Financial Inclusion and Urban cooperative banking system in India

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Abstract

Financial inclusion is important priority of the country in terms of economic growth and development of society as it enables to reduce the gap between rich and poor. It helps to channelize money-flow to the economy and also ensures people who are unable to access financial system so far can access it with ease. The paper discusses the role of financial inclusion in the economy and how financial inclusion through urban cooperative banks can be a viable option for inclusive growth in India.

Keywords: Financial Inclusion, Banking System, RBI, UCB, Economic Growth,

Introduction

A vast segment of India's population exists on the margins of India's financial systems. There is growing concern about people being 'under-banked'. Financial inclusion is important priority of the country in terms of economic growth and development of society as it enables to reduce the gap between rich and poor. It helps to channelize money-flow to the economy and also ensures people who are unable to access financial system so far can access it with ease. Financial Inclusion poses policy challenges on a scale and with an urgency that is unique for developing countries which house more than 90% of the world's unbanked population. Developed countries policy makers have recognized that there are complex and multi-dimensional factors that contribute to financial exclusion and therefore require a comprehensive variety of providers, products and technologies that best suits the socio-economic, political, cultural and geographical conditions in these countries. India's experience as a developing country towards ensuring financial inclusion and weeding out financial exclusion has been unique. Indian economy has achieved a phenomenal economic growth during the last decade or so. But this growth has not been inclusive. Also, though poverty or the number of poor is decreasing over the years, the trend is not substantial. By being local in nature and intricately interwoven with the local community, cooperative banks have a clear advantage over commercial banks for financial inclusion.

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Labor costs of cooperative banks are considerably less than that of commercial banks and generally operating costs are also minimal. It is evident that cooperative banks have feasible options for inclusive growth through rural development, creating opportunities for employment, income generation. Financial inclusion - access to financial services - is increasing worldwide, often with official support. An effort has been made in this paper to assess the impact of the initiatives taken by RBI towards greater 'Financial Inclusion' & what more needs to be done to achieve full & meaningful financial inclusion?

Urban Cooperative Banks (UCBs) in corporate circles or even public sector commercial banking and chances are that you will evoke a smirk of dismissal. There are over 1,650 UCBs with close to 7,000 branches in the country. Yet they form a tiny part of the banking system accounting for less than 3% of the total banking assets and deposits and less than 3.5% of total advances. They also follow the 80-20 rule to the "T". The top 20% of UCBs account for almost exactly 80% of its deposits. In spite of being present in 25 states, much (almost 80%) of the action happens in the five states of Gujarat, Maharashtra, Andhra Pradesh, Karnataka and Tamil Nadu – with the lion's share going to Maharashtra. As on March 31, 2010, the state accounted for over a third of all UCBs, almost half of all UCB branches, around 60% of total extension counters of UCBs and more than 85% of all its automated teller machines (ATMs). Accordingly, more than 60% of the total banking business of the UCB sector was concentrated there but their numbers have been dwindling in recent years. During 2000-2010, 132 banks had their licenses cancelled and 62 merged with other banks. In this scenario, it is perhaps understandable why this sector does not exactly steal the limelight in banking policy discussions.

Appendix table V.3: State-wise distribution of UCBs (end-March 2011)								
State	Total number of UCBs	Total number of branches (including head office cum branches)	Total number of Extension Counters	Total number of ATMs	Number of districts with a presence of UCB branch	Number of districts without a presence of UCB branch	Deposits (Rs. Cr.)	Advances (Rs. Cr.)
1	2	3	4	5	6	7	8	9
1.Andhra Pradesh	106	260	6	3	21	2	5,348	3,963
2.Assam	8	22		0	5	22	438	187
3.Bihar	3	5	1	1	2	22	65	33
4.Chhattisgarh	12	22	2	0	8	10	369	120
5.Delhi	15	79	1	0	1	0	1,563	854
6.Goa	6	66	1	0	2	0	1,696	1,019
7.Gujarat	243	853	2	70	24	1	22,422	13,250
8.Haryana	7	17	1	0	7	13	397	219
9.Himachal Pradesh	5	9	1	0	3	3	346	193
10.Jammu & Kashmir	4	19	4	0	6	16	307	156
11.Jharkhand	2	2		0	2	36	17	9
12.Karnataka	268	840	9	18	30		14,333	9,602
13.Kerala	60	358	2	1	14	0	5,522	3,844
14.Madhya Pradesh	52	90	1	0	23	26	1,317	624
15.Maharashtra	539	4526	117	1003	35	0	1,38,124	90,260
16.Manipur	3	10	1	0	2	7	176	80
17.Meghalaya	3	4		0	3	4	106	49
18.Mizoram	1	1		0	1	7	23	8
19.Orissa	12	46	4	0	13	17	1,017	578
20.Puducherry	1	6	0	0	1	3	122	100
21.Punjab	4	19	1	0	2	18	717	356
22.Rajasthan	39	200	3	3	23	10	3,711	2,159
23.Sikkim	1	3			2	2	13	9
24.Tamil Nadu	129	313	0	4	32	0	4,822	3,773
25.Tripura	1	2		0	2	3	1	9
26.Uttar Pradesh	70	242	19	9	39	33	4,052	1,953
27.Uttarakhand	5	61	2	3	8	5	2,037	1,340
28.West Bengal	46	103	2	3	11	8	2,969	1,593
All India	1645	8178	180	1118	322	268	2,12,031	1,36,341
Note: Data are provisional.								

Source: rbi.org.in

Review of Literature

"Financial Inclusion" was formally articulated by Dr. Y. V. Reddy, Governor, RBI, in the 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 population, urged banks to review their existing practices to align them with the objective of financial inclusion. The main features of the approach involve 'connecting' people with the banking system and not just credit. Taking a cue from the Rangarajan Committee, which first studied the issue of Financial Inclusion in depth, Financial Inclusion is defined as the process of ensuring access to financial services and timely and adequate credit where needed by vulnerable groups such as weaker sections at an affordable cost from mainstream financial institution. As Dr. Chakrabarty, Deputy Governor, RBI explains only the mainstream financial institutions have the capacity to provide full services and meet the SCRIPT by extend in the complete breadth of services Savings, Credit, Remittance, Insurance, Pension, Payments transactions. Mainstream institution i.e., banks must fulfill their core function of intermediating and transferring resources from surplus to deficit units but both deficit and surplus units are those with low incomes, consequently the RBI moved swiftly to enforce multiple policy level changes ranging from provision of new products, relaxation of regulatory guidelines and other supportive measures to achieve sustainable and scalable financial inclusion, to ensure that customers who are linked to the banking system is provided with all the basic financial products that are required to enhance their income generation capacity thus helping them to work their own out of poverty. In November 2005, a new concept of basic banking 'no-frills' account with 'nil' or very low minimum balance was introduced to make such accounts accessible to vast sections of the population. In January 2006, the Reserve Bank permitted banks to engage Business Facilitators (BFs) and Business Correspondents (BCs) as intermediaries for providing financial and banking services. KYC requirements for opening bank accounts were relaxed for small accounts in August 2005, thereby simplifying procedure. To facilitate easy opening of accounts especially for small customers, KYC guidelines have been simplified to such an extent that small accounts can be opened without any documentation by just giving a self certification in the presence of bank officials. Financial Literacy is an important adjunct for promoting financial inclusion. Through Financial literacy and education, we disseminate information on the general banking concepts to diverse target groups, including school and college students, women, rural and urban poor, pensioners and senior citizens to enable them to make informed financial decisions.

Methodology

The present study is based on secondary data. The report of trend and progress of banking in India by RBI, annual report of NABARD (National Bank for Agriculture and Rural Development), Report of the Task Force to Study the Cooperative Credit System and Suggest Measures for its strengthening by RBI have been used as the data base.

Steps towards financial inclusion by RBI

RBI has been giving adequate attention and has stepped in whenever it felt that the banking community as a whole has missed out or not given the desired attention to certain areas. This is the reason why the Reserve Bank is placing a lot of emphasis on financial inclusion. In India, the focus of the financial inclusion at present has been confined to ensuring a bare minimum access to a savings bank account without frills with a limited overdraft facility to all. RBI has framed guidelines with a view to achieving greater financial inclusion, 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. The nature and number of transactions in such accounts would be restricted and made known to customers in advance in a transparent manner. Efforts are being made so that all banks give wide publicity to the facility of such no frills account to ensure greater financial inclusion. Banks and financial institutions have to take a lead here for achieving our objective of reaching out to people. Cooperative banks and regional rural banks being local level institutions are well suited for achieving financial inclusion. Being local institutions they are ideally suited for achieving Financial Inclusion. The use of IT solutions for providing banking facilities at people's doorsteps holds the potential for scalability of the Financial Inclusion initiatives. Many Pilot projects have been initiated in various States using smart cards for opening bank accounts with bio-metric identification. However, we have to now ensure that the gains and lessons from these Pilot projects are translated into an achievable, affordable and implementable plans on a pan India basis to leverage the benefits of inclusive growth, otherwise all our hard work in recent years would fizzle out without many tangible benefits.

Role of UCBs in achieving financial inclusion

Traditionally, we have seen and observed that the poor have not been welcomed to the banking fold by the banks and financial institutions with a misconception that they are not bankable and there is no business opportunity in offering services to the under-privileged and poor people in the semi-urban rural and slum-dwellers in the metropolitan cities. Banks and financial institutions had been till recent times financially excluding these people on the pretext that;

- They have no or few assets,
- They have nothing to offer as collateral,
- They have no business experiences,
- They cannot be trained for availing financial services,
- They have no credit history, and
- They cannot understand the nuances of banking due to illiteracy or less education.

Financial inclusion is the zeitgeist of the contemporary world; we can barely construct a successful society if we tended to get away from the trend. It is regrettable that our banks have had a rather unedifying record in terms of accepting the spirit of the time. Anand Sinha, Deputy Governor of the RBI has said the hoi-polloi inhabiting the country's semi-rural and rural areas is still unbanked and under-banked. The banks' services are exclusive of this huge population. In Mr Sinha's view, the urban cooperative banks could play an important role in bringing the poor within the banking framework. As the poor could barely access commercial banks, the UCBs could cover them. Altogether, the cooperative banks are a crucial link in the situation and their further expansion would do a lot of good in terms of financial inclusion. It is significant that both Sinha and the Y.H.Malegam Committee have favoured a greater presence of UCBs in the areas that are yet to be banked.

Conclusion

Financial Inclusion has not been picking up despite best of intentions and efforts from the authorities. The reasons can be:

1. The general apprehension among the people that they get noticed or there can be some harassment or their secrets get shared with official agencies which may lead to some embarrassment in their perception which has no basis.
2. Illiteracy to understand and comply with the formalities is the other reason, which keeps people away from formal institutions.
3. The products banks offer do not suit their immediate requirements. What they require is some confidence that they will be able to get some loans as and when they want without much of formalities.
4. The timing is the essence of their problem to come to the banks' fold. Most of these people are some small retailers/vendors, labourers, some technically skilled workers like plumbers, electricians, auto mechanics, house maids, drivers, bullock cart owners, rickshaw pullers, iron scrap collectors and dealers etc., and their work starts early in the morning and the bank timings do not at all suit them.

Today, we need to understand that Financial Inclusion is critical for achieving inclusive growth in the country. To achieve that, we have to expand our scope of financial inclusion initiatives to reach out to people at the grass-root level. Intensification of the efforts in the right direction and appropriate policy support should enable the inclusion agenda move closer to the target.

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