

Evolution And Functional Framework of Small Finance Banks in India: A Comprehensive Analysis

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Abstract- Small Finance Banks (SFBs) represent a noteworthy advancement in India's banking and financial landscape, with the goal of enhancing financial inclusion and serving the neglected segments of society, such as small enterprises, marginal farmers, and economically disadvantaged households. This paper investigates the development of SFBs in India, tracking their origins from the suggestions of the Nachiket Mor Committee (2014) to the issuance of licenses by the Reserve Bank of India (RBI) in 2015. The study examines the operational framework governing SFBs, concentrating on their regulatory stipulations, operational protocols, range of services, and target clientele. Additionally, the paper underscores how SFBs serve as a link between conventional banking offerings and the financial demands of the unbanked population. By assessing their financial performance, outreach, and societal impact, the study offers perspectives on the role of SFBs in promoting inclusive growth. The paper also discusses the obstacles these banks encounter, including limited geographical coverage, compliance expenses, and competition from other financial entities. In conclusion, it highlights the future prospects of SFBs in reinforcing India's banking system through inclusive, technology-driven, and sustainable financial solutions.

Keywords: Financial Inclusion, Banking Sector Reforms, Functional Framework, SFB Evolution

1. INTRODUCTION

The Indian financial system has experienced a remarkable transformation over the years, especially in its initiatives to promote financial inclusion and ensure that banking services are accessible to all segments of society. Among the various policy advancements, the establishment of Small Finance Banks (SFBs) represents a crucial milestone toward achieving inclusive development. These banks were

designed to cater to the needs of the underserved and unbanked populations, such as small and marginal farmers, micro and small enterprises, and low-income individuals. The Nachiket Mor Committee's recommendations in 2014 prompted the Reserve Bank of India (RBI) to issue guidelines and later grant licenses to certain entities to function as SFBs in 2015. SFBs are required to concentrate on priority sector lending and operate under a structure that balances social impact with financial viability. They operate similarly to commercial banks but place a strong focus on rural outreach, small loan offerings, and attracting deposits from unbanked communities. Their contribution to empowering grassroots-level financial access has been vital, particularly in remote and rural areas. This paper explores the development and operational framework of SFBs, evaluating their contributions, compliance requirements, and the obstacles they encounter. Through an analysis of their growth and functional structure, the study highlights the significance of SFBs in India's banking and economic environment.

2. REVIEW OF LITERATURE

Pritha Chaturvedi (2022): The Role of Small Finance Banks in Promoting Financial Inclusion in India The article examines the role of Small Finance Banks (SFBs) in fostering financial inclusion in India. Established by the Reserve Bank of India in 2015, SFBs target unbanked populations and focus on micro, small, and medium enterprises. Key challenges include limited infrastructure and adapting to market changes, especially post-COVID-19. By utilizing technology and enhancing financial literacy, SFBs aim to provide accessible, affordable services. Their

continued development is crucial for improving economic growth and empowering marginalized communities throughout India.

Dr. Kanchan, Rakesh Choudhary (2022): Financial Performance Analysis using CAMEL Model with Special reference to Listed Small Finance Banks in India, The article highlights the crucial role of Small Finance Banks (SFBs) in promoting financial inclusion in India. Introduced by the Reserve Bank of India, SFBs serve unbanked populations and micro, small, and medium enterprises. Despite challenges such as infrastructure limitations and COVID-19 impacts, SFBs leverage technology to provide accessible financial services and drive economic growth in marginalized communities.

Monali Ray (2021): The article discusses the significance of Small Finance Banks (SFBs) in India, aimed at enhancing financial inclusion for underserved populations and micro, small, and medium enterprises. Established by the Reserve Bank of India, SFBs face challenges like infrastructure constraints and COVID-19 impacts but utilize technology to deliver accessible financial services, fostering economic growth and empowerment in marginalized communities.

3. OBJECTIVES OF THE STUDY

- a) To analyze the functional structure of SFBs, including their operational focus, lending practices, deposit mobilization, and customer base.
- b) To track the evolution of selected Small Finance Banks (SFBs) in India.
- c) To measure and analyze performance of SFBs in India and their role in financial inclusion

4. RESEARCH METHODOLOGY

4.1 Research design: Descriptive Research Design

4.2 Quantitative Approach: A quantitative research approach is adopted to assess the financial performance, lending patterns, and deposit mobilization of selected SFBs. The study involves numerical data collection and statistical analysis to draw meaningful conclusions.

4.3 Sample size: The study covers a sample of selected Small Finance Banks operating in India whose annual reports were available up to 31st March 2024. The banks included in the sample

are chosen based on the availability and accessibility of relevant data.

4.4 Statistical tools used for the study: Percentage Analysis, Comparative Analysis, Graphical Representation.

4.5 Data analysis and interpretation: The collected data has been systematically analyzed using secondary sources such as RBI publications and bank annual reports. Key performance indicators like Net Interest Margin (NIM), Credit-Deposit Ratio, and Capital Adequacy Ratio were studied and interpreted to evaluate the functional efficiency of SFBs.

4.5.1 Functional Structure of SFBs, including their operational focus, lending practices, deposit mobilization, and customer base.

The Reserve Bank of India, in its 2013 discussion paper on the "desirability and practicality of having small and localized banks as preferred vehicles for financial inclusion," emphasized the need for innovative strategies to integrate the poor into formal financial services.

In 2014, the Nachiket Mor Committee proposed two models of banking systems: the Horizontally Differentiated Banking System (HDBS) and the Vertically Differentiated Banking System (VDBS), with a focus on payments, deposits, and credit as foundational elements.

Subsequently, in November 2014, the RBI issued licensing guidelines for the establishment of Small Finance Banks (SFBs). The primary objective was to cater to the financial needs of low-income individuals and small business units. These banks aim to deepen financial inclusion by providing accessible avenues for savings and credit, especially for the unserved and underserved segments of society, leveraging advanced technology and cost-effective operations.

The core objective of Small Finance Banks (SFBs) is to provide essential banking services to the poor, marginalized communities, and their small-scale enterprises. As part of their mandate, SFBs are required to open at least 25% of their branches in unbanked rural areas and allocate 75% of their Adjusted Net Bank Credit (ANBC) towards priority sector lending.

4.5.2 Key features of Small Finance Banks include:

- They are authorized to accept all types of deposits, similar to regular commercial banks.

- SFBs are permitted to provide loans and advances.
- Prior approval from the RBI is mandatory for expanding their branch network during the first three years of operation.
- Their geographical scope is limited, with a focus on serving specific regions.
- The primary target customers are financially excluded individuals and micro and small enterprises.
- SFBs are not permitted to lend to large-scale industries or corporate.

4.5.3 Operational Focus of SFBs:

- Financial Inclusion:** SFBs aim to promote financial inclusion by providing essential banking services to individuals, small businesses, and rural populations.
- Microfinance:** They offer small loans to individuals and small businesses for income generation, agriculture, and other productive purposes.
- Small Business Lending:** SFBs provide credit to small business units, micro and small enterprises, and other entities in the unorganized sector.

- Targeted Sectors:** A significant portion of their lending portfolio is directed towards micro enterprises and those in the unorganized sector, often in rural and semi-urban areas.
- Technology and Low-Cost Operations:** They leverage technology to reduce costs and improve service accessibility, often using a low-cost, high-technology approach.
- Non-Risk-Sharing Services:** In addition to core banking, SFBs may also offer other non-risk-sharing financial services like insurance, pension products, and mutual funds.

4.5.4 The evolution of selected Small Finance Banks (SFBs) in India: The evolution of Small Finance Banks (SFBs) in India marks a significant shift towards financial inclusion, aimed at providing affordable banking services to underserved populations, particularly in rural and semi-urban areas. Established under the guidelines of the Reserve Bank of India (RBI) in 2015, SFBs have played a crucial role in promoting financial services such as savings, credit, and insurance to small businesses, farmers, and low-income households.

Table 1: Small Finance Bank Name, Established Year, Headquarter Location, Number of Branches (2016–2024)

S N	Bank Name	Establis hed Year	Head Quarter	No. of Branches								
				2016	2017	2018	2019	2020	2021	2022	2023	2024
1.		2015	Mumbai, Maharashtra	23	100	206	242	354	500	600	700	800
2.	Equitas Small Finance Bank	2016	Chennai, Tamil Nadu	412	520	632	752	856	861	964	1050	1150
3.	Capital Small Finance Bank	2016	Jaipur, Rajasthan	57	89	100	129	150	158	170	175	177
4.	Shivalik Small Finance Bank	2016	Shimla, Himachal Pradesh	DNA	DNA	DNA	DNA	DNA	46	46	129	129
5.	Utkarsh Small Finance Bank	2016	Varanasi – UttarPradesh	4	45	311	557	827	888	794	938	1082
6.	ESAF Small Finance Bank	2017	Thrissur, Kerala	0	284	400	622	622	700	753	760	756
7.	AU Small Finance Bank	2017	Jaipur, Rajasthan	DN A	403	474	474	406	919	1027	1049	2408
8.	Ujjivan Small Finance Bank	2017	Bengaluru, Karnataka	DNA	464	574	574	575	590	590	629	752
9.	Suryoday Small Finance Bank	2017	Navi Mumbai, Maharashtra	DNA	145	241	241	241	241	241	241	241
10.	Fincare Small Finance Bank	2017	Bengaluru, Karnataka	0	80	591	591	610	919	919	1231	DNA
11.	ESAF Small Finance Bank	2017	Thrissur, Kerala	0	284	400	622	622	700	753	760	756
12.	Jana Small Finance Bank	2018	Bengaluru, Karnataka	0	0	10	337	500	600	736	751	760
	Total			496	2414	3939	5141	5763	7122	7593	8413	9011

Note: The data for certain years is not readily available in the public domain.

This table provides data on the number of branches for various small finance banks in India from 2016 to

2024. The banks listed are IDFC First Bank, Equitas Small Finance Bank, Capital Small Finance Bank,

Shivalik Small Finance Bank, AU Small Finance Bank, Ujjivan Small Finance Bank, Suryoday Small Finance Bank, Fincare Small Finance Bank, ESAF Small Finance Bank, and Jana Small Finance Bank. The table shows the growth trajectory of each bank,

starting from their respective years of establishment, highlighting significant expansions in the number of branches across the years. Some banks, like AU Small Finance Bank, showed notable growth in the 2020s.

Chart 1: Total Branch Expansion of Small Finance Banks in India (2016–2024)

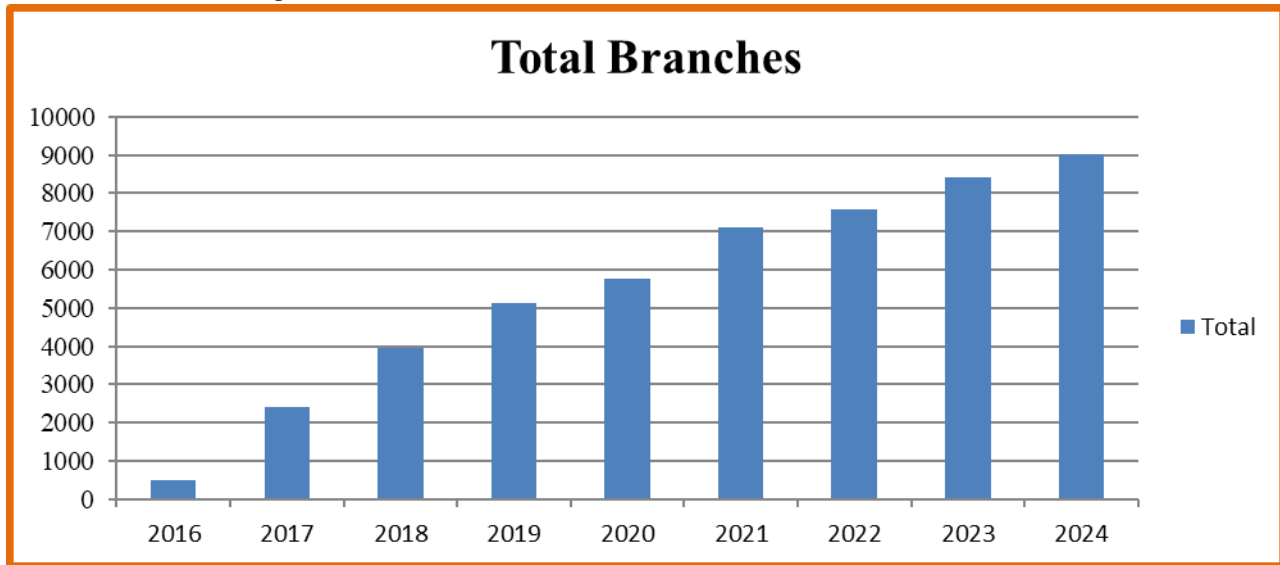


Table 2: Selected Small Finance Bank Deposit Details (2020–2024)

SN	Bank Name	Deposits in Rs. Cr.				
		2020	2021	2022	2023	2024
1.	Ujjivan Small Finance Bank	10,780	13,135	18,292	25,537	31,462
2.	Jana Small Finance Bank	9,651	12,316	13,536	16,334	22,571
3.	AU Small Finance Bank	26,163	35,979	52,584	69,364	87,182

Table 3: Trend Analysis of Deposits (Indexed to 2020 = 100)

SN	Bank Name	Trend Analysis of Deposits				
		2020	2021	2022	2023	2024
1.	Ujjivan Small Finance Bank	100	122	170	237	292
2.	Jana Small Finance Bank	100	128	140	169	234
3.	AU Small Finance Bank	100	138	201	265	333

Interpretation of Deposit Trends (2020–2024):

- AU Small Finance Bank shows the strongest growth trend among the three banks. Its index rose from 100 in 2020 to 333 in 2024, indicating a 233% increase in deposits. This consistent upward trend reflects strong customer confidence, effective deposit mobilization, and business expansion.
- Ujjivan Small Finance Bank also demonstrates a steady and significant increase, growing from 100

in 2020 to 292 in 2024. This indicates nearly threefold growth in deposits, highlighting recovery and stability in performance.

- Jana Small Finance Bank, while showing growth (from 100 to 234), reflects a comparatively moderate rise. The trend is slightly less steep, suggesting a slower pace of deposit growth relative to its peers.

Table 4: Selected Small Finance Bank Loans advanced Details (2020–2024)

SN	Bank Name	Loans advanced in Rs. Cr.				
		2020	2021	2022	2023	2024
1.	Ujjivan Small Finance Bank	14,043.64	14,493.95	16,303.17	21,289.66	26,882.92
2.	Jana Small Finance Bank	9,959.24	11,599.67	13,006.67	17,759.56	23,111.27
3.	AU Small Finance Bank	26,992.42	34,608.91	46,095.26	58,421.54	73,162.65

Table 5: Selected Small Finance Bank Loans advanced Details (2020–2024)

SN	Bank Name	Comparative Analysis of Loans advanced			
		2021 vs 2020	2022 vs 2021	2023 vs 2022	2024 vs 2023
1.	Ujjivan Small FinanceBank	3.81%	0.24%	48.15%	36.24%
2.	Jana Small Finance Bank	25.44%	9.17%	12.78%	30.49%
3.	AU Small Finance Bank	15.46%	19.64%	38.57%	28.52%

Chart 2: It is showing Comparative Analysis of loans Advanced (2020-2024)

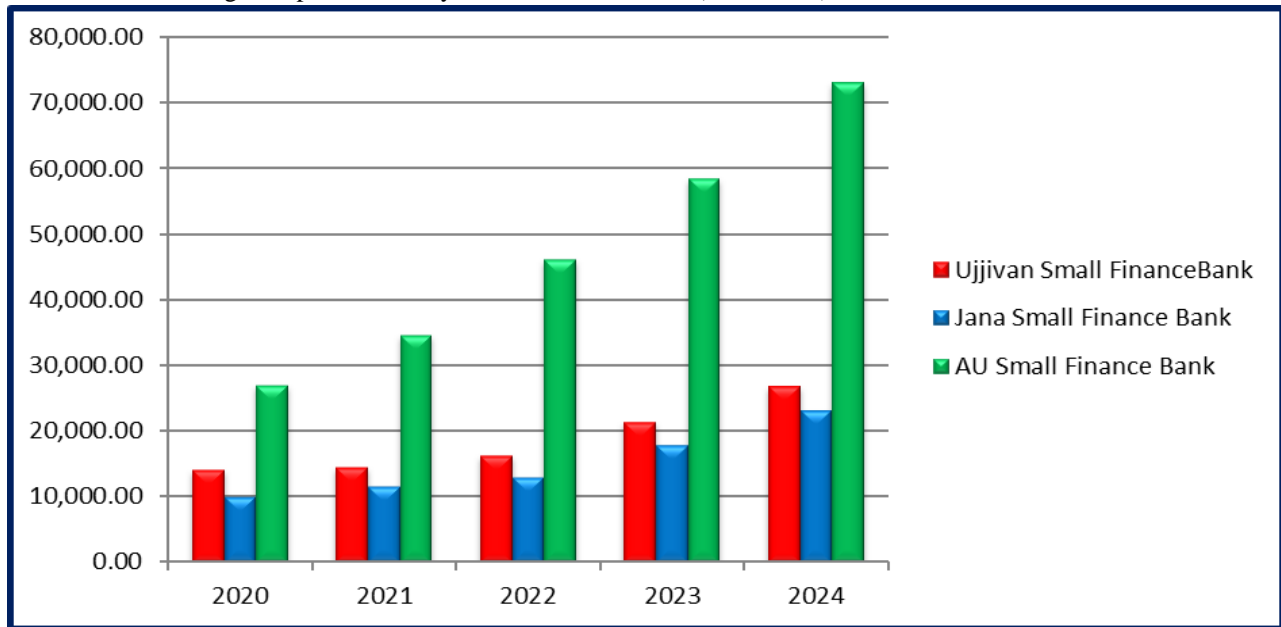


Table 6: Selected Small Finance Bank Income Details Details (2020–2024)

SN	Bank Name	Income Details in Rs. Cr.				
		2020	2021	2022	2023	2024
1.	Ujjivan Small Finance Bank	2,703.60	2,806.07	2,812.80	4,164.99	5,677.15
2.	Jana Small Finance Bank	1,991.52	2,497.73	2,726.54	3,075.01	4,013.05
3.	AU Small Finance Bank	4,285.88	4,950.05	5,921.73	8,205.41	10,554.71

Table 7: Selected Small Finance Bank Income Details (2020–2024)

SN	Bank Name	Statistical Tool on Income			
		Mean	Median	Std Deviation	CAGR
1.	Ujjivan Small Finance Bank	3,632.92	2,812.80	1292.467	20.86%
2.	Jana Small Finance Bank	2,860.77	2,726.54	754.8277	19.46%
3.	AU Small Finance Bank	6,783.56	5,921.73	2578.088	30.42%

Note: CAGR means Compound Annual Growth Rate (CAGR)

Interpretation:

A) Ujjivan Small Finance Bank

- Mean income is ₹3,632.92 Cr, showing a moderate overall income level across 5 years.
- Median income (₹2,812.80 Cr) is lower than the mean, suggesting income has grown significantly in later years, especially 2023 and 2024.
- Standard Deviation of ₹1,292.47 Cr indicates moderate fluctuations in income.

- A CAGR of 20.86% indicates a healthy growth rate, suggesting strong upward income momentum.

B) Jana Small Finance Bank

- Mean income is ₹2,860.77 Cr, the lowest among the three, showing a comparatively slower growth trajectory.
- Median is very close to the mean, indicating a consistent income trend with fewer fluctuations.

- Standard Deviation of ₹754.83 Cr is the lowest, reflecting more stable and predictable income patterns
- CAGR of 19.46% shows a steady but slower growth rate compared to peers

C) Jana Small Finance Bank

- Mean income is ₹6,783.56 Cr, the highest, indicating strong income performance overall.

- Median of ₹5,921.73 Cr supports this with consistently high income.
- Standard Deviation of ₹2,578.09 Cr is also the highest, which indicates significant year-on-year growth and fluctuations.
- CAGR of 30.42% is the most impressive, highlighting aggressive expansion and performance over the years

Table 8: Selected Small Finance Bank Key Performance Ratios (2020–2024)

SN	Bank Name	ROCE (%)					CASA (%)				
		2020	2021	2022	2023	2024	2020	2021	2022	2023	2024
1.	Ujjivan Small FinanceBank	3.55	4.12	2.58	4.58	4.48	13.53	20.55	27.29	26.41	26.69
2.	Jana Small Finance Bank	2.06	2.40	3.04	4.09	3.80	7.39	16.29	22.52	20.20	19.70
3.	AU Small Finance Bank	2.92	4.37	2.74	2.33	2.31	14.47	23.00	37.28	38.43	33.40

Table 9: Selected Small Finance Bank Trend Analysis of Key Performance Ratios (2020–2024)

SN	Bank Name	ROCE (%)					CASA (%)				
		2020	2021	2022	2023	2024	2020	2021	2022	2023	2024
•	Ujjivan Small FinanceBank	100	116.1	72.7	129.0	126.2	100	152	202	195	197
•	Jana Small Finance Bank	100	116.5	147.6	198.5	184.5	100	220	305	273	267
•	AU Small Finance Bank	100	149.7	93.8	79.8	79.1	100	159	258	266	231

Interpretation:

- Ujjivan shows moderate, stable growth in both metrics: ROCE improved to 126.2 and CASA to 197 by 2024. While not as aggressive as Jana in ROCE or AU in CASA, Ujjivan reflects balanced and consistent performance, suggesting steady growth and prudent financial management.
- Jana Small Finance Bank shows the strongest ROCE growth over the five-year period, rising from 100 (2020) to 184.5 (2024). This indicates nearly 85% improvement in capital efficiency, suggesting better profitability from capital employed.
- AU Small Finance Bank has the highest growth in CASA, peaking at 266% in 2023, ending at 231% in 2024. A high CASA ratio indicates strong deposit mobilisation through low-cost current and savings accounts, which improves profitability.

5. SUGGESTIONS

Banks should focus on improving capital efficiency, maintaining strong CASA growth, and optimizing operational costs. Jana can sustain its momentum with diversification, while AU must address declining ROCE. Ujjivan should leverage its stable CASA base. All banks should invest in digital platforms, customer retention, and data-driven strategies for sustainable growth.

6. LIMITATIONS OF STUDY

The study is limited to secondary data from 2020 to 2024, which may not reflect real-time market dynamics. It excludes external factors like economic policy changes or industry-wide risks. The analysis focuses only on three banks, limiting generalizability. Qualitative aspects like customer satisfaction and service quality are not considered.

7. CONCLUSIONS

The analysis highlights that Jana Small Finance Bank excels in both ROCE and CASA growth, demonstrating strong profitability and efficient capital usage. Ujjivan shows steady performance, while AU Small Finance Bank's declining ROCE raises concerns despite strong CASA growth. All banks should focus on optimizing capital deployment and enhancing customer retention.

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