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Financial Inclusion in India: Key to Holistic Economic Development

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ABSTRACT

It has been seventy years since we got freedom and all the governments from then onwards have made several frontal development efforts in all the fields including the banking and financial system. Yet, a large section of population in India in particular and world over in general is excluded from core banking services. Around 22 percent of population still remains under below poverty line and their income is less than what is required to survive. Growth with equity has always been prime objective of all policy developments. However the gap has been widening up between the rich and the poor. Financial system is that one sector where this divide is seen and the elite section of society enjoys more sophisticated banking services and products while excluding large section from their outreach. The paper penetrates into discussing current status of India with regards to financial inclusion and leading endeavors of governments in achieving this milestone.

INTRODUCTION

It is widely accepted that there is a positive correlation between development and financial inclusion. However this correlation got tremendous boost in recent times. Given India's massive population size, achieving greater inclusive growth and financial development saw varied endeavors on the part of government of India including Jan Dhan Yojana, Paytm payment banks, Atal pension yojana among others.

With more than half of population living below BPL, access to finance by each and every one living in that segment becomes a major challenge given the documentation required in financial system. Poor, marginalized are the most vulnerable people and that idea of inclusive economic and financial development will require to bring them within the reach of financial system with access to bank account, a simplified system to save and invest , and to obtain credit.

Banking industry underwent several drastic changes in the last two decades ranging from lesser documentation to hi-tech developments in industry including online bank platforms to innovative financial products and services like ATMs, debit and credit cards etc.

However the technological development has created a divide and various financial innovations remain confined to elite sections of society. Given that several backward people are yet to get acquainted with modern cellular phones, internet access, banking industry has seen a pattern showing only a certain section using modern sophisticated products which raises the question of inclusive financial development.

In its landmark research work titled "Building Inclusive Financial Sectors for Development" (2006), more popularly known as the Blue Book, the United Nations has raised the basic question: "why are so many bankable people unbanked?" An inclusive financial sector, the Blue Book says, would provide access to credit for all "bankable" people and firms, to insurance for all insurable people and firms and to savings and payments services for everyone.

Today, the issue of financial inclusion is not just confined to India, but it is a concern for all economies world over. Attaining inclusive development requires that all developmental strategies emphasize on left out segment equally.

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OBJECTIVES OF STUDY

- Exploring the importance of financial inclusion for economic and social development of society.
- Reviewing current status of financial inclusion particularly in India and world in general.
- Reviewing the steps taken by governments in this regard to bring more and more people into the system.
- Analyzing that to what extent the steps and measures taken by governments have been successful in achieving financial inclusion.

METHODOLOGY OF STUDY

Distinct information and data for research can be utilized from various primary as well as secondary sources. Under our study secondary research was carried out to find out present status of financial inclusion in India for which information from published articles, newspapers, journals govt. reports and websites have been collected. Websites of institutions like RBI and reports from various expert committees submitted to govt. have been used. Also, personal interviews were conducted as primary source of information.

FINANCIAL INCLUSION: AN OVERVIEW

The term financial inclusion has been debated a lot with different people having varied views. However the essence of financial inclusion is to bring those people within the ambit of financial system who were previously excluded. Though there is no universally accepted definition, it is essentially defined in term of exclusion from the financial system. Anyone having excess to particular financial product or service is considered financially included. However time has seen drastic changes and now it just does not mean physical access but covering access to diversified financial products and services and their use and understanding.

Rangrajan's committee on financial inclusion defines it as:

"Financial inclusion may be defined as the process of 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"

Financial services include a range of services including insurance and payment & settlement services. The main aim is to bring unbanked people into formal financial system and bring them out of poverty. However the focus has been persisting on delivering credit.

Access to finance can be divided into following segments

- Those having access to any bank or bank like institution
- Those having access to services from non-bank financial institution but not using bank services
- Those having access to informal service providers
- Population having no access to any financial service.

In the measurement of financial inclusion, a reverse approach of financial exclusion is adopted, since inclusion is perceived to be difficult. Inclusion essentially focuses on outreach to financial product or services. Parameters like number of bank accounts, numbers of bank branches which have generally been used as measure of financial inclusion provide only half-truth information on the level of financial inclusion in an economy.

In India, financially excluded sections include marginalized farmers, landless laborers, slum dwellers, migrants, tribal, socially excluded people among others. There are a number of factors due to which institutional credit in rural areas is yet to come in each and everyone's outreach like risk perception, cost of assessment and management, lack of rural infrastructure, huge geographical spread of rural areas with more than half a million villages, some sparsely populated.

NSSO survey result:-

The committee debated that aspects like savings, remittance facilities, insurance etc. are fundamental. However what is at the core of determining inclusion into or exclusion from financial system is access to credit.

According to NSSO data, 45.9 million farmer households in the country, which is 51.44%, out of a total of 89.3 million households does not access credit either from institutional or non-institutional sources.

IMPORTANCE OF FINANCIAL INCLUSION

Financial inclusion provides a means to under privileged and neglected strata of society to save in order to absorb the economic shocks. It not just targets to provide minimal financial services but also leads to holistic economic development. And hence robust policy formation for financial inclusion has far reaching economic and social ramifications.

Even today, in India, the most widely and frequently used source of credit among medium and lower income households is moneylender or informal sector. Banking yet remains hampered by political and bureaucratic interventions which limits the banks' willingness to reach out to marginalized people. A wide section of India's poor including unskilled and semi-skilled, tribal remains unbanked or away from the reach of formal financial system. Also many young newly born small enterprises find it grossly difficult to obtain credit for their smooth functioning in their early ages from organized financial system and hence financially excluded. In India, over 40% working population earn but have no formal saving platform. Financial inclusion will go a long way in providing protection to poor from unscrupulous moneylenders.

Apart from the benefits of equitable growth, financial inclusion will make it possible for the government to transfer payments under its ambitious schemes like MGNREGA or LPG subsidies directly to the beneficiaries and eliminating corrupt middlemen. It will also increase the customer base of banks proving low cost deposits and help manage asset liability mismatch in a better way.

RATIONALE OF THE STUDY

According to census 2011, only about 58.7% of households are using formal banking services. Only 55 per cent of population has deposit accounts and 9 percent have credit accounts with banks. There is no doubt financial development and economic development go hand in hand. Therefore all economies endeavor to make their financial system robust and efficient. India has also set up a committee under the chairmanship of Mr. C. Rangrajan to suggest measures to increase financial inclusion and

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hence called Rangrajan committee on financial inclusion.

However several questions emerge on the issue that why financial inclusion needs policies. Like any other product or services why can't it find a market of its own. The reasons are multifaceted-

A) Financial exclusion- it has been observed that there a demand for financial services but these have not been provided, therefore these are used by only a certain segment of population. Those excluded include rural, poor regions, and those living in harsh, extreme conditions. Therefore this vast excluded segment has to rely upon unscrupulous money lenders, wherein, the poor get trapped in vicious circle and then never get out of the abject poverty.

B) High cost- with already low levels of income many people find it extremely difficult to bear chargers of financial products and services and so remain out of reach of sophisticated services. Hence, even if services are made available they show no inclination to avail given their economic constraints.

C) Non-price barriers- accessing formal financial services requires documentation on the part of customers which poor and undocumented people find difficult to establish their identity and income proof. Other than infrastructural problems of older times, non-access to internet and its understanding by poor has become a modern barrier to avail various services made online available.

D) Behavioral aspects- A study in behavioral economics has demonstrated that a lot of people find it uncomfortable to use formal financial services largely because of difficulties in understanding language, documentation requirement and complex conditions which come with financial services etc.

WHO ARE THE EXCLUDED AND WHY?

Many people are excluded from mainstream banking ranging from very low income poor to people with low or no information. Main reasons behind financial exclusion are-

a) Unavailability of information- low or no information concerning bank branches, services and products, interest rates keep people excluded from mainstream banking.

b) Documentation requirement- a lot of people find it difficult to produce proper documents before banks for availing services like opening bank account or obtaining loan.

c) Unawareness- many people are not aware of banking terms and conditions defined time to time.

d) Exorbitant charges- commercial banks levy charges on transactions including on non-availability of minimum balance, quarterly charge, annual charge, debit card charges, SMS alert etc.

e) Lack of access- those people living in geographically isolated regions find it difficult to avail banking services. Even majority of rural people also find it difficult as most of the commercial banks are established in the vicinity of cities away from the rural areas.

f) Illiteracy- due to illiteracy or very low education level many people find it difficult to understand banking system.

FACTORS AFFECTING ACCESS TO FINANCIAL SERVICES

There are several factors which keep a large number of people at bay from using financial services and therefore find themselves excluded from formal financial system.

Gender issues

Though women may have or open bank accounts but access to credit is often restricted to women who have or can hold title to assets like land and buildings and other property or they must obtain male guarantees for the purpose of borrowing.

Age factor

It has been observed that the financial service providers generally target middle of economically active population and they overlook older or younger potential customers in designing suitable products for them.

Legal identity

Lack of proper documentation for accessing financial services like identity cards etc. often exclude women, economic and political refugees and migrant workers.

Limited literacy

A vast segment of poor and illiterate people do not have financial literacy and understanding of banking system. It becomes biggest constraint or challenge to bring them within the web of banking system.

Place of living

It's not just matter of distance to bank from remote area but lack of rural transportation and infrastructure and sometimes high mobility of people with no fixed or formal address which keep many away from formal banking services.

Psychological and cultural barriers

There is feeling particularly among low income groups that banks are for richer and that they are not concerned about them make way for their self-exclusion from the system. Moreover, some beliefs and faiths in religious communities also keep them away from accessing financial services.

Bank charges

In some countries most of the transactions are done free of any charge till the time required balance is maintained. However in some other countries charges are exorbitant which fall disproportionately on poor who often find unbearable.

Terms and conditions

Several terms and conditions associated with use of financial products and services like minimum monthly average balance etc. dissuade may people from utilizing such products and services.

Type of occupation

Many banks are yet to develop their capacity to evaluate loan applications of small borrowers and unorganized enterprises and hence due to their higher risk perception tend to deny credit.

COSTS AND CONSEQUENCES OF FINANCIAL EXCLUSION

The costs and consequences of financial exclusion may be of two types- financial and social. From financial perspective, it affect**s** individual entities access to credit which ultimately affect their opportunities to grow in the industry. And from social perspective, it limits the output and loss of welfare and country's growth potential. The more tangible outcomes of financial exclusion include cost and security issues in managing cash flow and payments,

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compromised standard of living resulting from lack of access to short term credit, higher costs associated with using informal credit, increased exposure to unethical, predatory and unregulated providers, vulnerability to uninsured risks and long term or extended dependence on welfare as opposed to savings (Chant Link and associates, 2004).

Both financial and social consequences can arise at the same time.

According to 2011 census report, 70 percent of Indian population live in rural areas. Some people who live in backward areas don't have bank accounts. They face difficulties dealing with cheques made out in their name by any person. They have to pay to cash their cheque.

Lacking a transaction bank account with payment facilities can make payment of bills costly particularly when such accounts are the norms and outlets for pying in cash are closed (BMRB, 2006; Corr 2006; Kempson and Whyley, 1998; Kempson et al, 2000).

Cost of banking services are higher for those who don't have continuous relationship with bank thereby leading to higher costs for them. We sometime see offers in newspapers or during online shopping that if we pay through debit or credit card, we will get discounted rates. So, people who don't have these cards are not able to get discounts. It is also difficult to get employment in countries where payment of wages is by electronic transfer into a bank account (Citizens Advice, 2006; Treasury Committee, 2006b).

Also, not having access or not knowing how to use properly bank services can, depending on history, status and life experience of people facing it, have an impact on self esteem and lead to self-isolation and depravation of social connections and social relationships with friends or family (Gloukoviezoff, 2004). So, this is social cost or consequence of financial exclusion.

People who are not able to get credit from banks have to resort to intermediaries or we can say zamindars which involve high cost and restricted conditions. People can fall into greater financial difficulties and over- indebtedness because of terms and conditions applied to mortgage or subprime products. Some credit providers also apply extra fees for extending credit or issue penalties for defaulting. Without savings, people have no means of coping with even small financial shocks or unexpected expenses and those who keep savings in cash do not benefit from interest payments (Kempson, E., McKay, S. and Collard, S. 2005).

PROGRESS IN FINANCIAL INCLUSION

Financial inclusion gain importance after the recommendations of the Rangarajan Committee in 2008. Banks began to realize the importance of connecting with more people for business growth. FI thus became an integral part of business of banks because one of the objective of FI is to pull poor community out of the exploitative moneylenders. So, RBI advice all private and public banks to submit Three year financial inclusion plan (FIP) starting from April 2010. RuPay (an Indian domestic debit card) was introduced on 26 March 2012 by the National Payments Corporation of India (NPCI) as a part of financial inclusion initiatives. It created better digital infrastructure. After the launch of FIPs, banks are progressing in areas like opening of bank outlets, opening of Bank Savings Bank Deposit Accounts (BSBDAs), deploying BCs, grant of credit through Kisan Credit Cards and General Credit Cards. The progress made on these parameters is reported to RBI by banks on monthly basis and the progress as on end March 2017 is given in Table below-

Particulars	End- March 2010	End- March 2016	End- March 2017
1	2	3	4
Banking Outlets in Villages – Branches	33,378	51,830	50,860
Banking Outlets in Villages>2000-BCs	8,390	98,958	105,402
Banking Outlets in Villages<2000- BCs	25,784	432,271	438,070
Total Banking Outlets in Villages – BCs	34,174	531,229	543,472
Banking Outlets in Villages- Other Modes	142	3,248	3,761
Banking Outlets in Villages -Total	**67,694**	**586,307**	**598,093**
Urban Locations covered through BCs	447	102,552	102,865
BSBDA-Through branches (No. in million)	60	238	254
BSBDA-Through branches(Amt. in ₹ billion)	44	474	691
BSBDA-Through BCs (No. in million)	13	231	280
BSBDA-Through BCs (Amt. in ₹ billion)	11	164	285
BSBDA-Total (No. in million)	**73**	**469**	**533**
BSBDA Total (Amt. in ₹ billion)	**55**	**638**	**977**
OD facility availed in BSBDAs (No. in million)	0.2	9	9
OD facility availed in BSBDAs (Amt. in ₹ billion)	0.1	29	17
KCCs -Total (No. in million)	24	47	46
KCCs -Total (Amt. in ₹ billion)	1,240	5,131	5,805
GCC-Total (No. in million)	1	11	13
GCC-Total (Amt. in ₹ billion)	35	1,493	2,117
ICT A/Cs-BC-Total Transactions (No. in million)	27	827	1,159
ICT A/Cs-BC-Total Transactions (Amt. in ₹ billion)	7	1,687	2,652

Source: Reserve Bank of India Annual Report 2016-17

During 2016-17, banking outlets in villages increased by 12,243, while the no. of accounts opened increased by 49 million. Similarly, total no. of transactions through the BC channel increased by 332 million, while the amount transacted increased by 965 billion. RBI has taken several steps to provide banking facilities in all unbanked villages in the country. A total of 74,414 villages with population more than 2000 were identified and allotted to various banks for coverage. As on March 31, 2017, 96 percent of the total villages allotted had been covered comprising of 19,875 villages through brick and mortar branches, 431,359 villages through BCs and 20,902 villages through other modes.

Also, Pradhan Mantri Jan Dhan Yojna has been designed to accelerate financial inclusion by providing access to financial services to all citizens of country like basic savings bank accounts, affordable credit, remittances facilities, insurance and pension facilities. The no. of new savings accounts has been phenomenal under the scheme.

Table: Progress of PMJDY up to 9th May 2018

Group of banks	**No. of new savings bank accounts opened (in millions)**	**Deposits accumulated (in Rs. Millions)**	**No. of Debit cards issued (in millions)**
Public sector banks	255.3	652182.5	192
Regional rural banks	50.7	137170.3	36.8

Private sector banks	9.9	22681.3	8.2
Total	316.6	812035.9	238

Source: PMJDY website

The benefit of such huge customer base is expected to provide huge benefit to consumers and banks in coming years.

INITIATIVES FOR FINANCIAL INCLUSION

- Banks Savings Banks Deposits Accounts: RBI advised all banks to open BSBDAs with minimum common facilities such as no minimum balance, deposit and withdrawl of cash, facility of providing ATM card etc.
- Simplified KYC norms: It helps to facilitate easy opening of bank accounts especially balances not exceeding Rs. 50,000 and aggregate crtedits not exceeding Rs. One lakh a year. Banks are allowed to use Aadhar card as a proof of both identity and address.
- Opening branches in unbanked villages: Banks are compulsorily required to allocate 25% of their total branches in unbanked villages.
- Financial Inclusion Plans: As discussed above, public and private sector banks are advised to submit 3 year FIPs.
- Private Corporates: few large corporate have undertaken projects like E-Choupal/ E-Sagar(ITC), Haryali Kisan Bazaar (DCM), Project Shakti(HUL) etc. These projects will bring improvement in the lives of participants and helps in economic development which is significant for Financial Inclusion.
- **Stand up India-** Under this scheme, every single branch of a public sector bank is asked to support one entrepreneur each from women and SC/St. category.
- **Swabhiman campaign**: It was introduced in 2004 on the recommendations of C. Rangrajan Committee. It focused on including people from rural areas into Banking Services and linking them in the financial sector. Under this public in rural areas is made aware of the benefits of financial services.
- Jan Dhan Account: similar to BSBDAs, these accounts were opened under Pradhan Mantri Jan Dhan Yojna. Jan Dhan account holder is compulsorily issued RUPAY debit card and many more services.

- Payment banks: These banks only accept deposit from public and will not lend loans. These payment banks provide payment services and deposit products to its target customers which are small businesses and low-income households. Till date 11 licenses have been granted out of which four banks are functional which are – Paytm, Airtel, Indian postal payment bank, Phinopayment.
- Small finance banks: Banks with a small finance bank license can provide basic banking service of acceptance of deposits and lending.
- Village Knowledge Centres: Union Bank of India established village knowledge centres at strategic rural locations for educating and updating rural people and farmers about latest technological developments.
- Pilot Project: In Andhra Pradesh, govt has started pilot project with six banks to make payments of social security pensions and AP Rural Employment. Those six banks are SBI, SBH, Andhra Bank, union Bank, UtTI Bank and AP Grameena Vikas Bank.
- Govt. of India has constituted two funds: Financial Inclusion Fund for meeting the cost of developmental and promotional

intervention of financial inclusion and Financial Inclusion Technology Fund to meet the cost of technology adoption.

- Atal Pension Yojna: It is a pension scheme which was launched for unorganized sector like drivers, gardeners, maids etc.

PROBLEMS AND CHALLENGES

- Corruption is major problem in India. Decisions are made at top level by leaders but these are not properly implemented at final level.
- Banks have to follow some rules which create hurdles for them in reaching to poor.
- Majority of population in India is financially illiterate. Even some educated people don't know how to write cheques or how to fill income tax returns.
- Many people don't maintain books of accounts. This leads to removing of these people from financial services of the banks.
- Migrants are facing difficulties in opening bank accounts. Commercial banks need to take care of the needs of migrant population in their financial inclusion plans.
- Adequate infrastructure such as digital and physical connectivity, uninterrupted power supply etc. are required for financial inclusion. Around 80,000 villages in India have no electricity and constraints of electricity directly affect the working of banks.
- Use of transaction account must be promoted. Some people open bank account but resort to use of cash for every transaction. People must be influenced to use bank accounts and make them functional so that they can get other financial services which can improve their economic welfare.

CONCLUSION

Despite making several efforts by the governments, regulators, financial institutions large chunk of sophisticated services and mainstream banking still remains away from the outreach of different sections across India. Though the motto of banking sector is to achieve higher profitability but it should not be at the cost of those excluded. Banks must come out with specific strategies to expand the outreach of their products and services for more financial inclusion. Developing linkages with micro finance institutions, NGOs, local communities can be one way. Moreover, banks must give wider publicity of providing no frill accounts. Financial literacy camps from time to time in remote areas, as well as modification of technological products like the use of ATM machines to make them user friendly may help illiterate start utilizing banking services. Banks can do it assuming as the business opportunity to expand their customer base though it may cost in the initial years as well as a means to comply with their corporate social responsibilities. Banks must venture out to even grab little margin per customer as this would translate into huge profits with wider customer base. They must go on to second order of thinking and take this as competitive advantage.

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