FINANCIAL INCLUSION IN INDIA

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ABSTRACT

Financial inclusion is the availability of banking services at an affordable cost to disadvantaged and low-income groups. In India, the basic concept of financial inclusion is having a savings or current account with any bank. In reality, it includes loans, insurance services, and much more. The Indian banking system will have to deliver on the plan for financial inclusion, the system, which demonstrated its resilience in the face of the recent global financial crisis, should adopt strong and urgent measures to reach the unbanked segment of society and unlock their savings and investment potentials. The banking sector has also taken a lead role in promoting financial inclusion. In India, the Reserve Bank of India (RBI) has initiated several measures to achieve greater financial inclusion, such as facilitating "no-frills" accounts and "General Credit Cards" for low deposit and credit. Alternate financial institutions, such as micro-finance institutions and Self-Help Groups, have also been promoted in some countries.

The main objective of this paper is to understand the concept of financial inclusion and Role of banks for financial inclusion in India.

***Key Words**: Financial Inclusion, Role of banks*

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INTRODUCTION: WHAT IS FINANCIAL INCLUSION?

India has, for a long time, recognized the social and economic imperatives for broader financial inclusion and has made an enormous contribution to economic development by finding innovative ways to empower the poor. Starting with the nationalization of banks, priority sector lending requirements for banks, lead bank scheme, establishment of regional rural banks (RRBs), service area approach, self-help group-bank linkage programme, etc., multiple steps have been taken by the Reserve Bank of India (RBI) over the years to increase access to the poorer segments of society.

Despite all these efforts, a significant proportion of the households, especially in rural areas, still remained outside the coverage of the formal banking system. It is estimated that about 40% of Indians lack access even to the simplest kind of formal financial services.

In India, the term financial inclusion first featured in 2005, when RBI, in its annual policy statement of 2005-06, while recognizing the concerns in regard to the banking practices that tend to exclude rather than attract vast sections of the population, urged banks to review their existing practices to align them with the objective of financial inclusion."

About 2.9 billion people around the world do not have access to formal sources of banking and financial services. In India alone 560 million people are excluded from formal source of finance, a figure in tight correlation with the 41.6 percent (457 million) of the population that still lives below the poverty line (US$1.25/day). While India has enjoyed growing domestic demand and globally recognized prowess in the areas of information technology, automotive, life sciences, telecommunications and even space exploration, its continued success and growth as an economic power (in common with other emerging economies) can only be assured if concrete steps are taken to ensure that the social and economic development is inclusive.

DEFINITION OF FINANCIAL INCLUSION

A **World Bank report states**, “Financial inclusion, or broad access to financial services, is defined as an absence of price or non price barriers in the use of financial services.”

The **Rangarajan Committee (2008)** defined**,** financial inclusion 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.”

It includes access to banking services, credit, insurance, savings and assets, money advice and financial literacy and capability. The barriers to financial inclusion are access exclusion, condition exclusion, price exclusion, marketing exclusion and self-exclusion.

An inclusive financial system facilitates efficient allocation of productive resources and thus can potentially reduce the cost of capital. Accesses to appropriate financial services can significantly financial inclusion. improve the day to-day management of finances (bill payment, money transfer etc.). Also inclusion in to financial system protect unbanked people from informal sources of credit, who charge higher interest rates and often resort to unethical/harsh recovery practices. Access to a bank account provides avenues for secure and safe saving practices. A bank account can also provide a passport to wide ranging financial services such as overdraft facilities, debit card and credit cards. A number of financial services, such as insurance and pension, necessarily require access to a bank account. Thus, an inclusive financial system enhances efficiency and welfare of a society.

General equation

$$\boxed{NFA + BC = FI}$$

Where, BC = Banks + OFIs + MFI + IT

NFA = No Frills Saving Bank Account

BC = Banks + Other Financial Institutions + Micro Finance Institutions + Information Technology

OFI = Insurance Companies, Mutual Funds, Pension Companies

REVIEW OF LITERATURE

- Banks would have to evolve specific strategies to expand the outreach of their services in order to promote financial inclusion. One of the ways in which this can be achieved in a cost-effective manner is through forging linkages with micro finance institutions and local communities. Banks should give wide publicity of no frills account. Banks need to redesign their business strategies to incorporate specific plans to promote financial inclusion of low income group treating it both a business opportunity well as a corporate social responsibility (V.Leeladhar, 2005).

- An empirical study of Sendhilvelan .M and Karthikeyan .K (2006) revealed to ensure financial inclusion of all segments of the population, in both rural and urban areas banks should give wide publicity to the facility of “no frills” account.
- In the paper by Laveesh Bhandari and Sumitha Kale (2008) titled ‘Digital Payments and Financial Inclusion’ enough emphasis has been given to the present scenario and the paper has brought out the importance of embracing technology as a cost effective measure to improve financial inclusion. Payments through mobile phones have been suggested as the most appropriate measure.
- The work of Ghorude .K.N (2009) indicated that attaining the objective of inclusive growth has to necessarily encompass the social, economic and political inclusion. Developing micro entrepreneurship with organizational and community based support is a way of strengthening inclusive growth.
- Muthiah Manoharan .P and Krishnaveni Muthiah (2010) found limited access to affordable financial services such as savings, loans, remittance and insurance services to the vast majority of the population in the rural area and unorganized sector is believed to be a constraint to the growth impetus in these sectors. The behavioral pattern shows that many people were not comfortable with formal financial services. The reasons were difficulty in understanding language, various documents and conditions that come with financial services

OBJECTIVES

The main objectives of this study were:

- To study the Historical reasons for financial exclusion in India
- To study the measures taken by the banks for financial inclusion.
- To analyze the difficulties involved in the adoption of financial inclusion.
- To find out how are the schemes of RBI on financial inclusion is taken into account.

METHODOLOGY

The entire discussion has been made on the basis of secondary sources. The different books, journals, newspapers and related websites have been consulted in this regard.

STATEMENT OF THE PROBLEM

Financial inclusion is a policy measure to address the issue of poverty which would ensure avenues for people. It is estimated that globally over two billion people are excluded from access to financial services, of which one third is in India. Access to various financial services enables the poor people to participate in the growth of the economy. Many banks are forced to adopt financial inclusion rather than their own interest. Only few banks are actively involved in financial inclusion to promote economic development. This study attempts to address the issues involved in the adoption of the financial inclusion plan and to widespread the financial inclusion.

HISTORICAL REASONS FOR FINANCIAL EXCLUSION – INDIA

Why financial exclusion	**What are the solution for financial inclusion**	**How solution can be applied**
Under developed IT-Telecom infrastructure in the interiors of country	• IT-Telecom integrated platform • Accessible network in interiors of country • Microbanking products • Technology platform that can be shared to reduce cost and improve efficiency	• IT – Telecom Integration • Data connectivity • Shared access7 • Well connected delivery channel for real time transaction
Higher cost of funds and administrative expenses	• Influx of technology products to scale • Higher Volumes • Better usage of data • Reduction in cost of delivery of service	• Low cost technology products, (standardised and inter-operable) • Shared access and self-service solution • Low cost data management system • Developing delivery channel such as BC model and self-service

		solution
Population and poverty	• Social development program • Involvement of other nongovernment bodies • Literacy campaign	• Government initiatives in social development • Government incentives and support for NGOs and SHGs • Development of MFI, SHGs & NGOs • Corporate involvement in literacy drive, e.g. Teach India campaign
Illiteracy (Includes financial illiteracy)	• Financial literacy campaign • Use of technology where ever possible • Customization of product for excluded populace	• National alliance driven by MFIs, SHGs, NGOs and even technology vendors • Interactive Voice Response System (IVRS), Self-service solution • Literacy campaign • Corporate drive for financial literary
Regional barrier (language and culture)	• Delivering solution in regional language • Localization of delivery channel • Co-operative or	• Technology Solution such as IVRS, • Delivery channels: Self-service and Business correspondent model

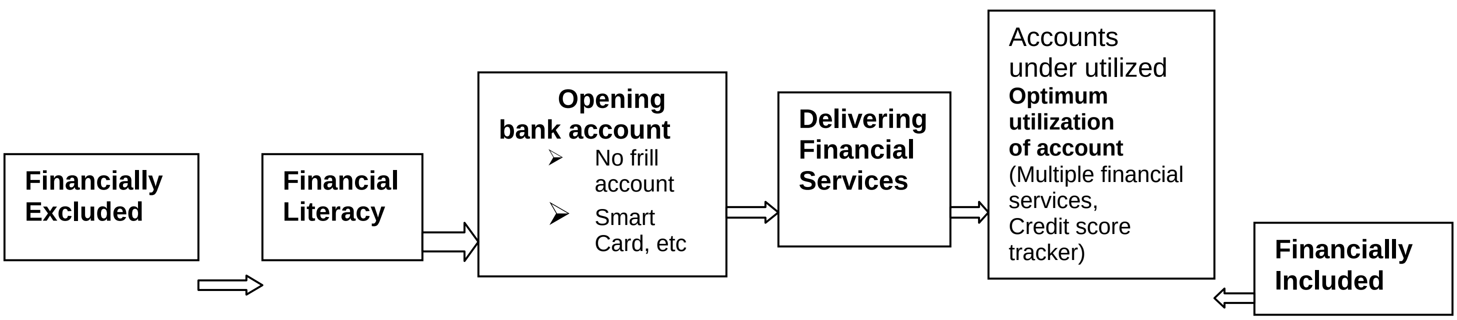
	community center	• Higher involvement of regional SHG, MFI, NGO

Source: Frost & Sullivan

FINANCIAL INCLUSION LIFECYCLE

The first step of Financial Inclusion is to educate customers and open an account. However, merely opening a bank account for a poor individual is not financial inclusion. This approach generally results in an inactive account or, at best, a repository for government benefits. A three-step approach (see Chart) is required to bring financially underserved individuals into a financially inclusive society. After improving financial literacy and opening an account of some form, it is usage of that account, linkage with
other financial services and access to all the financial instruments that are
required to complete the financial inclusion lifecycle. Optimum utilisation of an account should be another target for banking service providers.

Chart : Financial Inclusion Lifecycles



PROCESS OF FINANCIAL INCLUSION IN INDIA

The process of financial inclusion in India can broadly be classified into three phases.

During the First Phase (1960-1990), the focus was on channeling of credit to the neglected sectors of the economy. Special emphasis was also laid on weaker sections of the society.

Second Phase (1990-2005) focused mainly on strengthening the financial institutions as part of financial sector reforms. Financial inclusion in this phase was encouraged mainly by the Kisan Credit Cards (KCCs) for providing credit to farmers. The SHG-bank linkage programme was launched by National Bank for Agriculture and Rural Development (NABARD) in 1992, with policy support from the Reserve Bank, to facilitate collective decision making by the poor and provide 'door step' banking.

During the Third Phase (2005 onwards), the ‘financial inclusion’ was explicitly made as a policy objective and thrust was on providing safe facility of savings deposits through ‘no frills’ accounts.

MEASURES FOR FINANCIAL INCLUSION IN INDIA

Several measures have been taken by both the Reserve Bank of India and the Government to bring the financially excluded people to the fold of the formal banking services. The important financial inclusion initiatives of RBI are given below:

- Introduction of ‘No-Frills’ account
- Relaxing 'Know Your Customer'(KYC) norms
- General Purpose Credit Card (GCC) Schemes
- Role NGOs, SHGs and MFIs
- Business Facilitator (BF) and Business Correspondent (BC) Models.
- Nationwide Electronic Financial Inclusion System (NEFIS)
- Project Financial Literacy
- Financial Literacy and Credit Counseling (FLCC) centers
- National Rural Financial Inclusion Plan (NRFIP)
- Financial Inclusion Fund (FIF)
- Financial Inclusion Technology Fund (FITF)

The status of financial inclusion in India has been assessed by different committees interms access to basic banking services by poor and weaker sections.

STATUS OF FINANCIAL INCLUSION IN INDIA

The Eleventh Five Year Plan (2007-12) envisions inclusive growth as a key objective. The inclusive growth implies an equitable allocation of resources with benefits accruing to every section of society. It is aimed at poverty reduction, human development, health and provides opportunity to work and be creative. Achieving inclusive growth in India is the biggest challenge as it is very difficult to bring 600 million people living in rural India into the mainstream. One of the best ways to achieve inclusive growth is through financial inclusion.

The success of the financial inclusion can be measured by the actual quantity and Quality of usage of the newly opened No Frill accounts. The number of no-frills account holders has more than doubled to 103.21 million in the year ending March 31, 2012, from 49.33 million in March 2010. The lead Bank in each district has been asked by RBI to draw a roadmap by the end of

March 31, 2010 For ensuring that all villages with a population of over 2,000 will have access to financial Services through a banking outlet, not necessarily a bank branch, by March 31, 2012. There will be an intermediate target to be achieved by March 31, 2011. Keeping in view the enormity of the task involved, the Committee on Financial Inclusion recommended the setting up of a mission mode National Rural Financial Inclusion Plan (NRFIP) with a target of providing access to comprehensive financial services to at Least 50 per cent (55.77 million) of the excluded rural households by 2012 and the remaining By 2015.

Financial Access points in India	**Status**
Number of no frills A/Cs	The number of no-frills account holders has more than doubled to 103.21 million in the year ending March 31, 2012, from 49.33 million in March 2010.
Total Number of Bank Branches	**97473 as on 30.6.2012**

Bank Group-wise Number of branches as on 30.6.2012

Bank Group	**Rural**	**Urban**	**Semi-urban**	**Metropolitan**	**Total**
Public Sector Banks	22146	17803	14223	13231	67403
Private Sector Banks	1555	4660	3580	3621	13416
Foreign Banks	7	9	61	247	324
Regional Rural Banks	12258	3094	830	148	16330
Total	**35966**	**25566**	**18694**	**17247**	**97473**

The **RBI and NABARD** have supported the propagation of micro finance considerably through the SHG-Bank Linkage Programme (SBLP) and have designed incentives to support micro finance institutions in forming Joint Liability Groups (JLGs). Commercial Banks are incentivised to lend to Micro finance institutions (MFIs) by placing MFIs under priority sector lending (PSL)4. PSL requirements mandate banks to ensure that 40% of their aggregate net banking credit goes to stipulated sectors that are considered important to foster financial inclusion.

- *Self Help Group Bank Linkage Programme (SBLP):* Designed and developed by the NABARD to promote and link Self Help Groups (SHGs) to banks in 1992, As on March 2011, NABARD has provided Rs. 25.45 billions to banks covering their lending to SHGs. Around 4.82 million SHGs received loans from banks with an outstanding amount of Rs 306.27 billion while 7.54 million SHGs have been linked to the banking system6. Despite this growth in the number of SHGs being linked with banks it is reported that there is almost no growth in loans in real terms as the average disbursed loan per SHG has declined in real terms from Rs 84,500 in 2010 to Rs 81,000 in 2011. In addition, it is also reported that compared to the previous year, the SBLP had underperformed during the year 2011-20128.

Women SHGs Development Fund: The Union Budget 2011-2012 has proposed to set up a "Women's SHG's Development Fund" with a corpus of Rs. 500 crore. The GoI created this fund to empower women and promote their SHGs11 and it is operated by NABARD through its two major microfinance funds- Financial Inclusion Fund (FIF) and the Financial Inclusion Technology Fund (FITF).

The FIF primarily supports capacity building inputs to service providers, resource centres, training institutes, financial institutions as well as promoting and nurturing SHGs. This fund will also support pilot projects for development of innovative products, processes and prototypes for financial inclusion. Likewise, FITF promotes technology innovation and solutions as well as research relating to technological interventions for financial inclusion.

CHALLENGES FACED BY BANKS IN INDIA TO FINANCIAL INCLUSION

There are many challenges faced by banks in India on financial inclusion process. Even though there are many villages in the country without bank branches, penetration of bank branches in to rural areas is difficult as they are unviable, saturated and having higher transaction cost. The villages are fragmented limiting the scale of operation of banks in rural areas. This necessitates last mile of financial inclusion to be met with a combination of agents and providers through technology leverage. The present Business Correspondent (BC) model is too restrictive, cash delivery points are too modest and the ideal financial inclusion model is yet to evolve in the country. The robust financial inclusion model requires comprehensive participation of all stakeholders which is currently lacking in the country. Financial inclusion among urban poor warrants an alternate strategy as the physical access is not the critical issue here. The pricing of financial assets and services is delicate in urban areas as it should ensure the poor are able to afford them at these prices. Also urban poor, particularly the slum dwellers suffer from identification problem as they are frequently moving from one part of the city to another or from one city to another. Lack of financial literacy among the urban poor or lack of marketing of financial instruments to the urban poor lead to limited awareness of financial portfolios by these people. Sometimes there is a self exclusion by the poor from the formal system as they are heavily depended on the informal credit sources which cater according to their convenience. Today complex financial services market offers consumers a vast array of products and service providers to meet their financial needs. This degree of choice requires that consumers be equipped with the knowledge and skills to evaluate the options and identify those that best suit their needs and circumstances. There is urgent need for financial education to make an informed choice from diverse options available to consumers and also refrain from financially destructive transactions. Unfortunately the level of financial literacy is very low in India. In this scenario, the Committee on Financial Inclusion (2008) gave six approaches to tackle the issue of financial inclusion in India. These include credit to the farmer households, bank advice on agriculture related matters, opening branches in villages with large population, simplification of the procedures in relation to granting of loans to small borrowers, further strengthening the SHG-Bank Linkage Programme (BLP), and effective implementation of business facilitator and correspondent model.

CONCLUSION:

In achieving inclusive growth in India, the Financial Inclusion will play a vital role and help the nation to drive away the not only rural poverty but also urban poverty in India. It is the duty of every Indian citizen to ensure that all the Indian will have bank account and everybody should take part actively in achieving 100% financial inclusion in India.

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