A Study on the Emerging Threats and Operational Challenges of Small Finance Banks in Ramanagara District

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Abstract: **In India, the Reserve Bank of India (RBI) serves as the vital regulatory authority overseeing the functioning of the banking area. In latest years, the Indian banking enterprise has witnessed great transformations, one of the most first-rate being the advent of Small Finance Banks (SFBs). These banks are a form of niche monetary establishments designed to provide fundamental banking services which includes accepting deposits and increasing loans. The number one objective of putting in place Small Finance Banks is to sell monetary inclusion with the aid of attaining underserved segments of society in particular small commercial enterprise devices, marginal and small farmers, micro and small businesses, and the unorganized area. On sixteenth September 2015, the RBI initiated a prime step in reshaping the monetary system by granting licenses to ten Small Finance Banks. These banks are considered the very last hyperlink inside the financial inclusion chain, solidified by comprehensive RBI guidelines. This article goal to discover the objectives, possibilities, challenges, and threats faced with the aid of Small Finance Banks inside the context of India's evolving financial landscape.**

Keywords: **Financial Inclusion, Banking Sector Reforms, Rural Banking, Regulatory Challenges**

1. INTRODUCTION

In recent years, the Indian banking sector has undergone major shifts as new banking models have emerged to boost financial inclusion. One notable change is the growth of Small Finance Banks (SFBs). The Reserve Bank of India (RBI) created and approved these banks to offer basic banking services to people who lack access to them. SFBs typically provide credit scores, savings options, and other financial products to micro and small enterprises small-scale farmers, and low-income households. While SFBs have expanded their reach and made a positive social impact, they face several operational and strategic hurdles that limit their growth and long-term success.

The primary objective of this study is to identify and assess the growing risks and operational difficulties encountered by small financing institutions in the Ramanagara District. This area has a varied economy and substantial rural population. There are several reasons for these operational challenges. These include laws that limit their operations, poor infrastructure, unhappy clients brought on by technical difficulties, and opposition from traditional banks and fintech firms. The objective of this study is to offer a fact-based comprehension of these issues. Furthermore, it aims to provide methods for bolstering SFBs' role of SFBs in fair economic growth in rural and semi-urban areas, such as Ramanagara.

2. REVIEW OF LITERATURE

P.Dhanya (2019): the Article to beautify economic inclusion through achieving underserved and unbanked populations. These banks aim to offer era-driven low-fee monetary offerings, particularly in rural and semi-urban areas. A majority of licensed SFBs originated from Microfinance Institutions (MFIs), already skilled in delivering microcredit to low-earning corporations. The key goal of SFBs is to provide formal credit get admission to at low priced costs and promote monetary literacy. Despite projects such as cooperative banks and SHGs, many still rely upon informal credit. SFBs cope with this gap with progressed ultimate-mile connectivity.

S. Kangayan (2020): This take a look at evaluations the sustainability of Small Finance Banks (SFBs) in India, introduced to sell monetary inclusion among the underprivileged. With over 21.9% of India's population below the poverty line, SFBs offer crucial banking offerings, such as savings, credit score, insurance, and transfers. Despite being new, SFBs have shown a robust performance, capturing approximately 17% of the microfinance market. The study adopts an exploratory research layout using secondary statistics from six purposively decided on SFBs. Analytical tools like ANOVA, correlation, and economic ratios are used to evaluate progress, price of finances, and Net Interest Margin (NIM) to assess lengthy-time period sustainability.

Vidya Chandrashekar (2022): This conceptual look at examines the function of Small Finance Banks (SFBs) in helping rural economies thru monetary inclusion, credit score get entry to, and process creation. While SFBs are important for selling monetary literacy and extending banking offerings, they face large challenges in debt series in rural regions. Issues include cultural obstacles, negative infrastructure, seasonal income fluctuations, collateral loss, and financial focus among debtors. These elements contribute to delayed payments and growing Non-Performing Assets (NPAs). This study aims to recognize these challenges and offer positive tips to assist SFBs in enhancing their debt recuperation and holding sustainable lending practices in rural areas.

3. OBJECTIVES OF THE STUDY

i. To identify the role of Small Finance Banks (SFBs) in promoting financial inclusion in society
ii. To analyze the emerging threats and operational challenges faced by Small Finance Banks (SFBs)

4. RESEARCH METHODOLOGY

4.1 Research layout: The research design for this study could be descriptive and exploratory.
4.2 Descriptive Research: This design will be used to explain the nature of the demanding situations, threats, and role of SFBs in monetary inclusion.
4.3 Exploratory Research: It will discover emerging threats, such as virtual disruptions, monetary shifts, and regulatory challenges that SFBs face in the location.

5.1 Profile of the Study Area

The look at region, Ramanagara District, placed within the country of Karnataka, is known for its colorful financial system, broadly speaking driven with the aid of agriculture, textiles, and the presence of small-scale industries. The district's evolving monetary landscape provides a critical context for inspecting the operational challenges faced by means of Small Finance Banks (SFBs).

5.1.1 Geographical and economic overview

Ramanagara district, located approximately 50 km southwest of Bengaluru, spans three,516 square kilometers and functions a hilly terrain with distinguished granite outcrops, inclusive of Ramadevarabetta. The district is renowned for its sericulture industry, earning it the nickname "Silk City," and hosts Asia's biggest silk cocoon market. Its economy is varied, with agriculture contributing 16.2%, industry 32.0%, and offerings fifty one. Eight% to the Gross District Domestic Product, totaling □42,800 crore in 2024-25.

The study area, Ramanagara District, located in the state of Karnataka, is known for its vibrant economy, primarily driven by agriculture, textiles, and the presence of small-scale industries. The district's evolving financial landscape provides a critical context for examining the operational challenges faced by Small Finance Banks (SFBs).

5.1.2 Geographical and economic overview

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5.1.3 Presence and penetration of SFBs

Small Finance Banks (SFBs) have improved their footprint in Ramanagara District to sell monetary inclusion and serve the credit needs of low-income and underserved groups. With a complete of 15 branches operated by means of six distinctive SFBs, their presence is well-dispensed throughout semi-urban and rural places. These banks offer a range of economic offerings, together with micro-loans, savings debts, and digital banking solutions. Their strategic penetration enables bridge the financial gap within the district by attaining unbanked populations, assisting self-employment, and strengthening the rural economic system. The increase of SFBs complements the bigger purpose of inclusive and sustainable monetary improvement in the region.

Table 1. List of Small Finance Banks Operating in Ramanagara District

SN	Bank Name	No of Branches
1	Ujjivan Small Finance Bank	04
2	AU Small Finance Banks	03
3	ESAF Small Finance Banks	01
4	Equitas Small Finance Banks	03
5	Suryoday Small Finance Banks	02
6	Jana Small Finance Bank	02

5.1.4 Banking habits in the district

Ramanagara district exhibits a various and evolving banking tradition, supported through a mix of Scheduled Commercial Banks, Cooperative Banks, and Small Finance Banks. With over 80 bank branches, together with Karnataka Bank, Ujjivan SFB, and numerous cooperative establishments, monetary get admission to is regularly enhancing. Approximately 75% of families have as a minimum one bank account, encouraged by using schemes like Jan Dhan Yojana. Digital banking adoption is rising, in particular in city pockets, while rural areas nonetheless depend closely on traditional banking. Cooperative banks and SFBs play a crucial position in supporting SHGs, small traders, and farmers, reflecting inclusive yet transitional banking conduct in the district.

5.2 Analysis and Discussion

5.2.1 The role of Small Finance Banks (SFBs)

A. Serving the Unbanked and Underbanked: SFBs are mandated to provide banking services to sections of society that lack get entry to to formal finance. According to the RBI, over sixty five% of SFB branches are placed in rural and semi-urban regions, without delay catering to financially excluded populations.

B. Microcredit and Small Loans: SFBs normally recognition on lending to micro and small companies, frequently with mortgage sizes below □25 lakhs. As of March 2023, SFBs had allotted over □1.2 lakh crore in loans to MSMEs, a important step in reducing credit exclusion.

C. Encouraging Savings Habits: By offering savings and fixed deposit products tailored for low-income groups, SFBs assist inculcate a financial savings tradition. In FY23, over four crore deposit accounts were opened by means of SFBs, contributing extensively to household financial safety.

D. Doorstep Banking and Technology Use: SFBs use technology and doorstep services (like cellular banking vans and marketers) to reach far off populations. This has enabled over 70% of their transactions to be accomplished digitally, lowering bodily access obstacles.

E. Focus on Priority Sector Lending: RBI mandates SFBs to allocate seventy five% of Adjusted Net Bank Credit to precedence sectors (like agriculture, education, housing), which immediately advantages marginalized agencies and promotes inclusive increase.

F. Promoting Women Empowerment: SFBs have supported girls via Self-Help Group (SHG) linkages and person lending. Reports show that around 30-40% of SFB borrowers are ladies, allowing economic independence and entrepreneurship.

G. Facilitating Financial Literacy: Many SFBs conduct economic literacy camps in rural regions. For example, Ujjivan SFB reached over 10 lakh people via attention applications, assisting people understand banking, saving, and credit score utilization.

H. Inclusive Customer On boarding: SFBs simplify account commencing using eKYC and Aadhaar-based totally structures, growing inclusion. As a end result, the majority of new accounts opened in rural areas through SFBs require minimum documentation and zero stability.

5.2.2 Threats faced by SFBs

Small Finance Banks (SFBs) in Ramanagara face several rising threats that project their stability and increase. These threats stem from regulatory pressures, technological disruptions, and intense competition from mainstream and virtual economic establishments.

Threats faced via Small Finance Banks (SFBs)

A. Competition: In Ramanagara District, Small Finance Banks (SFBs) face vast opposition from a diverse array of monetary institutions. The district hosts 14 financial institution branches, which includes prominent players like Karnataka Bank Ltd. Additionally, cooperative banks which includes Sri Laxmi Mahila Souharda Pattina Sahakari Niyamita and The Bangalore City Co-Operative Bank Ltd. Have a remarkable presence. This competitive panorama challenges SFBs to distinguish themselves and correctly serve the financial desires of the nearby populace.

B. Policy and regulatory changes: In Ramanagara District, Small Finance Banks (SFBs) come across numerous coverage and regulatory challenges that effect their operations. These include compliance with stringent Reserve Bank of India (RBI) tips, such as retaining at least seventy five% of Adjusted Net Bank Credit (ANBC) in precedence sector lending, with at least 50% directed towards loans as much as □25 lakh. Additionally, SFBs ought to adhere to exposure limits, which includes a most of 10% of capital budget to a single borrower and 15% to a group of borrowers. These regulatory requirements necessitate meticulous danger management and operational techniques.

C. Rising operational costs: Small Finance Banks (SFBs) in Ramanagara District face escalating operational prices, mainly because of regulatory compliance and technological advancements. Nationally, banks are growing their IT spending to about 10% of working prices, up from 6%-eight%, to address RBI's scrutiny over virtual infrastructure and cybersecurity . This trend is obvious in SFBs in Ramanagara, where investments in middle banking systems and digital fraud monitoring are critical to satisfy regulatory standards and beautify service transport.

D. Digital disruption: In Ramanagara District, Small Finance Banks (SFBs) face big demanding situations due to virtual disruption. Nationally, over 40% of banking transactions are performed digitally, with cellular banking being the primary approach for fifty five% of purchasers. This shift intensifies competition from fintech firms and virtual-first systems, compelling SFBs to put money into sturdy digital infrastructure to meet evolving purchaser expectancies.

E. Low-income margins: Small Finance Banks (SFBs) in Ramanagara District face demanding situations because of low-profit margins, impacting their financial sustainability. Nationally, the go back on property (RoA) for SFBs is projected to say no from 2.1% to about 1.7% in FY25, normally because of reduced internet interest margins and multiplied credit fees . This trend displays the broader economic pressures affecting SFBs inside the vicinity.

F. Difficulty in attracting skilled workforce: Small Finance Banks (SFBs) in Ramanagara District face challenges in attracting and retaining skilled employees, particularly in rural areas. Nationally, the banking sector experiences an average annual employee turnover rate of approximately 12%, with SFBs often reporting higher figures due to limited career growth opportunities and geographic constraints. This turnover increases recruitment and training costs, impacting operational efficiency. Additionally, the demand for digital banking skills is rising, yet the supply of qualified professionals remains insufficient, further exacerbating staffing challenges in SFBs.

G. Higher risk of NPAs: In Ramanagara District, Small Finance Banks (SFBs) face heightened risks of Non-Performing Assets (NPAs), particularly in microfinance and unsecured lending sectors. Nationally, SFBs reported a gross NPA ratio of 3.2% as of September 2023, with total NPAs amounting to □8,608 crore. This figure is notably higher compared to other banking segments, indicating increased asset quality stress. The rural demographic, characterized by informal income sources and limited credit history, contributes to elevated default rates, challenging SFBs in maintaining asset quality.

H. Customer retention challenges: In Ramanagara District, Small Finance Banks (SFBs) encounter significant challenges in customer retention, primarily due to limited digital infrastructure and strong competition from established banks and fintech platforms. Nationally, the average customer retention rate for financial services stands at 78%, with banking slightly lower at 75% . However, SFBs often experience higher attrition rates, as customers increasingly seek seamless digital experiences and personalized services. Approximately 20% of customers switch banks due to poor customer experience, highlighting the critical need for SFBs to enhance service quality and digital engagement to retain their clientele.

5.2.3 Operational challenges

Small Finance Banks (SFBs) face various operational challenges that impact their efficiency and growth, particularly in serving underserved populations. These challenges are largely driven by resource constraints, regulatory requirements, and the need to balance traditional banking practices with modern technology.

A. Limited branch network: In Ramanagara District, Small Finance Banks (SFBs) face operational challenges due to a limited branch network. According to Karnataka Gramin Bank's data, Ramanagara has only 14 bank branches, including those of SFBs like Ujjivan and ESAF. This limited presence restricts financial access, especially in rural areas, hindering the banks' ability to serve the underserved population effectively.

B. Inadequate digital infrastructure: In Ramanagara District, Small Finance Banks (SFBs) face operational challenges due to inadequate digital infrastructure. Nationally, rural India accounts for over 53% of internet consumption, yet internet connectivity remains a significant barrier in many rural areas, affecting the adoption of digital banking services . Additionally, despite the government's efforts to enhance digital literacy through initiatives like PMGDISHA, a substantial portion of the rural population still lacks the necessary skills to navigate digital banking platforms effectively . These factors hinder SFBs' ability to offer seamless digital services, impacting customer engagement and operational efficiency.

C. Difficulty in credit appraisal: In Ramanagara District, Small Finance Banks (SFBs) encounter significant challenges in credit appraisal, particularly when assessing rural borrowers with limited formal documentation. Nationally, over 40% of India's population depends on agriculture, often lacking formal credit histories, which complicates risk assessment for SFBs. Additionally, the implementation of stricter lending rules in November 2023 has increased the difficulty of credit appraisal, as banks are now required to maintain higher capital reserves for microcredit loans, further constraining their ability to extend credit to underserved populations.

B. High employee turnover: In Ramanagara District, Small Finance Banks (SFBs) face challenges related to high employee turnover. Nationally, the banking sector experiences an average annual employee turnover rate of approximately 12%, with SFBs often reporting higher figures due to limited career growth opportunities and geographic constraints. This turnover increases recruitment and training costs, impacting operational efficiency. Additionally, the demand for digital banking skills is rising, yet the supply of qualified professionals remains insufficient, further exacerbating staffing challenges in SFBs.

C. Debt recovery challenges: In Ramanagara District, Small Finance Banks (SFBs) face significant challenges in debt recovery, particularly in microfinance and agricultural lending sectors. Nationally, over 200,000 cases are pending in Debt Recovery Tribunals (DRTs), with resolutions proceeding at a rate of 30,000–40,000 cases per year, leading to an estimated seven-year backlog . This delay exacerbates the difficulty for SFBs in recovering dues, especially from rural borrowers with limited formal documentation. Additionally, the Reserve Bank of India's recent directive to halt fresh loans to borrowers with existing defaults has intensified repayment challenges, as many rural clients lack steady incomes, thereby increasing default rates

D. Limited product portfolio: Small Finance Banks (SFBs) in Ramanagara District face operational challenges due to a limited product portfolio, which hinders their ability to offer comprehensive financial services to underserved populations. Nationally, SFBs are required to allocate 75% of their Adjusted Net Bank Credit (ANBC) to priority sectors, with at least 50% directed towards loans up to □25 lakh. These regulatory constraints, coupled with limited resources, restrict SFBs from diversifying their offerings beyond microloans, agricultural loans, and basic savings products. Consequently, SFBs struggle to meet the diverse financial needs of their clientele, impacting their competitiveness and growth potential.

6. SUGGESTIONS

- Enhancing Digital Infrastructure: SFBs should invest in upgrading their digital platforms to provide seamless banking services, especially in rural areas. Digital literacy programs should be introduced to empower customers and bridge the technology gap.

- Expanding Product Portfolio: Small Finance Banks should diversify their offerings to include insurance, fixed deposits, and investment options. This will help meet the varied financial needs of rural populations and improve customer satisfaction.

- Strengthening Debt Recovery Mechanisms: SFBs should focus on implementing more effective debt collection strategies using data-driven tools and partnerships with local recovery agencies. Additionally, introducing flexible repayment plans could enhance recovery rates and reduce NPAs.

- Improving Employee Training and Retention: To reduce high turnover, SFBs should offer comprehensive training programs and career growth opportunities for their employees. Providing competitive benefits and creating a positive work culture can significantly improve retention and operational efficiency.

7. LIMITATIONS OF STUDY

- The study will be limited to Ramanagara District, which may not reflect trends in other regions.
- Availability and reliability of data from small finance banks and customers may be restricted.
- Limited time for data collection may affect the depth of analysis.

8. CONCLUSIONS

Small Finance Banks (SFBs) in Ramanagara District have significantly contributed to enhancing financial inclusion by catering to the needs of underserved and rural populations. However, their growth and operational efficiency are hindered by various challenges such as intense competition from established banks, regulatory and policy limitations, rising operational costs, limited digital infrastructure, and difficulties in debt recovery. Moreover, high employee turnover and a narrow product portfolio further constrain their performance. Addressing these issues through strategic policy support, technological upgrades, workforce development, and diversified financial offerings can improve their resilience. Strengthening SFBs is crucial for ensuring inclusive and sustainable financial development in the district.

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