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RESEARCH ARTICLE

THE RBI'S DIGITAL LENDING GUIDELINES: ASSESSING THE IMPACT ON CREDIT ACCESS FOR INDIA'S UNDERBANKED POPULATION

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Abstract

Digital lending has changed the way many Indians access credit. Mobile applications, online lending platforms and digital verification have made it possible for borrowers to apply for loans without visiting a traditional bank branch. This development has been particularly important for people who may have limited access to formal banking services. However, the rapid growth of digital lending also created concerns about high charges, misuse of personal data, misleading loan offers and aggressive recovery practices. In response, the Reserve Bank of India (RBI) introduced its Guidelines on Digital Lending in September 2022. This paper examines the purpose of these guidelines and considers their potential effect on credit access for underserved borrowers. It focuses on changes in consumer protection, data usage, disclosure and the relationship between regulated entities and digital lending service providers. The evidence suggests that the RBI's approach has strengthened transparency and accountability in digital lending, although stricter compliance requirements may increase costs for some lenders. The broader challenge is therefore to ensure that regulation removes harmful lending practices without making legitimate digital credit unnecessarily difficult to access.

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Introduction:-

Access to affordable credit is an important part of financial inclusion. Individuals may need loans for education, medical expenses, household consumption or small businesses, while small enterprises often require working capital to continue their operations. Traditional banks, however, may not always be able to serve every borrower efficiently. People without a long credit history, stable documentation or easy access to bank branches can face difficulties obtaining formal loans. Digital lending has attempted to address some of these limitations. Borrowers can increasingly apply for loans through mobile applications and online platforms, with digital systems being used for customer identification, credit assessment, approval and disbursement. The rapid growth of this industry also created new risks. Some digital lending applications were accused of charging excessive fees, collecting unnecessary personal information and using aggressive recovery methods. The RBI's 2022 guidelines were introduced partly in response to these concerns. The RBI stated that the rules were intended to address issues including mis-selling, data privacy, unfair business conduct and unethical recovery practices. This creates an important policy question: can stronger regulation protect borrowers without reducing access to legitimate digital credit?

Growth of Digital Lending in India:-

Digital lending is part of a broader transformation in India's financial system. The spread of smartphones, digital payments, Aadhaar-based identification and online financial services has made it easier for financial institutions to reach customers without relying entirely on physical branches. For lenders, digital processes can reduce the time required to assess and approve a loan. For borrowers, this can mean faster access to funds and fewer visits to a bank branch. Digital lending can therefore be particularly useful for individuals who have traditionally been underserved by formal financial institutions. However, speed also creates risks. A borrower who receives a loan almost immediately may not fully understand its total cost or repayment conditions. Similarly, automated credit decisions may rely on large amounts of personal information. The challenge for regulators is therefore to encourage the efficiency of digital lending while ensuring that borrowers are adequately protected.

The RBI's 2022 Digital Lending Guidelines:-

The RBI issued its Guidelines on Digital Lending on 2 September 2022. The framework applied to commercial banks, specified cooperative banks and non-banking financial companies (NBFCs). One of the central principles was that regulated financial institutions could not avoid responsibility simply because they used a Lending Service Provider (LSP) or Digital Lending App (DLA). The regulated entity remained responsible for ensuring compliance with the applicable rules. The guidelines introduced several important requirements. First, the total cost of a digital loan had to be clearly disclosed to the borrower through the Annual Percentage Rate (APR) and a standardised Key Fact Statement. Second, loan disbursement and repayment were required to take place directly between the borrower and the regulated entity rather than through third-party pool accounts. Third, borrowers were to receive a cooling-off period during which they could exit certain digital loans by paying the principal and proportionate costs without an additional penalty. The framework also introduced requirements concerning grievance redressal and reporting of digital loans to credit information companies. These measures were designed to make the relationship between borrowers and digital lenders more transparent.

Data Privacy and Responsible Lending:-

Data has become an important part of digital credit assessment. Traditional lenders may rely heavily on documents such as income statements, bank records and credit histories. Digital lenders can potentially use information collected through online platforms and mobile devices. This can help lenders assess borrowers who have limited traditional credit histories. However, excessive data collection can create privacy risks. The RBI's framework therefore requires data collection to be based on a need for the information and on explicit borrower consent. The RBI's handbook also states that digital lending apps and service providers should not store personal information beyond specified basic information and should maintain appropriate privacy policies. This is important for underbanked borrowers because people who have limited experience with formal financial products may be less able to judge whether an application is collecting unnecessary information. Better disclosure and consent can therefore improve the quality of financial inclusion, rather than simply increasing the number of people who receive loans.

Recovery Practices and Consumer Protection:-

One of the most controversial aspects of some digital lending operations has been loan recovery. The speed and scale of digital lending can create problems when borrowers are unable to repay on time. Aggressive recovery practices can cause significant financial and personal distress. The RBI's 2022 framework specifically addressed concerns about unethical recovery practices and required greater accountability from regulated entities and their lending service providers. The RBI's annual reporting has identified concerns including mis-selling, breach of data privacy, unfair business practices, excessive interest rates and unethical recovery methods as reasons for strengthening regulation. The guidelines also require information about recovery agents to be disclosed to borrowers, helping make the recovery process more transparent. These measures can increase trust in digital credit. However, stricter recovery rules can also increase the cost of servicing loans for lenders. This creates a potential trade-off between consumer protection and the cost of providing credit.

Could Regulation Reduce Credit Access?:-

The main concern examined in this paper is whether stronger regulation could unintentionally reduce access to credit. Suppose a digital lender previously approved small loans using a highly automated system. If regulation requires additional documentation, data controls and compliance procedures, the cost of processing each loan may increase. This could have a larger effect on small loans than large loans because the lender receives less revenue from each transaction. As a result, some lenders may decide that certain high-risk or low-value borrowers are no longer profitable to serve. This is an important concern for underbanked populations. However, the opposite argument is also possible. Stronger regulation may increase confidence in digital lending and encourage more

people to use formal credit providers. If borrowers know that the lender is regulated and that loan costs and recovery procedures must be disclosed, they may be more willing to participate in the formal financial system. Therefore, regulation does not necessarily have to reduce credit access. Its effect depends on whether the rules primarily remove harmful practices or create excessive costs for legitimate lenders.

Digital Infrastructure and the Future of Credit Access:-

The development of India's digital financial infrastructure may help solve some of this tension. The RBI has supported initiatives designed to make credit assessment faster while improving access to reliable financial information. One example is the Unified Lending Interface (ULI), which connects lenders and data providers through standardised APIs. According to the RBI, by March 2025 the platform had 44 participating lenders, including banks and NBFCs, and access to more than 60 data services across 12 loan journeys. Such infrastructure could allow lenders to make better-informed decisions without relying on excessive or inappropriate personal data. This could be particularly valuable for small businesses and borrowers with limited traditional credit histories. The objective should therefore be to move towards better information rather than simply more information.

Assessing the Impact on Underbanked Borrowers:-

The impact of the 2022 guidelines can be considered through three dimensions.

Credit Availability:-

The key question is whether legitimate lenders continued to provide loans to borrowers who previously had limited access to formal credit. A fall in digital loan volumes after regulation would not automatically prove that the guidelines harmed financial inclusion. It could instead indicate that some low-quality or predatory lending activity disappeared. Similarly, an increase in lending volumes would not automatically prove that the guidelines were successful. Credit could increase while borrowers still face high costs or unsuitable loan products.

Credit Quality:-

A better measure of financial inclusion is whether borrowers receive credit that is affordable and appropriate for their circumstances. A small loan that is easy to obtain but carries unclear charges or aggressive recovery conditions may provide short-term access but create long-term financial problems.

Consumer Protection:-

The third dimension is whether borrowers have better information and greater control over their financial data.

The 2022 guidelines clearly strengthened this part of the framework by requiring greater disclosure, explicit consent and clearer responsibility for regulated entities.

Discussion:-

The evidence suggests that the RBI's approach represents a shift from simply encouraging digital lending towards encouraging responsible digital lending. This distinction is important. Financial inclusion should not be measured only by the number of people who receive loans. It should also consider whether those loans are transparent, affordable and suitable for borrowers. The 2022 guidelines may have increased compliance costs for some lenders, particularly digital platforms that previously depended heavily on outsourcing and extensive data collection. However, these costs need to be compared with the potential social costs of poorly regulated lending. At the same time, regulation should avoid creating such high compliance costs that legitimate lenders withdraw from smaller or riskier segments of the market. The ideal regulatory framework should therefore protect borrowers while allowing responsible lenders to continue experimenting with technology and new credit models.

Conclusion:-

The RBI's 2022 Digital Lending Guidelines were introduced at an important stage in India's financial development. Digital technology had created new opportunities to provide fast and convenient credit, but the rapid growth of digital lending also created concerns about privacy, transparency and recovery practices. The guidelines strengthened the responsibility of regulated entities, improved disclosure requirements and placed greater limits on how borrower information could be collected and used. These changes can improve trust in digital financial services and help prevent harmful lending practices. However, the effect on credit access should be evaluated carefully. A reduction in digital lending volumes would not necessarily mean that financial inclusion has worsened, just as higher lending volumes would not automatically mean that borrowers are better served. The more meaningful measure is whether underserved borrowers can obtain affordable, transparent and responsibly provided credit. India's future digital

lending framework will therefore need to maintain a balance. Regulation should be strong enough to prevent exploitation but flexible enough to allow responsible lenders to serve borrowers who may not fit easily into traditional banking models. The development of digital infrastructure such as ULI suggests that India may be able to move towards a model in which better data and technology improve credit assessment without requiring excessive collection of personal information. The long-term success of digital lending will ultimately depend on whether technology can expand financial inclusion while maintaining borrower protection.

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