Research Paper
Impact Factor: 6.304
Peer Reviewed & Indexed Journal
www.ijbarr.com

IJBARR
E- ISSN -2347-856X
ISSN -2348-0653

SPURT IN DIGITAL FINANCIAL SERVICES - COVID – 19 DID WHAT DEMONETISATION COULDN'T

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Abstract
Digital financial services and related tools together, have the potential to bring sustainable benefits to consumers and entrepreneurs - extending the reach and access of financial services to potential investors/consumers; offering more convenient, faster and secure transactions; providing services that are tailored-made and facilitate their usage, thereby creating opportunities to develop financial literacy competencies, increasing opportunities for fruitful interactions between financial services providers and consumers through digital interfaces. The digital revolution goes hand-in-hand with new financial service products and providers entering the market offering services directly to individuals through digital channels.The increased usage of digital payment systems facilitated financial transactions during the COVID-19 pandemic and the subsequent lockdowns, social distancing and no-contact protocols.

Keywords:Demonetization, Digitalisation, Digital Currency, Digital Transactions, Digital Financial Services.

Demonetization

Demonetization is a procedure by which certain cash or currency notes are replaced with the other modes of financial transactions such as cheques, electronic payment etc. Demonetization of currency notes (Rupees 500 and 1000) was implemented on November 8, 2016, in India. The government declared the withdrawal of 500- and 1000-rupee notes so as to battle the black money and fake currency. As expected, the sudden deficiency of currency prompted a void in the business. Serpentine lines in the ATMs and banks saw the normal open quickly trading the old notes with the new ones and keeping the old notes in the banks. This movecentred to a greater amount of computerized, online exchanges consequently upgrading the instalments of machines such as Automatic tellers to replace the cash. Another 2000-rupee notewas brought into the monetary system as high-esteem cash. New notes of 500 and 1000 rupees were likewise dischargedin the market in the consequent days.

The total currency available for use in India was Rs. 17.77 lakh crore (US$260 billion). The Indian government reported a prompt prohibition on two noteworthy bills that record for most by far of all currency available for use. Indianswere given approximately two months' time to replace/ change those notes for different bills, including recently printedones. The demonetization has resulted in paving the way of new trend in the transaction, i.e. online shopping and digital payments and implications on the rural consumer.

The reasons behind demonetization, according to the Government were to control black money and to give a boostto digitalization of banking and financial services. Impact of demonetization can be seen in terms of digital wallets and its suppliers, customers, and the market prepared for mass selection of advanced wallets. The demonetization has been instrumental in increasingthe transaction volumes of online bank transactions, e-clearing, e-KYC etc.

Digitalisation

Digitalisation is transforming the financial services industry and the way that consumers interact withfinancial products and service providers, driven by rapidly expanding mobile technologies,

IJBARR
E- ISSN -2347-856X
ISSN -2348-0653

enhanced dataprocessing and analytical capabilities and increased connectivity between smart devices and financialservices platforms and applications.Digitalisation in the form of technological innovation is having an ongoing transformative impact onsocieties and economies. In relation to financial services, digitalisation has significantly affected all sectorsranging from payments to banking and saving to insurance to investing, with the emergence of many newproducts, services, distribution models by existing market players and new entrants such as tech-companies both large and small.

The benefits of digitalisation for financial consumers are significant. They have the potential to support greater access to financial products and services thereby supportingfinancial inclusion. Digitalisation also acts as a spur for competition by expanding the range of providersvia new entrants, contributing to increasing efficiency of operations of financial services providers andfacilitating comparison shopping and switching of products.

There are also new risks to consumers associated with digitalisation specific to the financial services sectorwhich need to be monitored and addressed. Such risks include new forms of theft or fraud perpetratedonline, data breaches and digital security incidents, excessive data profiling leading to financial exclusion,lack of privacy and manipulation of consumers' behavioural biases when operating online. Moreover, thenature of digital security risk is extremely dynamic, with the continuous appearance of new threats andidentification of new vulnerabilities.In this increasingly digital environment and faced with these new and evolving risks, the need for effectivefinancial consumer protection, including data protection, is more important than ever. The policies andapproaches developed and adopted by financial consumer protection policy makers and oversight bodiesneed to evolve and adapt in line with the digital environment.

Digital Financial Services

Digital financial services (DFS) can be defined as financial operations using digital technology, including electronic money, mobile financial services, online financial services, i-teller and branchless banking, whether through bank or non-bank institutions. DFS can encompass various monetary transactions such as depositing, withdrawing, sending and receiving money, as well as other financial products and services including payment, credit, saving, pensions and insurance. DFS can also include non-transactional services, such as viewing personal financial information through digital devices. (OECD, 2017).

Digital financial inclusion in times of covid-19

The adverse effects of the COVID-19 pandemic aretrickling down to major sectors of the Indianeconomy,with manufacturing, auto, retail, aviation and hospitalitybearing the brunt of the lockdown. This in turn has affectedfast-growing digital payments which are closely linked to these sectors. Shut shops, travel bans andreduced discretionary spends by consumers (on diningout, movies and entertainment and so on) are furthernegatively impacting digital payments.Digital payment volume declines are seen in airlines,tourism, hospitality, hotels, entertainment, e-commerce(non-essentials) and restaurants, among other sectors.Further, cross-border payments, be they B2B or C2B,have significantly declined owing to the temporary shuttingdown of borders further, resulting in restricted movementof goods. International remittances too have been affectedand have reduced.

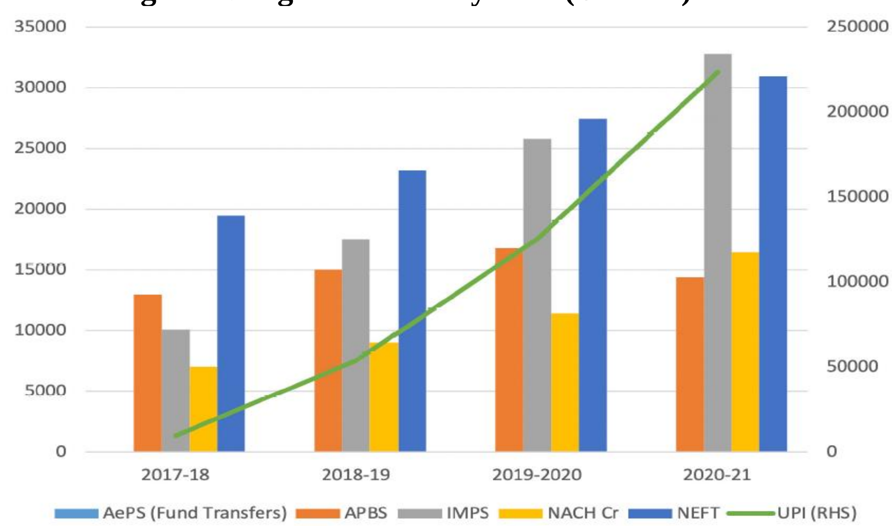
However, there are also a few areas that are seeing anuptick in digital payments by way of increased adoptionduring the lockdown. These include online grocerystores, online pharmacies, OTT players (telecom andmedia), EdTechs, online gaming, recharges and utility/billpayments.Digital payment volumes are also receiving a boost throughthe Government, which has pledged monetary assistanceto the poor via direct transfers to bank accounts.The finance minister and the CEO of the NationalPayments Corporation of India have also urged peopleto increase the use of digital payments in order to makepayments contactless.Digital payments, once a convenience, have become anecessity in these times. With a majority of the sectors thatcontribute to digital payments still in a state of flux, it is stilltoo early to ascertain the long-term impact of COVID-19 ondigital payments.

As per the BRICS Digital Financial Inclusion Report, 2021, published by the Reserve Bank of India, the COVID-19 pandemic and the consequent restrictions imposed to curb its spread, necessitated implementation of a host of measures to ensure smooth functioning and continuous availability of not only the RBI-operated centralised payment systems, but also the payment systems operated by other Payment System Operators (PSOs).

The following measures were undertaken in India:

1. The Real Time Gross Settlement (RTGS) and the National Electronic Funds Transfer (NEFT) systems became operational on a 24x7x365 basis from December 2020 and December 2019, respectively.
2. The RBI engaged in constant discussions with the National Payments Corporation of India (NPCI) and other authorised PSOs to ensure uninterrupted operations of all payment systems. The PSOs and their services were declared as ‘essential services’ and allowed to work even under the lockdown protocols. NPCI fast-tracked the onboarding system on UPI or UPI-QR to make it totally contactless and fully online.
3. The Government’s Direct Benefit Transfer (DBT) payments of the government welfare transfers were facilitated by the National Automated Clearing House (NACH) – Aadhaar Payment Bridge System (APBS), wherein bulk transfers are made to individuals based on the beneficiary Aadhaar number. Consequently, Aadhaar based cash withdrawals at micro-ATMs and Business Correspondents using Aadhaar enabled Payment System (AePS) have also witnessed an increase in transactions (Figure 1). To promote digital payments, banks have temporarily waived fund transfer charges on their digital platforms such as NEFT, RTGS and IMPS.

Figure 1: Digital Retail Payment (Volume) - India



Source: BRICS Digital Financial Inclusion Report, RBI, 2021

The RBI had issued guidelines to enhance public awareness about the availability of various digital payments modes that could be used from home while maintaining social distancing. As a part of financial awareness drive, during July 2020-March 2021, 178 e-BAAT (electronic Banking Awareness and Training) programmes were conducted on electronic payment systems, covering both their benefits and issues related to cyber security. Further, stakeholders in the payment ecosystem, including the RBI, have been releasing advertisements promoting the use of digital payments.

4. As regards contactless card payments using NFC-enabled EMV Chip cards, the RBI had increased the per transaction limit from INR 2,000/- to INR 5,000/- for relaxation of PIN requirement at the time of performing the transaction. Transactions above this value can be done in contactless mode, but with PIN entry. This measure was taken to make the card payments at PoS terminals safer from health point of view.

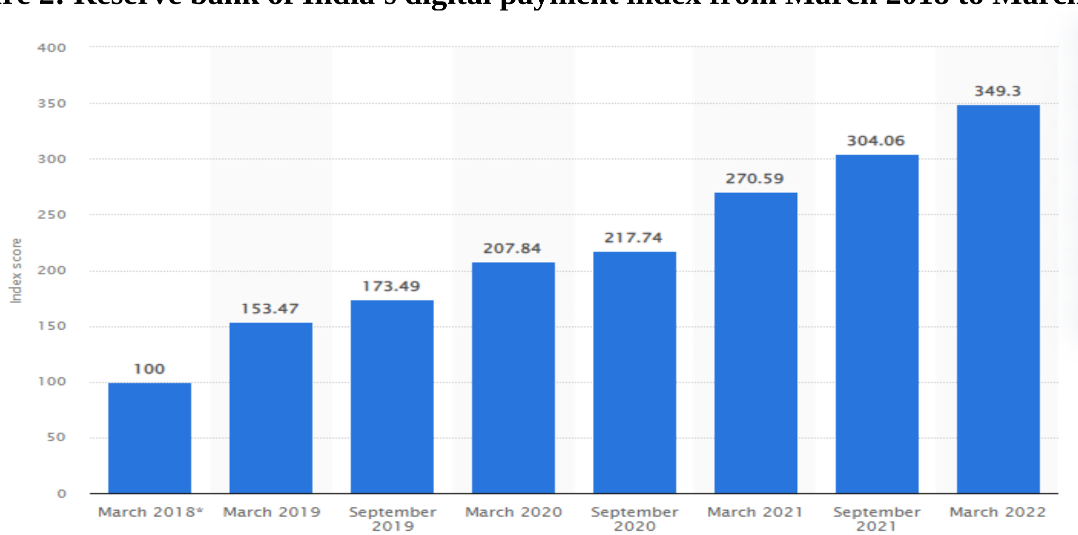
5. The Money Transfer Service Scheme (MTSS) operators ensured that inbound remittances were paid to the beneficiaries without any delay and also encouraged their customers to receive remittances in their bank accounts to avoid issues/ difficulties in cash pay-out.

6. “Digital KYC” and “Equivalent e-Documents”, and video verification were facilitated through simplified and flexible procedures.

7. To increase customers’ convenience, facility of cash withdrawal from full-KYC PPIs issued by non-banks were allowed (April 2021).

8. The RBI developed the Digital Payments Index (DPI), to measure the diffusion and deepening of digital payments through five broad parameters, viz., Payment Enablers, Payment Infrastructure – Demand side Factors, Payment Infrastructure - Supply-side Factors, Payment Performance, and Consumer Centricity (Figure 2).

Figure 2: Reserve bank of India's digital payment index from March 2018 to March 2022



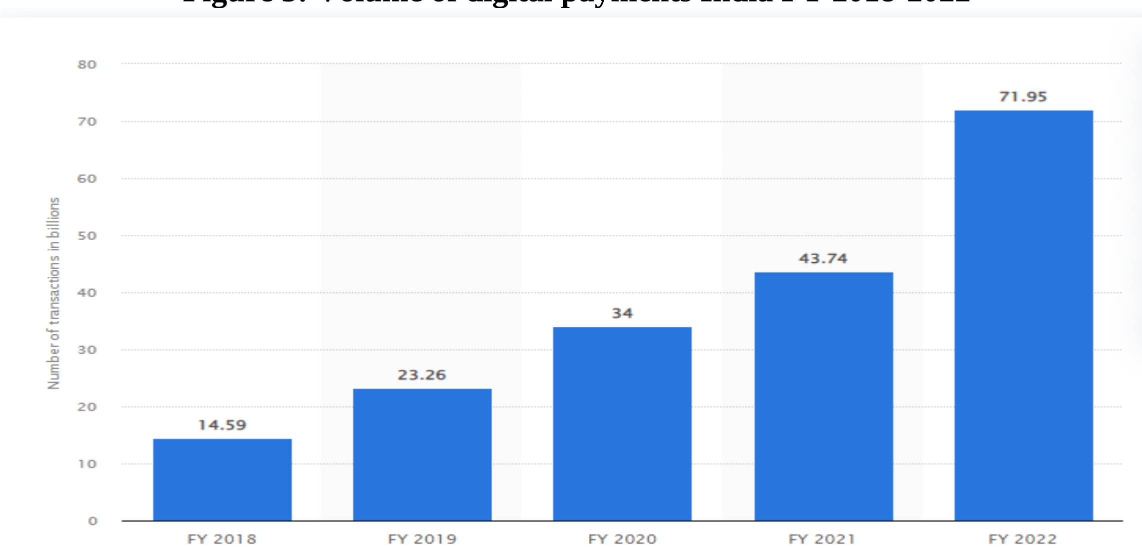
Source: https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=53123#

As of March 2022, the Reserve Bank of India's digital payment index stood at 349.3 as compared to 304.06 in September 2021. The RBI-DPI index has shown consistent growth since its inception in 2018, which is used as the base year for calculation.

The growth of digital payment infrastructure in the country was both a consequence and a need of the hour following demonetization. RBI and the National Payments Corporation of India (NPCI) fostered a varied digital payment ecosystem in the country catering to the large and diverse population.

Consequently, the country's digital payment landscape multiplied manifold times in the last years.Noteworthy is the expansion of the United Payment Interface which witnessed a transaction volume of 45 billion in 2022. RBI intends to explore the future of digital money in the form of central bank digital currency (CBDC). Three new digital payment initiatives namely RuPay Credit card on UPI, UPI Lite, and Bharat BillPay Cross-Border Bill Payments were also recently launched by RBI at Global Fintech Fest 2022.

Figure 3: Volume of digital payments India FY 2018-2022

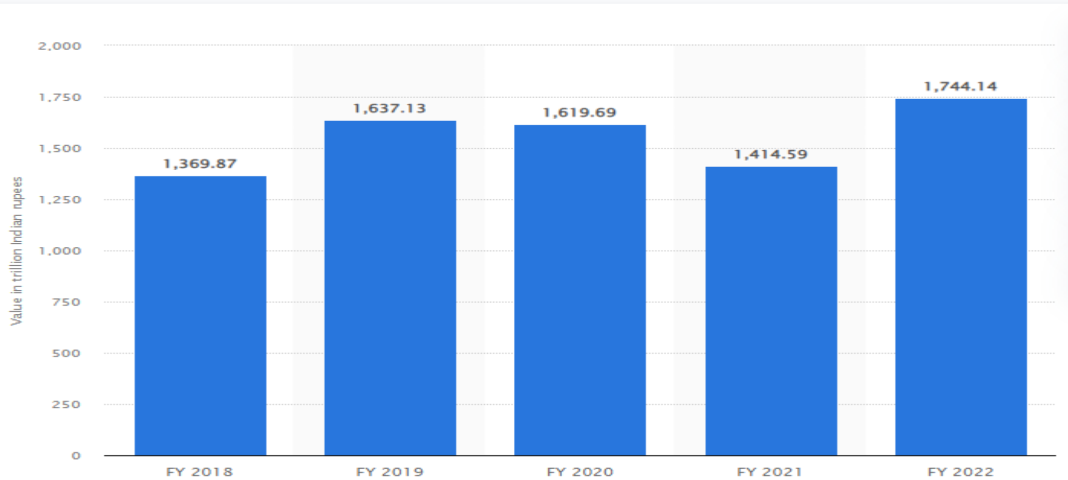


Source: https://www.statista.com/statistics/1251321/india-total-volume-of-digital-payments/

In financial year 2022, around 71 billion digital payments were recorded across India. This was a significant increase compared to the previous three years.The total value of digital payments included large-scale interbank payments, such as Real Time Gross Settlement (RTGS) or National Electronic Funds Transfer (NEFT), as well as payments used by individuals, such as credit and debit cards. India's mobile payment system, Unified Payments Interface (UPI), recorded strong gains, both in numbers and in value, since 2015. Thereby, it comes as no surprise that international key players, such as Google Pay or Amazon Pay, entered the market. Nevertheless, the most used app in 2021 was domestic app PhonePe.

Since the beginning of the COVID-19 pandemic in India the number of digital payment transactions continued to grow. This was also true for the various methods of credit and debit transfers, including mobile payments through UPI. Nevertheless, the value of card payments and of large value credit transfers, such as RTGS, decreased considerably in financial year 2021.

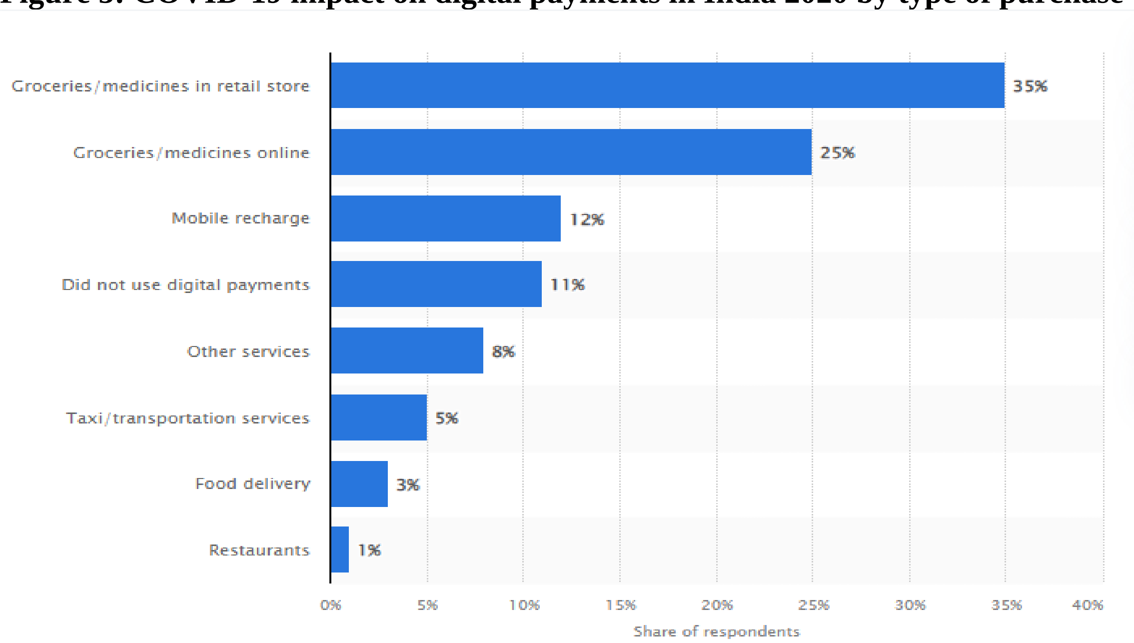
Figure 4: Value of digital payments India FY 2018-2022



Source: https://www.statista.com/statistics/1251319/india-total-value-of-digital-payments/

In financial year 2022, digital payments in India amounted to over 1.7 quadrillion Indian rupees in total. This was an increase compared to the previous two years, when the total value stood above 1.4 quadrillion rupees, respectively.The total value of digital payments included large-scale interbank payments, such as RTGS or NEFT, as well as payments used by individuals, such as credit and debit cards, or UPI transactions.

Figure 5: COVID-19 impact on digital payments in India 2020 by type of purchase



Source: https://www.statista.com/statistics/1111084/india-coronavirus-impact-on-digital-payment-purchases/.

According to the results of a survey among Indians on the impact of the coronavirus (COVID-19) and its consequent lockdown, a majority of respondents reported using digital payments to purchase groceries,

IJBARR
E- ISSN -2347-856X
ISSN -2348-0653

medicines and other essentials. This had a higher share at retail stores than online.India went into lockdown on March 25, 2020, the largest in the world, restricting 1.3 billion people, extended until May 3, 2020.

Conclusion

The COVID-19 pandemic has enhanced the focus on all aspects of digital financial inclusion. There has been accelerated use of the digital financial services mainly due to the relaxations and innovative approach adopted by the authorities, private players adopting the remote business and payment models and increase in first-time consumers due to lockdown and social distancing protocols. While these are encouraging developments, the challenges of bridging the digital divide have got amplified. The risk of cyber incidents, online frauds, illicit financial flows and data privacy have come to the fore with increase in customer uptake as most of these technologies and platforms are relatively new and evolving. As the countries emerge from the pandemic, the digital financial system will have a crucial role to fulfil the aspirations and needs of our economies recovering from the pandemic. At the same time, these new technologies must be designed and implemented with adequate safeguards so as not to exacerbate the risk of further marginalising the excluded section. Going ahead, the authorities have to focus on a robust and safe architecture to strengthen the trust of the stakeholders which will help in broadening the coverage and impact of digital financial inclusion.

The increased usage of digital payment systems facilitated financial transactions during the COVID-19 pandemic and the subsequent lockdowns, social distancing and no-contact protocols. There was a 42 percent increase in global cashless payments (PwC study, 2021) Furthermore, there was a cross-generational shift to digital channels with older people (56 years and above) increasingly accessing digital payment modes during this period (World Payments Report, 2020). The private sector, especially small businesses, increased their presence online and gave an impetus to the digitalisation of payments. The private players are also spearheading innovation in the retail digital payment space and fostering financial inclusion. These increased retail transactions along with the digital direct transfer of COVID-19 related social benefits from government to individuals and MSMEs, expanded the ambit of financial inclusion.

Given the increasingly digital environment for financial products and services, now further accelerated by responses to the COVID-19 pandemic, and the potential for digitalisation to support greater financial inclusion and inclusive growth, effective financial consumer protection is more important than ever. It is equally important that the policies and approaches developed and adopted by financial consumer protection authorities evolve and adapt in line with the changing environment.

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IJBARR
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