4]

Aadhaar-seeded PMJDY bank account

- Seamless transfer of G2P payments for employment, maternity benefits (PMMYY and JSY), scholarships, LPG subsidy, social benefits, and incentives, among others
- Access to pension schemes like APY and NPS
- Easy access to various insurance products like PMSBY, PMJJBY, PMFBY, among others
- RuPay card issued to manage card-based transactions
- Hassle-free overdraft (credit) facility by banks
- Easy to link the account to BHIM app (mobile banking) and process remittance as well as pay utility bills

Figure 2: PMJDY scheme design

PMJDY accounts consistently show higher account activity (figure 3). As per the government's assessment, between March 2015 and March 2022, the deposits increased about 10.62 times, and accounts increased about 3.06 times. This increase is in line with Gunther's (2017) observation that while PMJDY's initial usage is low, over time, it converges with other accounts. Moreover, several studies and articles between 2014 and 2017, such as this, this, and this, slammed and cautioned the government for the poor scheme design. But seven years after PMJDY's launch, account usage has only seen an upward trend. A World Bank analysis from a 2017 paper notes that JDY may have allowed banks to meet the unmet demand for credit for some households that lacked prior access to formal banking products.

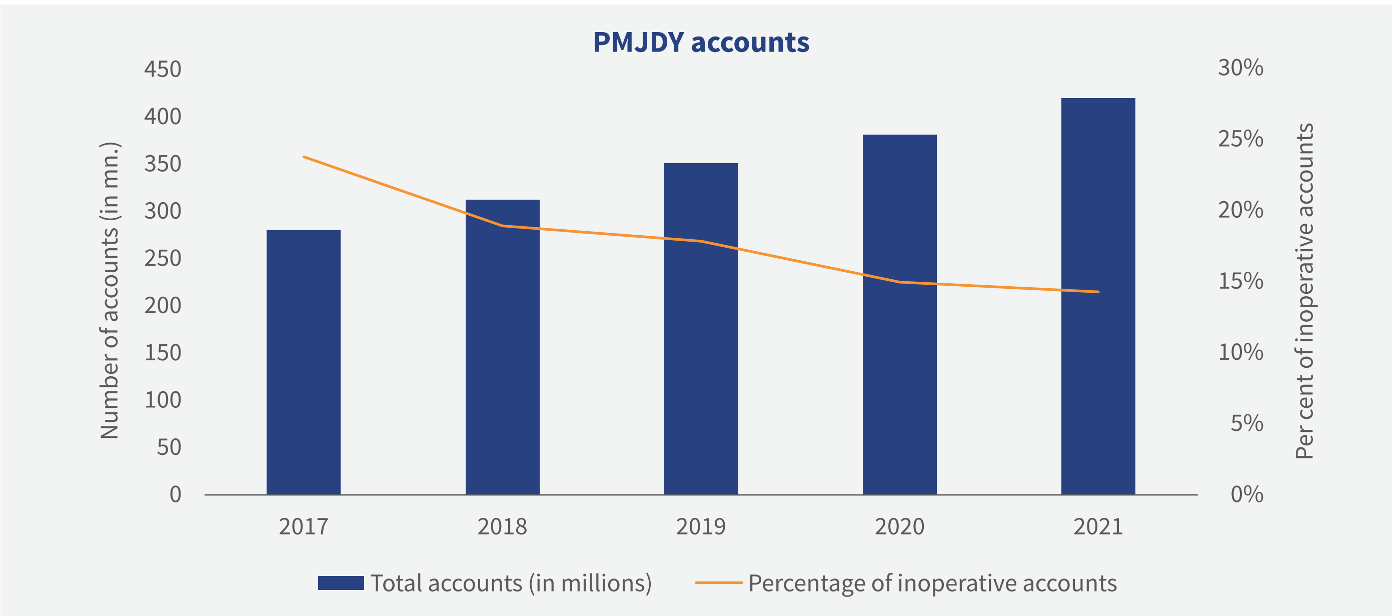

Figure 3: PMJDY account use vs dormant accounts
Source: Financial inclusion annual report 2021

[4] Within two years of the scheme's launch, banks and their agents had opened 310 million accounts. While MSC estimates that around a third of these were opened by people who already had another bank account, the impact on access to essential banking services was impressive. PMJDY-2.0 was launched in August 2018 with enhanced benefits, including the doubling of the overdraft limit to INR 10,000 (USD 139) and INR 200,000 (USD 2,778) accident insurance cover for RuPay cardholders.

The financial inclusion drive in India is based on the "JAM Trinity" and founded on the 472.8-million basic financial inclusion "PMJDY" accounts. As of November 2022, these accounts have a remarkable average balance of INR 3,800 (USD 50) per account. Grossed up to take care of the 17% "inoperative"[5] accounts, assuming they have zero balance, this gives an average balance of INR 4,578 (USD 60)—a huge amount for the low-income people—the target segment for the PMJDY accounts.

The bank account mix in India

The account mix is critical in the context of account dormancy. PMJDY accounts are around 18% of the total deposit accounts in India. RBI reports that India has approximately 2.6 billion deposit accounts. These accounts belong to six broad categories:

01 Saving account (which includes the PMJDY accounts)

02 Current account

03 Salary account

04 NRI account

05 Recurring deposit (RD) accounts

06 Fixed deposit (FD) accounts

Many Indians hold a range of these accounts. The Government of India has consistently improved the delivery of financial services, created use cases, in particular—many new direct benefit transfers, and distributed COVID-19 financial assistance to ~420 million people using bank accounts. The number of accounts receiving government benefits has increased (figure 4).

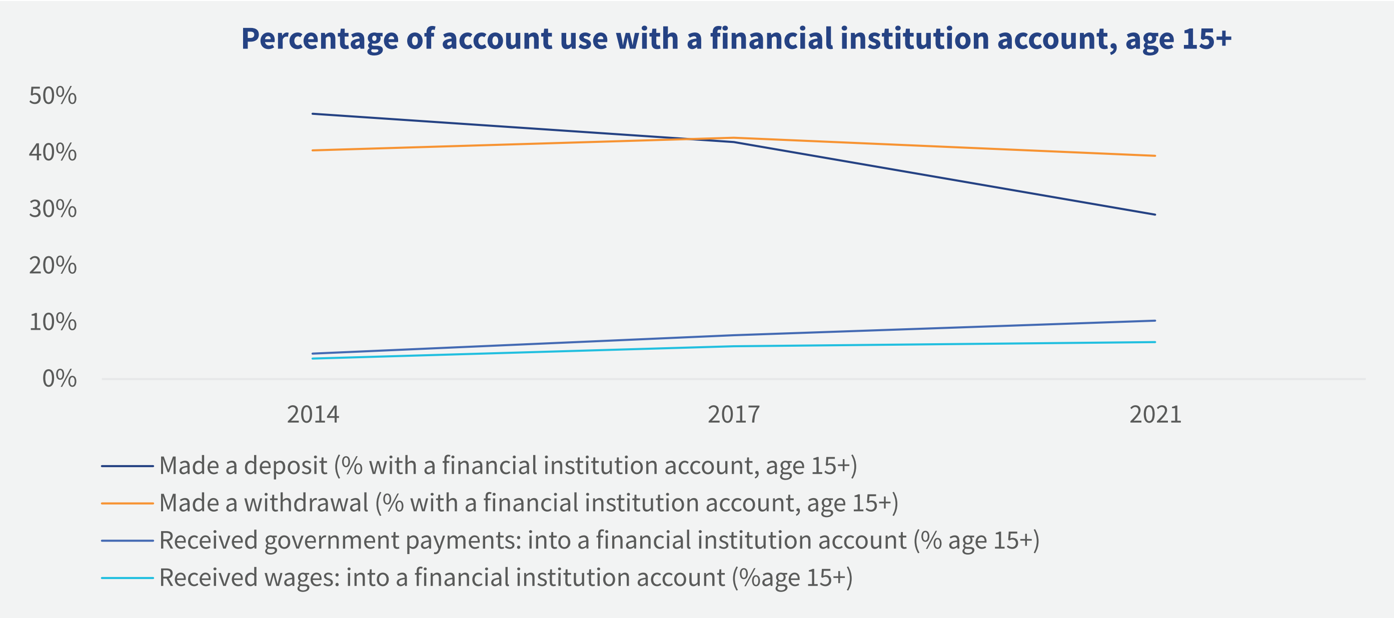

Figure 4: How Indians use their bank accounts, Findex 2021

[5] In contrast to Findex, the Reserve Bank of India defines an account as "inoperative" when there are "no transactions in the account for over a period of two years."

Decoding the inactive accounts

We discuss five critical reasons for bank account inactivity below.

1. Inactivity in PMJDY accounts

As indicated earlier, the government reports that 82 million (17%) of the 473 million PMJDY accounts are inactive. We attribute this to users who had an existing bank account and still opened a PMJDY account. Günther (2017) analyzed financial inclusion data of India using multiple data sets, such as Findex, Finscope, MSC, and FII data, and found that 51% of individual PMJDY account holders have a non-PMJDY account. This happened due to multiple reasons:

- During 2006-2012 when banks first deployed business correspondent network managers (BCNMs) to offer agent banking, BCNMs had to bid for specific geographies to operate. Later, they were allocated those geographies. In the absence of many transactions, most agents' income came from account-opening fees for NFAs[6]—the precursor to the PMJDY accounts. Read Is the Business Correspondent Model in Policy Paralysis? for more details. In this initial period, banks often changed the BCNMs representing them in different districts for various reasons. When this happened, more often than not, the new BCNM restarted the account-opening process for customers all over again. This practice was usually due to a lack of technical and backend compatibility across BCNMs and banks. See How Many Accounts Does A Man Have To Open To Be Financially Included? for more information.

- Prime Minister Narendra Modi launched the PMJDY formally on Independence Day, 2014. After the launch, BCNMs raced to meet the ambitious targets set by the government for account opening. As a result, the same individuals were often encouraged to open multiple accounts amid over-zealous account opening drives.

These factors led to people opening multiple PMJDY accounts when they only needed one. As a result, their other accounts remained dormant.

Multiple accounts for a user are not just a PMJDY phenomenon. Non-PMJDY account holders may have multiple accounts for various reasons. For example, despite RBI's notification in 2012 to support agent-level interoperability, consumers often had to open multiple accounts to access services and government payments from specific banks. People may open a new bank account to avail of the bank's specific deposit or credit product[7] facilities and stop using those accounts over time.

[6]The Indian regulator had first announced in 2005 that accounts with zero balance facility could be opened with a minimum of know your customer requirements. The banks initially called them no-frills accounts. In 2012, the regulator changed this term to Basic Saving Bank Deposit accounts. RBI guidelines. The PMJDY accounts are essentially BSBD accounts.

[7]For example, banks ask a customer to open a bank account and then open a loan or credit account for a customer. When the loan duration is over, it is not certain whether the user will continue to use the bank account. Similarly, a customer may open a bank account to avail a high-interest deposit product and stop using it when the deposit tenure is over.

2. Inactivity in all types of bank accounts due to domestic migration

Our discussions with bankers reveal that they often see dormant accounts for customers who relocate. These customers open a new account at the destination and stop using their older account. Thus, inter-state or inter-district migration contributes significantly to dormancy since India has many migrants. The current estimates could be between 506 million (average population growth) and 652 million (assuming the same growth percentage as between 2001 and 2011). We take an average of these two to arrive at an estimated 579 million migrants in India. Assuming a similar proportion (38%) of inter-state and inter-district migration based on data from 2011, 220 million migrants may have moved to a different place. Assuming the Findex percentage of account penetration (80%), we estimate 176 million migrants may have inactive accounts.

3. Inactivity due to the death of account holders

Per the Reserve Bank Policy, any account without activity in the past two years is considered dormant or inoperative. Banks transfer the money from an account that has been dormant for 10 years to the RBI's Depositor Education and Awareness Fund (DEAF). Recently, Nirmala Sitharaman mentioned that India had 90 million such accounts with USD 3.3 billion in balance.

The factors listed above are the ones for which we may not have much under control. For example, women and men with more than one account are likely to stop using one account, and the dead will not return to using their bank account. The regulator, the Ministry of Finance, and banks can check overzealous account-opening drives.

The account inactivity story, however, does not end here. Other reasons for account inactivity offer clear opportunities for action. We discuss these below.

4. Inactivity due to the poor design of channels and interfaces, such as agents and digital interfaces

Many people fear using digital interfaces or cannot use them, or fail to access agents. An estimated 198 million adult account holders are illiterate, given the 22% illiteracy in India in 2022. These customers fear complex interfaces. As a result, they refrain from using such services. Findex (2021) provides more insights—we learned that 16% of the excluded reported that they could not operate an account independently. We also know that many customers lack trust in agents. MSC's latest study on DBT and women's economic empowerment finds that out of the 45% of women who use formal financial services, 31% are unable (35%) or unwilling (63%) to withdraw money from their account without help from a male household member (See Figure 5). Such accounts are highly likely to become dormant after the government transfers stop.

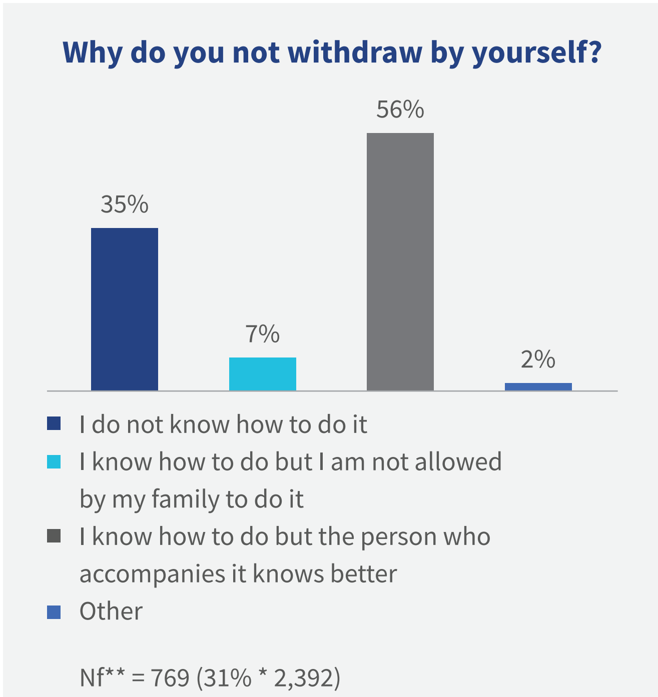

Figure 5: Findings from MSC study on G2P and WEE

5. Inactivity due to lack of use case

Findex reports that 41% of people do not keep money in their accounts. This number corresponds to 410 million adult Indians. This high proportion of inactive accounts indicates that PMJDY accounts are not responsible for account dormancy alone. The apparent lack of use cases may significantly drive inactivity for many accounts. For example, we have a limited understanding of the fundamental problems restricting women's access to formal financial services and their usage. In our work, we found that many female user groups have limited opportunities to use accounts regularly. Despite the rollout of women-specific direct benefit transfers, such as Ujjwala, 55% of women do not use bank accounts. Further, the Findex data suggests that 22.5% of women do not have an account, and 32.3% of women's accounts are inactive.

Obvious next steps, but maybe not

All stakeholders know of some of these challenges and many stakeholders have been working on them—in patches. Yet we have not seen adequate concerted actions on:

1. Products tailored for low-income women and men based on their wants and mental models;
2. Making digital user interfaces more intuitive through oral principles;
3. Developing digital capability and confidence of those stranded on the wrong side of the digital divide; and
4. Using agents to deliver a broader range of services, including helping those without access or confidence to use digital services.

A fundamental shift is needed to do this well and move away from seeing financial inclusion as an end in itself, from building financial systems and services and seeking use cases. We need to see financial services as part of a larger ecosystem to support, enable, and improve real-world economic activities, such as agriculture, enterprise development, health, education, and government services (figure 6).

In this new approach, financial services will become a crosscutting support component of digitally-enabled, real-world economic activities. Financial services will serve as an ancillary enabling service—driven by real needs arising from the real economy, and digital services will play an increasingly important role. This will mean that instead of starting with "designing financial services", we start with the real-world needs of poor and vulnerable communities and build services and infrastructure in response to them.

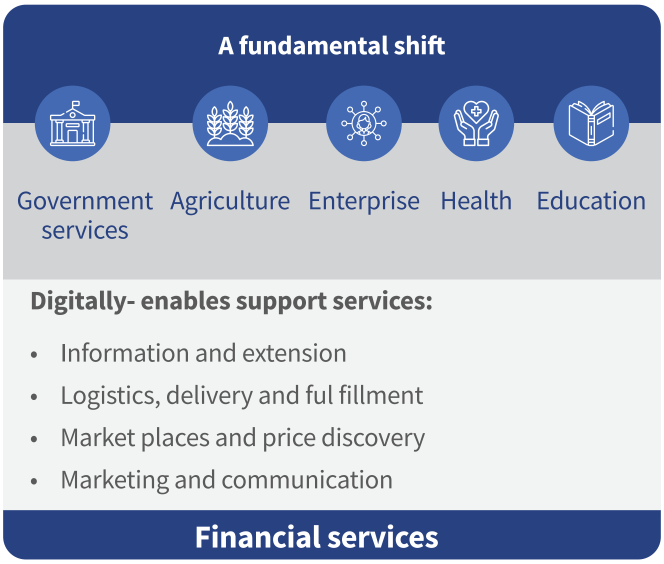

Figure 6: Our approaches to financial inclusion must undergo a fundamental shift