



Article

# Reassessing Financial Inclusion through the Lens of Neo-banking Innovations

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**Abstract:** The digital transformation of the financial sector has brought neobanks to the forefront as innovative intermediaries that extend financial services through digital platforms. The article examines the emergence of neobanks in the financial ecosystem of Indian regulatory framework. Neobanks are digital-only financial institutions without physical branches and it is rapidly expanded due to innovative technology, changing consumer preferences and regulatory shifts. The paper explores how neo banks contribute to financial inclusion aim of achieve the SDG goals of sustainable development of nations. The study finds that neobanks enhance accessibility, affordability and customer-centric design. But regulatory constraints limit their inclusive potential, underscoring the need for policy reforms that balance innovation with consumer protection. The qualitative methodology is used to understand the role of neo banks in financial inclusion in the context of India. As the traditional banking model in comparison to neo banking model is less customer-centric. The study support neo banking model for higher growth rate which can be apparent in financial inclusion index.

**Keywords:** Neo banks, financial inclusion, customer-centric design, consumer protection.

## INTRODUCTION

Financial inclusion has been recognized as cornerstone of inclusive economic development in India. The Sustainable Goals of the United Nations are aligned with the goal of the Reserve Bank of India, with the quoted slogan “*Innovate for Progress, Build for Tomorrow.*” The goal's essence is to create infrastructure, innovation and industry. The Reserve Bank of India first discussed the concept of financial inclusion in 2005 (Toshniwal R. et.al,2024). The concept of financial inclusion enables businesses to eradicate unemployment in both rural and urban areas. The economic resources are accessible primarily to the population, therefore, pursuing Financial Inclusion (FI) is necessary for poverty eradication and overall development of nation (Bhattacharyya A and Khan M,2021). Financial

inclusion entails that individuals and enterprises have access to as well as effectively utilise a range of affordable financial services-including payments, saving, credit, insurance and transactional facilities-that are delivered responsibly and sustainably. Therefore, the urgency of the introduction of neo banks in the financial ecosystem as a fully licensed banks is the highest need. Such access is fundamental to enabling individuals to manage economic risks, accumulate wealth and invest in productive activities. As a key facilitator, financial inclusion significantly contributes to the achievement of seven out of the seventeen Sustainable Development Goals by fostering inclusive economic growth, generating employment, advancing the economic empowerment of women and playing a crucial role in the eradication

of poverty (World Bank Group, 2025).

The Financial Inclusion Support Framework (FISF), launched by the World Bank Group in April 2013, aimed to enhance the scale and effectiveness of country-led financial inclusion reforms. Supported by \$25 million from the Netherlands Ministry of Foreign Affairs and \$6.7 million from the Bill & Melinda Gates Foundation, FISF facilitated technical assistance, policy dialogue and knowledge sharing across several low- and middle-income countries. Its objective included promoting access to and usage of financial services such as payments, credit, insurance and savings, particularly among low-income individuals and micro, small and medium-sized enterprises (World Bank Group, 2022).

FISF had two core components: Country Support Programs (CSPs) and a Knowledge Agenda. CSPs, implemented in eight countries (e.g., Rwanda, Indonesia), support national financial inclusion strategies, infrastructure development, diversified services and consumer protection. Key outcomes included the adoption of financial regulations, expansion of financial education initiatives and strengthening of institutional capacities. This programs by United Nation were concluded by June 2020. The Knowledge Agenda addressed cross-cutting themes such as digital finance, women's financial inclusion, agricultural finance, consumer protection and the use of data and technology. Numerous reports, policy notes and learning events disseminated evidence-based insights, including innovations in retail payments; therefore, the role of smart contracts and strategies to mitigate risks in digital finance. Overall, FISF contributed to deepening the financial inclusion ecosystems by aligning national strategies, enabling digital infrastructure and generating global knowledge relevant for policymakers and practitioners (World Bank Group, 2022).

Therefore, FISF played a critical role in advancing financial inclusion by supporting policy reform, digital innovation, institutional capacity building and knowledge dissemination. Its targeted interventions directly contributed to several sustainable development goals (SDGs), including poverty reduction (SDG 1), Gender equality (SDG 5), decent work and economic growth (SDG 8), and reduced inequalities (SDG 10). Furthermore, by promoting responsible finance, transparency, and equitable access, FISF aligns with the core principles of Corporate Social Responsibility (CSR), encouraging both public and private sector actors to integrate inclusive and ethical practices into their operations, thereby fostering long-term sustainable development.

Therefore, neo banks can play a significant role as the key promise of the neo banking ecosystem. It will simplified onboarding, low-cost and customer-centric digital platforms. In the Indian context, where smartphone penetration and digital payment gateways has opened the infrastructure mechanism for neo banking. Under which neobanks can be used as an advance financial inclusion tool for Indian population which is vastly expanded from high mountains to plain areas. The research article demonstrates the importance of neo banking in the Indian financial ecosystem for the purpose of financial inclusion of the population. Under which, (SDG) Sustainable Development Goal can be achieved at a large scale.

### RESEARCH QUESTION

The research question is *how do neobanks contribute to financial inclusion in India, particularly underserved populations.*

### RESEARCH GAP

The research gap is marked, as financial inclusion is multidimensional including usage, stability and financial capability. However traditional banking model does not fully support all the requirements of financial inclusion. However, neo banks have capability to overcome this gap. But due to uncertainty in regulatory mechanism, the potential of the neo banking model is not visible as it should be.

### RESEARCH METHODOLOGY

To resolve the research question, the study adopts a doctrinal and qualitative legal research methodology, supplemented by policy analysis and comparative insights. The research is primarily analytical in nature and examine legal texts, regulatory documents, policy reports and academic literature to assess the role of neobanks in financial inclusion.

The methodology is appropriate because neobanks in India operate within a regulatory grey area where statutory interpretation and regulatory intent are central to understanding their impact. The data is divided into two category primary and secondary data. The primary source of the research article is statute and regulations-Reserve Bank of India Act, 1934, Banking Regulation Act, 1949 and regulatory instruments of RBI circulars, master directions and guidelines on digital lending, fintech partnerships, KYC norms and payment systems. The other official reports are also used as source of primary data. The secondary source of data is peer-reviewed journal articles on financial inclusion and neo banks. The reports published by World Bank, Basel Committee on Banking Supervision. Other industrial reports (PwC) used for contextual understanding of the matter.

## DISCUSSION

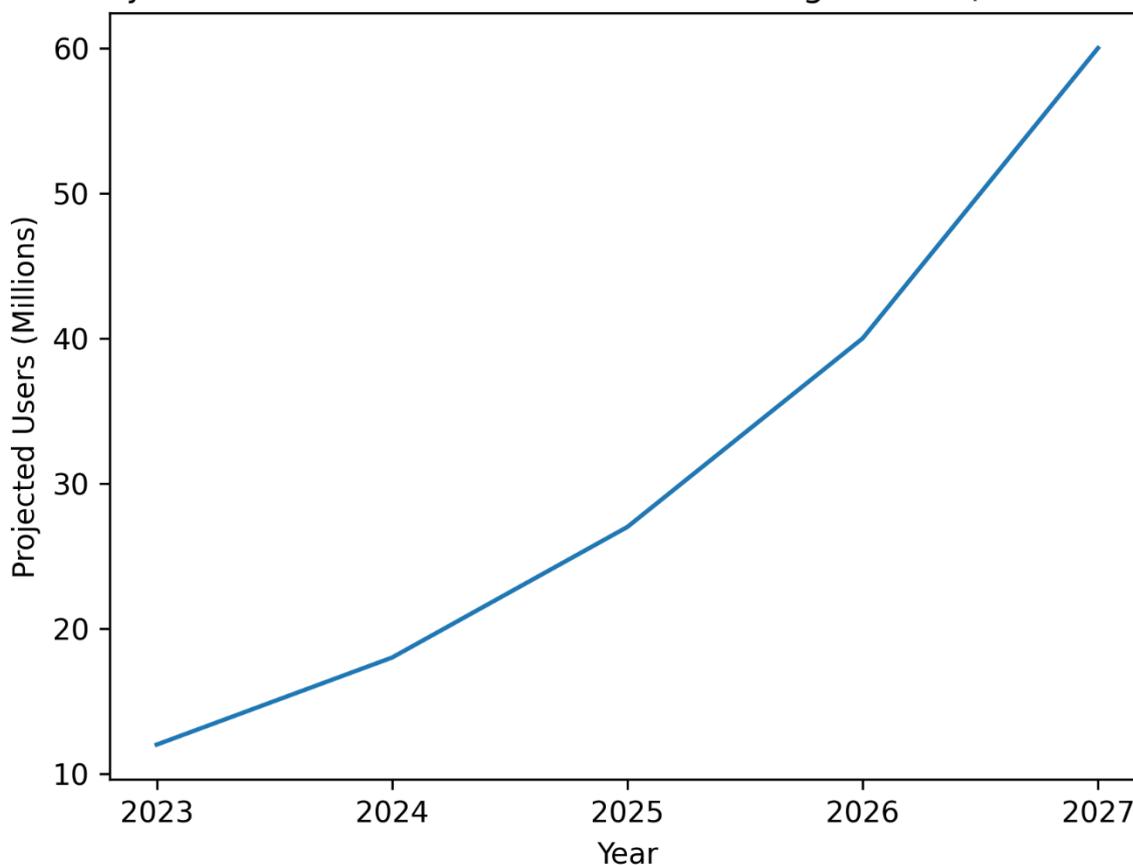
### Conceptual Framework: Neobanks in India and its role in Financial Inclusion

#### Defining Neobanks

Neo-banks are technology driven financial service providers that deliver banking services primarily through mobile applications and digital platforms. In India, neobanks do not possess independent banking licenses and are prohibited from accepting deposits directly (PwC,2021). Instead, they operate through partnerships with licensed banks or non-banking financial companies (NBFCs). This partnership-based model differentiates Indian neo-banks from fully licensed digital banks operating in jurisdictions such as the United Kingdom and Singapore. The neo banking service can be leveraged by mobile applications, digital payment, cloud computing and data analytics as neo banks streamlined financial services by instant payment account opening, budgeting tools and real-time transaction monitoring thereby redefining traditional banking experiences (Birla & Arya, 2025). They provide 100% digital financial banks that provide financial services through web platforms. They do not have physical branches, they free from brick-motor system. They

built their infrastructure on modern technologies like cloud computing, Application Process Interface (API) and Artificial Intelligence, which ease them to deliver a highly personalized and efficient user experience. As in India neo banks are not licensed by Reserve Bank of India to function as full fledge banks. Therefore, they become partner with the licensed commercial banks or NBFCs and private banks as third -party service provider. But they providing regulated services such as account opening, salary account opening, savings, payments, transaction of money and loans. They are front-end service providers (UnPay, 2024). The leading neo-banks in India are RazorpayX, NuBank, Instant Pay, Fampay, Jupiter, NiyoX, Kotak 811. The figure shows the projected growth of Indian Neobanks. At the Compound Annual Growth Rate of 50% through 2025 (Nileshkumar Kailashbha R., 2025). As Neo-banking helps customers to implement there tasks more efficiently as comparison with traditional banking. The productivity of the customer is enhanced by using neo-banking apps (Venkatesh *et al* 2003), (Bhatnagr P. and Rajesh A. 2023).

Projected Growth of the Indian Neobanking Market (50% CAGR)



(Source: author)

#### Definition of Traditional Banks

Traditional banks operate through physical branch

networks and are subject to comprehensive prudential regulation under RBI Act, 1934, Banking

Regulation Act, 1949. In Indian legal framework, traditional banks refer to banking institutions that are licensed, regulated and supervised by Reserve Bank of India and that conduct banking business through physical branch- based infrastructure in addition to digital channels.

#### Definition under the Banking Regulation Act, 1949

The Banking Regulation Act, 1949 provides the statutory foundation for traditional banking in India. Under section 5(b) of the Banking Regulation Act, 1949:

*“Banking means the accepting, for the purpose of lending or investment, of deposits of money from the public, repayable on demand or otherwise and withdrawable by cheque, draft, order or otherwise.”*

Traditional banks are intuitions that legally engage in this activity of “banking” as defined under the Act.

Further, section 5(c) defines a “banking company” as: *Any company which transacts the business of banking in India.*

Traditional banks public sector banks, private sector banks or foreign banks operating in India fall squarely within this definition as they are authorized to accept public deposits and extend credit.

Crucially, section 22 of the Banking Regulation Act,1949 mandates that:

*“no company shall carry on banking business in India unless it holds a license issued by the Reserve Bank of India.”*

This licensing requirement distinguishes traditional banks from neobanks and fintech entities, which do not possess independent banking licenses.

#### Under Reserve Bank of India Act, 1934

The Reserve bank of India Act, 1934 establishes the RBI as India’s central banking authority and confers extensive supervisory powers over traditional banks. Under section 3 the RBI is constituted as the central bank responsible for regulating the issue of banknotes and maintaining stability.

More specifically, section 21 and 35A of the RBI Act,1934 empower the RBI to:

- Control advances by banking companies
- Issue binding directions in public interest
- Regulate banking policy to ensure financial stability

Traditional banks are subject to these statutory directions, including prudential norms, capital adequacy requirements and risk management obligations.

Therefore, the uncertainty at the initial stage of definition of neo banks and related services demonstrates the legal challenges. It is essential to bridge the gap which is apparently visible in the legislation. The consequences of the regulatory gaps are visible to financial stability of the nation.

## **Financial Inclusion in India: Legal and Policy Context**

Role of neo banks in advancing financial inclusion, in India the hurdles of financial inclusion are geographic inaccessibility of bank branches, high cost of serving low-income customers and documentation KYC barriers as well as low financial literacy and trust deficits. While Indian government made initiatives such as Jan-Dhan-Aadhaar- Mobile trinity which supported the system of account ownership, international and domestic indicators show that usage, credit access and service quality gaps persist. This unmet demand creates space for technology-driven banking models including neo-banks. There are regulatory limitations on neo-banks, but still, they are playing functional role in comparison to formal banking model. According to an official press release by the Press Information Bureau, Government of India, the Reserve Bank of India’s Financial Inclusion Index (FI-Index) a consolidated measure of access, usage and quality of financial services across sectors rose to 67.0 in 2025 up from 64.2 in March 2024 (Government of India Press Information Bureau, 2025).

## **Regulatory framework governing neobanks in India**

Neo-banks are not licensed banks in India. In the Indian regulatory framework, they are function as digital financial service platforms and operating in partnership with RBI-regulated banks and NBFCs. They are offering banking like services without holding deposits. Indirectly, it shaped by Banking Regulation Act, 1949, RBI Act,1934, Payment and Settlement Systems Act, 2007, RBI Digital Lending Guidelines, 2022 (Reserve Bank of India, 2023). Despite regulatory limitations, neo-banks play a significant role in inclusion rather than a formal banking role. But they are highly vulnerable for the digital financial fraud ecosystem.

## **Role of Neobanks in Financial Inclusion**

Neo-banks reduce entry barriers to financial services by enhancing digital access and simplified onboarding of financial activities. It will enabling fully digital onboarding using e-KYC and offering app-based interfaces in local languages. The model of neo banks system will be particularly relevant in semi-urban and rural areas. Migrant populations and young- first time users will easily approach the financial ecosystem. Neo-banks enable account opening through digital KYC processes, reducing the need for physical documentation and branch visits. This significantly lowers entry barriers for individuals in rural and semi-urban areas. By lowering transaction and onboarding costs, neo-banks help extend services to populations traditionally considered economically unviable by brick-and-mortar banks or traditional banks. The

cost reduction and affordability are also the key feature of neo banking ecosystem. By eliminating physical infrastructure, neobanks reduce operational costs and offer low-free or zero- balance accounts. This affordability is particularly relevant for low-income users who are sensitive to banking charges.

Neo banking will serve the underserved segment of the population. Neo banks increasingly target micro, small and medium enterprises (MSMEs), freelancers and gig workers segments which are often excluded from traditional banking order. By using alternative data and digital transaction histories neobanks facilitate access to credit for these groups. Neo-banks represent more than a technological shift in cross-border finance, they embody a structural opportunity

to reduce remittance costs, curb reliance on informal channels and advance meaningful financial inclusion among migrant committees. By lowering transaction fees, enhancing digital accessibility and aligning with global targets such as SDG 10C, neo-banks have the potential to transform remittances from a costly necessity into a vehicle of economic resilience and empowerment provided that issues of trust, digital literacy, regulatory balance and infrastructural access (Badre, A. 2024). Countries like Chile, Brazil and Mexico where neo banks are webbing the network for bridging the gap between digital accounts, microloans and financial education to those who are excluded in traditional financial model (Abbott, et al.,2021, Paslar, A., & Cobzari, L.,2025).

### Role of Neo-Banks in Advancing Financial Inclusion in India



(Source: author)

### Challenges and Limitation

The absence of regulatory framework is deviating neo banking path and being misused by con-artist. The lack of legal framework for neobanks creates uncertainty regarding liability, consumer protection and supervisory oversight. Data localization requirements and cybersecurity obligations further complicate compliance. In the state-of-art, ambiguity regarding the legal obligation of neo banks, data protection and grievance redressal create unclear situation and confusion. Customers are not sure, whether responsibility lie with the neo banks or its partner bank, raising concern under consumer protection law. The Basel committee reported under his report titled digitalisation of finance, highlights

the capacity building and coordination in implication of digitalisation. As per the report it is important for banks and supervisors to sufficient staff and resources with all the required capabilities and handful knowledge and skills to mitigate the risk and assess the new technologies for this business models. Digitalisation has increased the issue of prudential supervision therefore coordination and communication between the authorities across the jurisdiction are important to address the considerations (Basel committee on Banking Supervision, May 2024).

### CONCLUSION

Neobanks represent a significant innovation within India's financial ecosystem and offer promising

avenues for advancing financial inclusion. By leveraging digital infrastructure and customer-centric design, they address several structural limitations of traditional banking. However, regulatory ambiguity and consumer protection concerns limit their effectiveness. A balanced regulatory framework that promotes innovation while safeguarding public interest is essential for realizing the inclusive potential of neobanks in India. To increase the inclusive potential of neobanks following measures are recommended introduction of a tiered or restricted digital banking license, clear allocation of consumer liability and grievance mechanisms, strengthening digital financial literacy programs and integration of neobanks into financial inclusion strategies and enhanced supervision of partnership-based fintech models.

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