FINACIAL INCLUSION IN INDIA

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ABSTRACT

Financial inclusion denotes delivery of financial services at an affordable cost to the vast sections of disadvantaged and low-income groups. Access to finance especially by the poor and vulnerable groups is prerequisite for poverty alleviation, employment, social upliftment and economic growth. Financial inclusion has become one of the most critical aspects in the context of inclusive growth and sustainable development in the developing countries like India. The Government of India and the RBI have been making concerted efforts to promote financial inclusion as one of the important national objectives. The government of India & RBI has out with a major initiative towards ensuring the inclusive growth through financial inclusion so that the access of financial service will reach to the mass population.

The banking industry has shown tremendous growth in volume and complexity during the last few decades. Despite making significant improvements in all the areas relating to financial viability, profitability and competitiveness, there are concerns that banks have not been able to include vast segment of the population, especially the underprivileged sections of the society, into the fold of basic banking services. Internationally efforts are being made to study the causes of financial exclusion and designing strategies to ensure financial inclusion of the poor and disadvantaged. The reasons may vary from country to country and hence the strategy could also vary but all out efforts are being made as financial inclusion can truly lift the financial condition and standards of life of the poor and the disadvantaged.

Keywords*: Poverty alleviation, Social upliftment, Economic Growth, Financial Viability,*

INTRODUCTION

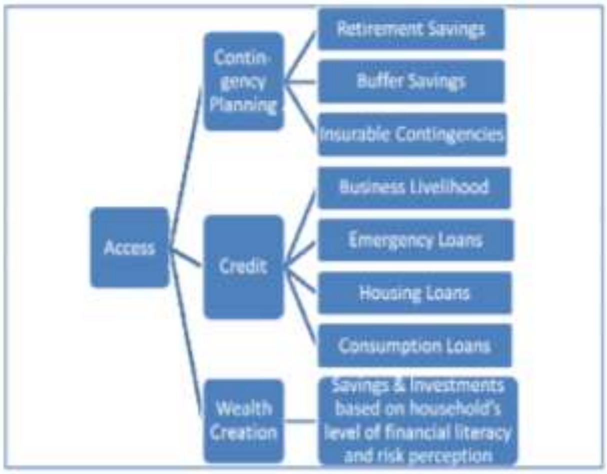
The Government of India and the Reserve Bank of India have been making concerted efforts to promote financial inclusion as one of the important national objectives of the country. Some of the major efforts made in the last five decades include - nationalization of banks, building up of robust branch network of scheduled commercial banks, co-operatives and regional rural banks, introduction of mandated priority sector lending targets, lead bank scheme, formation of self-help groups, permitting BCs/BFs to be appointed by banks to provide door step delivery of banking services, zero balance BSBD accounts, etc

Definitions

Financial inclusion may be defined as the process of ensuring access to financial services and timely and adequate credit where needed by vulnerable groups such as weaker sections and low income groups at an affordable cost (The Committee on Financial Inclusion, Chairman: Dr. C. Rangarajan).

Financial Inclusion, broadly defined, refers to universal access to a wide range of financial services at a reasonable cost. These include not only banking products but also other financial services such as insurance and equity products (The Committee on Financial Sector Reforms, Chairman: Dr.Raghuram G. Rajan). Household access to financial services is depicted in Figure I.

Figure I: Household Access to Financial Services



Source: A Hundred Small Steps - Report of the Committee on Financial Sector Reforms (Chairman : Dr. RaghuramRajan).

The essence of financial inclusion is to ensure delivery of financial services which include - bank accounts for savings and transactional 2 purposes, low cost credit for productive, personal and other purposes, financial advisory services, insurance facilities (life and non-life) etc.

FINANCIAL INCLUSION IN INDIA

FINANCIAL INCLUSION

FINANCIAL inclusion is the delivery of FINANCIAL services at affordable costs to vast sections of disadvantaged and low income groups.

History evolution of financial inclusion

Policy makers have grapped with the issue of reducing the scope of informal sector since colonial times.

Nicholson report (1895) was the first to highlight the need to establish "LAND BANKS" as an alternative to dominance of money lenders . resulting , the cooperative credit socities Act , 1904 was passed to provide , amongst other things , a legal basis for cooperative credit socities .

Even after 70 years of independence, a large section of Indian population still remain unbanked. This malaise has led generation of **FINANCIAL instability** and pauperism among the lower income group who do not have access to FINANCIAL products and services.

Historical Perspective

- 1954 : All-India Rural Credit Survey Committee report -suggested Multi-agency approach for financing the rural and agricultural sector;
- 1963 : Formation of Agricultural Refinance Corporation
- 1969: Nationalization of 14 major Private Banks – The flow of agricultural and rural credit witnessed a rapid increase
- 1972–Mandatory system of Priority Sector Lending (PSL)
- 1975 : Establishment of RRBs
- 1980 : Nationalisation of 6 more private banks

- 1982 : Establishment of NABARD through the transfer of RBI's agricultural credit department Provision of bank credit under Govt. Sponsored Subsidy Schemes Linking Agricultural Credit Targets at 18% with individual bank's net bank credit
- 1990–Implementation of the concept of Village level credit planning for 15 to 20 villages allotted to each of rural, semi-urban and urban branches of PSBs and RRBs under Service Area Approach
- Formulation of potential linked credit plan for each district annually by NABARD
- Agricultural Debt Relief Scheme and Financial Sector Reforms
- SHG-Bank Linkage as the most suitable model in Indian context a/c to NABARD
- 2000-Reforms sharply focused on Agricultural credit
- doubling the flow of agricultural credit – implementation of agricultural credit package
- Annual Special Agricultural Credit Plan

On tracks _ of NDA govt ..
Financial inclusion is expected to make sigifcant changes in the economy , especially the rural economy , which is expected to witness a revolution in availability of financial instruments mainly because of —

- **PMJDY**
- **gold monetization scheme**
- **MUDRA**
- **DBT**

PMJDY _	No.of accounts	Zero balanced accounts
Public sector banks	12.7	52.3 %
private sector banks	2.9	52.1%
RRBS	0.7	49.3%

which will operate through the banking system will also ensure regularity of flow of liquidity in housholds and therefore opportunities for investment.

Why FINANCIAL Inclusion in India is Important ?
The policy makers have been focusing on FINANCIAL inclusion of Indian rural and semi-rural areas primarily for three most important pressing needs.

1. **Creating a platform for inculcating the habit to save MONEY** – The lower income category has been living under the constant shadow of financial duress mainly because of the absence of savings.

2. Providing formal credit avenues – So far the unbanked population has been vulnerably dependent of informal channels of credit like family, friends and moneylenders. Availability of adequate and transparent credit from formal banking channels shall allow the entrepreneurial spirit of the masses to increase outputs and prosperity in the countryside.

3. Plug gaps and leaks in public subsidies and welfare programmes – A considerable sum of money that is meant for the poorest of poor does not actually reach them. While this money meanders through large system of government bureaucracy much of it is widely believed to leak and is unable to reach the intended parties. Government is therefore, pushing for direct cash transfers to beneficiaries through their BANK ACCOUNTS rather than subsidizing products and making cash payments.

What are the steps taken by RBI to support FINANCIAL inclusion?

A. Initiation of no-frills account – These accounts provide basic facilities of deposit and withdrawal to accountholders makes banking affordable by cutting down on extra frills that are no use for the lower section of the society. These accounts are expected to provide a low-cost mode to access BANK ACCOUNTS. RBI also eased KYC (Know Your customer) norms for opening of such accounts.

B. Banking service reaches homes through business correspondents – The banking systems have started to adopt the business correspondent mechanism to facilitate banking services in those areas where banks are unable to open brick and mortar branches for cost considerations. Business Correspondents provide affordability and easy accessibility to this unbanked population. Armed with suitable technology, the business correspondents help in taking the banks to the doorsteps of rural households.

C.EBT – Electronic Benefits Transfer – To plug the leakages that are present in transfer of payments through the various levels of bureaucracy, government has begun the procedure of transferring payment directly to accounts of the beneficiaries. This "human-less" transfer of payment is expected to provide better benefits and relief to the beneficiaries while reducing government's cost of transfer and monitoring. Once the benefits starts to accrue to the masses, those who remain unbanked shall start looking to enter the formal FINANCIAL sector.

What more is to be done for FINANCIAL inclusion?

FINANCIAL inclusion of the unbanked masses is a critical step that requires political will, bureaucratic support and dogged persuasion by RBI. It is expected to unleash the hugely untapped potential of the bottom of pyramid section of Indian economy. Perhaps, financial inclusion can begin the next revolution of growth and prosperity.

India had scored poorly on financial inclusion parameters when compared with the global average

as per Reserve Bank of India in its annual report

The report quoted a World Bank study in April 2012, which had shown half of the world's population held accounts with formal financial institutions. The study said only nine per cent of the population had taken new loans from a bank, CREDIT UNION or microfinance institution in the past year. In India, only 35 per cent have formal accounts versus an average of 41 per cent in developing economies.

***India also scored poorly in respect of_**

- CREDIT CARDS
- Outstanding mortgage
- Health insurance
- Adult origination of new loans and mobile banking.

Intiatives by RBI __

- BCs — 110,000 business correspondents employed through the business facilitator and business correspondent (BC) models and set up goals for banks to provide access to formal banking to all 74,414 villages with population over 2000.
- RBI also adopted the information, communication, technology-based agent bank model through BCs for door-step delivery of financial products and services since 2006
- Minimum infrastructure for operating small customer transactions and supporting up to 8-10 BCs at a reasonable distance of 2-3 km.

FINANCIAL INCLUSION & RURAL CREDIT

Overview

- French proverb rightly stresses the urgency of Credit to the farmers "Credit supports the farmer as the hangman's rope supports the hanged"
- RBI estimates : 40% of the Indians do not even have a bank account.
- Sources of credit for cultivator households
- 27% of the households from formal sources
- 22% from informal sources
- 51% with virtually no access

Mico-Finance Services

- credit / savings
- insurance,
- pension services,
- money transfer,
- Leasing
- issue / discount of warehouse receipts and future / option contracts for agricultural commodities and forest produce.

Indices

- Index of Financial Inclusion (IFI) : Kerala -> MH -> Karnataka-> Bihar
- Micro-finance Penetration index(MPI)
- Micro-finance Poverty penetration index(MPPI)
- Even states like Gujarat and MH lag behind the national average of 40.1%
- Short-term loans for (working capital) cultivation of all crops of economic importance;
- Long-term loans for the development of irrigation potential, purchase of farm equipment and machinery, Land Development, Plantation crops and horticulture,Sericulture, hi-tech agriculture, Cold-storage and market yards

Financial inclusion & Institutional Structure & Mechanisms

- Institutional Structure of Rural Banking includes & Formal : (direct/indirect & short-term/long-term)
- RBI – regulator of SCBs
- NABARD: (re-financing)
- Commercial Banks – Credit Disbursal
- Local Area Banks (LABs) – their geographical spread is constrained to few districts; Private in nature

Trends

- Agricultural credit (Loan amount : Commercial banks > Cooperative banks > RRBs);
- Domination of Cooperative banks in credit disbursement till 2000 is being replaced by Commercial banks (as % of total credit);
- 1993 : Cooperatives – 61% ; Commercial banks – 32.7%; RRBs – 5.9%
- 2000 : Cooperatives – 37.9% ; Commercial banks – 54.1%; RRBs – 7.8%
- 2012 : Cooperatives – 18.3% ; Commercial banks – 71.2% ; RRBs – 10.5%

Essential Elements of Rural Credit

- Credit can neither be cheap and facile nor on easy terms without regard to its use, but it should be guarded, guided and productive
- Credit institution should have tailor-made loan products to match the specific needs of target groups
- Loans must be linked to credit-worthiness of the purpose rather than to the credit-worthiness of the Person

Financial Inclusion Strategies

- **BC-model**
- **PoS(Point of Sale)**
- **No-frills accounts** (With very little or no minimum balance), simplification of KYC norms
- **KCC – Kisan Credit Card** – from the year 1998-99 –to meet production credit requirements and short-term credit needs in a timely and hassle-free manner credit for crop production
- **Lead Bank Scheme** -1969 aimed at
- **Ultra small Branches** with Bank officers offering other services , undertake field verification and follow-up banking transactions.
- **Direct Benefit Transfer** : Cash transfer through Aadhar payment Bridge requires Bank accounts which leads to financial inclusion.

Committee on financial inclusion

Khan Commission

RBI set up in 2004 to look into FINANCIAL inclusion and the recommendations of the commission were incorporated into the mid-term review of the policy (2005–06) and urged banks to review their existing practices to align them with the objective of FINANCIAL inclusion. RBI also exhorted the banks and stressed the need to make available a basic banking 'no frills' account either with 'NIL' or very minimum balances as well as charges that would make such accounts accessible to vast sections of the population

Of the many schemes and programmes pushed forward by RBI the following need special mention.

Rangarajan Committee

4 major reasons for lack of financial inclusion

- Inability to provide collateral security
- Poor credit absorption capacity,

- Inadequate reach of the institutions
- Weak community network
- there is need to organize Urban/peri-Urban poor people into Neighbourhood Groups (NHGs) on the same pattern as has been adopted for the rural poor.(Need to extend the mandate of NABARD to cover beyond rural areas)
- alter the emphasis somewhat from the large Bank led, public sector dominated, mandate ridden and branch-expansion-focused strategy to Micro Banks.

2nd ARC(Administrative reforms commission) on Financial Inclusion:

- Innovation is critical for financial inclusion. This would mean developing newer financial products in terms of loans, savings, insurance services etc. which are tailored to the needs of the poor.
- Currently, most public sector Banks and micro-finance institutions have a narrow product offering, which limits the choice of the SHGs and also constrains them in terms of utilizing the loans productively.

Nachiket mor committee: Committee on Comprehensive Financial Services for Small Businesses and Low Income Households" was set up by the RBI in Sep 2013 under the chairmanship of Nachiket Mor, an RBI board member.

Key Recommendations

1. Providing a universal bank account to all Indians above the age of 18 years by January 1, 2016. To achieve this, a vertically differentiated banking system with payments banks for deposits and payments
2. **wholesale banks for credit outreach.** These banks need to have Rs.50 crore by way of capital, which is a tenth of what is applicable for new banks that are to be licensed.
3. **DEEPAK MOHANTY**

The Reserve Bank of India (RBI) on 15 July 2015 constituted a committee to work out a five-year (medium-term) action plan for financial inclusion. The 14-member panel will be headed by RBI executive director Deepak Mohanty.

1. The Committee will work to spread the reach of financial services to unbanked population.
2. To review the existing policy of financial inclusion including supportive payment system and customer protection framework taking into account the recommendations made by various committees set up earlier.

New trends in financial inclusion

Source: Tarazi and Breloff, 'Non-bank E-money issuers-Regulatory approaches to protecting customer funds,' CGAP Focus Note 63, July 2010.

The Inter Bank Mobile Payment Service can revolutionize the way payments are made. With corporates coming in as business correspondents, banks, telecom players and companies can work out a viable model for financial inclusion.

Universal financial inclusion, talked of for decades by policymakers, finally may be coming to fruition. All the requisite pieces have been coming together, some rather rapidly in the past few years, and some of the most dramatic changes to sweep the economy have happened in the payment and settlement system.

For years, India has been seen as lagging behind, with Kenya pointed to as the poster boy of mobile money and financial inclusion, even though India had all the components of a conducive environment — large unbanked population, stable banking system, growing tele-density with a competitive mobile landscape, and significant technological capabilities.

The several regulatory roadblocks here have recently been eased at a sizzling pace — the push on business correspondents, the first step away from the branch model of expansion, has increased with progressive relaxation in guidelines, and last September corporates were allowed to act as BCs for banks, a big breakthrough in providing a comprehensive eco-system for financial inclusion.

MOBILE SERVICES' POTENTIAL

While large multi-player telecom and banking sectors augur well for competition, the flip side is the need for inter-operability to allow payments and settlements seamlessly across service providers. This link is in place now with the Inter Bank Mobile Payment Service (IMPS), provided by the National Payments Corporation of India (NPCI), a service that is set to revolutionise the way payments are made across the country.

Here the UID is expected to play a crucial role for segments like migrants who have stayed out of the system so far.

NON-BANK MODEL

It has to said that there is no lack of demand for financial services in India. Banks have typically refrained from innovating for the bottom of the pyramid, deterred by the low values here. On the other hand, mobile operators are in sync with transaction-based business models for low value transactions that are the need for those out of the formal financial system.

There is, therefore, a perfect synergy here to be exploited and with the RBI pushing for financial inclusion now, it is for the telecom operators, banks and merchants/companies to work out a sustainable business model.

CONCLUSION

Based on this paper Increasing liberalization and higher economic growth, the role of banking sector is perched to increase in the financing pattern of economic activities in the country. To assemble the growing credit demand, the banks need to organize resources from a wider deposit base and extend credit to activities previously not financed by banks. The trend of growing commercialization of agriculture and rural activities should produce greener pastures, and banks should examine the benefits of increasing saturation therein. Financial inclusion will strengthen financial deepening and provide resources to the banks to increase credit release

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