Financial Inclusion in India

Pinal Barot
Assistant Professor, Faculty of Business Administration, GLS University

Abstract: Finance has become an essential part of an economy for development of the society as well as economy of nation. For, this purpose a strong financial system is required in not only in under-developed countries and developing countries but also developed countries for sustainable growth. Through Financial inclusion we can achieve equitable and inclusive growth of the nation. Financial inclusion stands for delivery of appropriate financial services at an affordable cost, on timely basis to vulnerable groups such as low income groups and weaker section who lack access to even the most basic banking services. In this paper, the researcher attempts to understand financial inclusion and its importance for overall development of society and Nation’s economy. This study focuses on approaches adopted by various Indian banks towards achieving the ultimate goal of financial inclusion for inclusive growth in India and analyses of past years progress and achievements. The relevant data for this study has been collected with the help of from various Research journals, Articles, reports of RBI, reports of NABARD and online resources. As the majority of the rural population is still not included in the inclusive growth, the concept of financial inclusion becomes a challenge for the Indian economy. Since 2005, many concerted measures are initiated by the Reserve Bank of India and Government of India in favor of financial inclusion but the impact of these did not yield satisfactory results. For developing nations the era is of inclusive growth and the key for inclusive growth is financial inclusion. Financial inclusion or inclusive financing is the delivery of financial services, at affordable costs, to sections of disadvantaged and low income segments of society. There have been many formidable challenges in financial inclusion area such as bringing the gap between the sections of society that are financially excluded within the ambit of the formal financial system, providing financial literacy and strengthening credit delivery mechanisms so as to improvised the financial economic growth. A nation can grow economically and socially if it’s weaker section can turn out to be financial independent. The paper highlights the basic features of financial inclusion, and its need for social and economic development of the society. The study focuses on the role of financial inclusion, in strengthening the India’s position in relation to other countries economy. For analyzing such facts data for the study has been gathered through secondary sources including report of RBI, NABARD, books on financial inclusion and other articles written by eminent authors.

Key words: Financial inclusion, Financial Exclusion, Business correspondents, KCCs, GCCs

1. Introduction

The process of economic growth, especially when it is on high growth line, must attempt to take participation from all sections of society. Lack of access to financial services for small/ marginal farmers and weaker sections of the society has been recognized as a serious threat to economic progress, especially in developing countries. The recent developments in banking technology have transformed banking from the traditional brick-and-mortar infrastructure like staffed branches to a system supplemented by other channels like automated teller machines (ATM), credit/debit cards, online money transaction, internet banking, etc. The moot point, however, is that access to such technology is restricted only to certain segments of the society. Many of research reports and surveys clearly show that large numbers of population does not have an access to basic banking and financial services not only in India but also whole world. This is termed “financial exclusion”. These people, particularly, those living on low incomes, cannot be access mainstream financial services and products such as bank accounts which are used for making payments and keeping money, remittances, affordable credit, insurance and other financial services, etc..

Financial Inclusion is considered to be the core objective of many developing nations since from last decade as many research findings correlate the direct link between the financial exclusion and the poverty prevailing in developing nations. According to World Bank report “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 term Financial Inclusion needs to be interpreted in a relative dimension. Depending on the stage of development, the degree of Financial Inclusion differs among countries. It’s been surprising fact that India ranks second in the world in terms of financially excluded households after china.

For the inclusive growth process of economy the
central bank has also provided high importance to the financial inclusion. Normally the weaker sections of the society are completely ignored by the formal financial institutions in the race of making chunks of profits or the complexities involved in providing finance to the weaker section. Financial inclusion or inclusive financing is the delivery of financial services, at affordable costs, to sections of disadvantaged and low income segments of society. There have been many formidable challenges in financial inclusion area such as bringing the gap between the sections of society that are financially excluded within the ambit of the formal financial system, providing financial literacy and strengthening credit delivery mechanisms so as to improvised the financial economic growth. Unrestrained access to public goods and services is the sine qua non of an open and efficient society. It is argued that as banking services are in the nature of public good; the availability of banking and payment services to the entire population without discrimination is the prime objective of this public policy. Thus the term Financial Inclusion can 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.

II. Objectives of the study:

This research paper has four main objectives:
1. To understand the financial exclusion and its extent.
2. To understand the financial inclusion and its importance.
3. To analyse the current status of financial inclusion in Indian economy.
4. To analyse Financial Inclusion Opportunities and Challenges for India.

III. Concept of Financial Exclusion:

Before we understand financial inclusion we should have knowledge about financial exclusion. The word of financial exclusion first time used in 1993 by Leyshon and thrift who were concerned about limited access on banking services as a result number of bank branches were closed. In1999, kempsion and whyley defined financial exclusion in border sense which refers to those people who have excluded access to mainstream financial services and product till date numbers of analysts added their views to define financial exclusion.

“Financial exclusion” describes as a situation in which people do not have access to mainstream financial product and services such as banks accounts, credit cards and insurance policies, particularly home insurance, education loan. The effects of financial exclusion can include exclusion from other mainstream services, such as pension or saving schemes, and can also lead to debt and/or cut off from essential utilities.

3.1. Extent to financial exclusion in globally:

As per the report of the World Bank, in survey of 148 economics approximately 2.5 million people do not have an bank account and totally excluded from mainstream financial services and products. They do not have access to affordable financial services which is an ultimate tool for overcoming poverty and minimize income inequalities.

As per the world bank report only 50 percent adults population have an account in formal financial institutions while rest of remain unbanked. Where 54.7 percent male adults have an account in formal financial institutions, only 46.3 percent female adults have an account. This report reveals that 20.9 percent adults use an account to receive their wages and only 22.4 percent adults saved at formal financial institutions in the past year. 9.0 percent adults have taken loan from formal financial institutions in the year of 2011.

55 percent of borrowers in developing countries use only informal source of finance. Not only financially excluded people require the banking services but obstacle such as cost, distance and documentations create very critical situation.

3.2 Financial exclusion in India:

India is place of the largest unbanked population where, only 35 percent adults having an account in financial institutions which shows that percentage of account penetration in India just below rest of the developing world. About 50 percent of adults reports in Andhra Pradesh and Delhi NCR and 40 percent in Gujarat, Kerala, and Maharashtra having a formal account but Bihar, Orissa, and Rajasthan reports less than 30 percent account penetration. As per data available from Census 2011, India is having population of around 1.22 billion and 65 per cent of adults across the country are excluded from the formal financial system. As per the report of World Bank, In India, only 35.2 percent adults above the age of 15 years have an account at formal financial institutions. 55 percent population has deposit accounts and only 9 percent population have credit accounts with formal financial institutions. Reports show that there is one bank branch per 14,000 persons. Just 18 percent are debit card holders and less than 2 percent are credit cards holders. In India, despite expansion of bank branches post reform period, the total branches of commercial banks
including RRB’s and SCB’s has still stood only 48000 in a country to provide service to 6 lakh villages. So there is only one bank branch over the 12.5 villages. In India and other BRICS economies unbanked respondents reported obstacles to access formal accounts.

The most common reason for not having a bank account in formal financial institutions is lack of enough money, a barrier reported by 63 percent of unbanked adults. The second major reason: a family member already having an account was cited by 41 percent respondents. Distance, cost, and lack of necessary documentation were each cited by about 20 percent of unbanked respondents, rates exceeding those in other BRICS economies.

Thus, financial inclusion has become equally important issue of under – developed, developing and developed economies for inclusive growth. Through the process of financial inclusion we can overcome the situation of the financial exclusion.

![Graph showing barriers to use of formal accounts](image1)

Financial inclusion is one of the most important aspects in the present scenario for inclusive growth and development of economies. The financial inclusion term was first time used by British lexicon when it was found that nearly 7.5 million persons did not have a bank account. But financial inclusion concept is not a new one in Indian economy. Bank Nationalisation in 1969, establishment of RRBs and introduction of SHG-bank linkage programs were initiatives taken by RBI to provide financial accessibility to the unbanked groups.

According to committee on Financial inclusion headed by Dr. C. Rangarajan 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.”

Financial inclusion can be described as the provision of affordable financial services, viz saving, credit, insurance services, access to payments and remittance facilities by the formal financial systems to those who are excluded. So, financial inclusion refers to access to vast range of financial product and services at affordable cost. It not only includes banking products but also other financial services such as loan, equity and insurance products.

Wherever Times is specified, Times Roman, or New Times Roman may be used. If neither is available on your word processor, please use the font closest in appearance to Times that you have access to. Please avoid using bitmapped fonts if possible. True-Type 1 fonts are preferred.

Households need access to finance for several purposes like creating buffer, retirement, saving to hedge against unpredictable situations and take products for insurable contingencies. Household also needs access to credit for livelihood creation, housing, consumption and their emergencies. Finally households require financial services to access a wide range of saving and investment products for wealth creation but it is all depends upon their level of financial literacy.
4.2 Importance of financial inclusion:

Easy access to financial services will allow the population leaving in lower strata, to save money safely and help in preventing concentration of economic power with a few individuals, thus mitigating the risks that the poor could face as a result of economic shocks. Therefore, providing access to financial services is becoming an area of concern for the policymakers as it has far reaching economic and social implications.

1. In India, The single most frequently used source of loan for medium Indian household is still moneylender. Large parts of our financial system are still hampered by political intervention and bureaucratic constraints, limiting their potential contribution. India’s poor, many of who work as agricultural and unskilled semi skilled wage labours and low salaried workers are largely excluded from the formal financial system. Even micro and small enterprises, find it difficult to have an access to formal sources of finance and thus are largely excluded from financial system. Over 40% of India working population earn but have no saving. Financial inclusion provides protection to poor from the control of the spurious money lenders.

RBI's Policy Initiatives to foster Financial Inclusion

The initiatives taken by RBI can be broadly classified under reach, access, products and transactions.

a) Reach

(i) Branch expansion in rural areas

Branch authorisation has been relaxed to the extent that banks do not require prior permission to open branches in centres with population less than 1 lakh. To further step up the opening of branches in rural areas, banks have been mandated to open at least 25 per cent of their new branches in unbanked rural centres. In the Annual Policy Statement for 2013-14, banks have been advised to consider frontloading (prioritizing) the opening of branches in unbanked rural. This is expected to facilitate the branch expansion in unbanked rural centres.

(ii) Business Correspondent/ Business Facilitator Model

With the objective of ensuring greater financial inclusion and increasing the outreach of the banking sector, banks were permitted by RBI in 2006 to use the services of intermediaries in providing financial and banking services through the use of Business Facilitators (BFs) and Business Correspondents (BCs). Business Correspondents are retail agents engaged by banks for providing banking services at locations other than a bank branch/ATM. It enables a bank to expand its outreach and offer limited range of banking services at low cost, particularly where setting up a brick and mortar branch is not viable.

(iii) Combination of Branch and BC Structure to deliver Financial Inclusion

The idea is to have a combination of physical branch network and BCs for extending financial inclusion, especially in geographically dispersed areas. To ensure increased banking penetration and control over operations of BCs, banks have been advised to establish low cost branches in the form of intermediate brick and mortar structures in rural centres between the present base branch and BC locations, so as to provide support to a cluster of BCs about 8-10 BCs at a reasonable distance of about 3-4 kilometers.

b) Access

(i) Relaxed KYC norms

- Know Your Customer (KYC) requirements have been simplified to such an extent that small accounts can be opened with self-certification in the presence of bank officials.
- RBI has allowed ‘Aadhaar’ to be used as one of the eligible documents for meeting the KYC requirement for opening a bank account

Roadmap for Banking Services in unbanked Villages

- In the first phase, banks were advised to draw up a roadmap for providing banking services in every village having a population of over 2,000 by March 7,2010. Banks have successfully met this target and have covered 74398 unbanked villages.
- In the second phase, Roadmap has been prepared for covering remaining unbanked villages i.e. with population less than 2000 in a time bound manner. About 4,90,000 unbanked villages with less than 2000 population across the country have been identified and allotted to various banks. The idea behind allocating villages to banks was to ensure availability of at least one banking outlet in each village.

(c) Products

Bouquet of Financial services

In order to ensure that all the financial needs of the customers are met, we have advised banks to offer a minimum of four basic products, viz.

- A savings cum overdraft account
- A pure savings account, ideally a recurring or variable recurring deposit
- A remittance product to facilitate EBT and other remittances
- Entrepreneurial credit products like a General Purpose Credit Card (GCC) or a Kisan Credit Card (KCC)

(d) Transactions

Direct Benefit Transfer
The recent introduction of direct benefit transfer, leveraging the Aadhaar platform, will help facilitate delivery of social welfare benefits by direct credit to the bank accounts of beneficiaries. The government, in future, has plans to route all social security payments through the banking network, using the Aadhaar based platform as a unique identifier of beneficiaries. In order to ensure smooth roll out of the Government’s Direct Benefit Transfer (DBT) initiative, banks have been advised to:

- Open accounts of all eligible individuals in camp mode with the support of local Government authorities.
- Seed the existing and new accounts with Aadhaar numbers.
- Put in place an effective mechanism to monitor and review the progress in implementation of DBT.

V. Role of Financial Inclusion in the Development of Indian Economy.

Banking and financial services play very crucial role in the growth and development of an economy. Research shows that a well-functioning and inclusive financial system is linked to a faster and equitable growth. There is wide range of personal finance options for higher and upper middle income population in the form of financially engineered and innovative products whereas a significantly large section of population still lack access to the most basic banking services that is holding a bank account. This is termed as “financial exclusion” which further leads to social exclusion. So it is necessary to provide individuals with easy and affordable institutional financial products or services popularly called “financial inclusion”. Universally, it is accepted that the objective of financial inclusion is to extend the scope of activities of the organized financial system to include within its ambit the people with low incomes. In India, there is a need for coordinated action amongst the banks, the government and related agencies to facilitate access to bank accounts to the financially excluded. In view of the need for further financial deepening in the country in order to boost economic development, there is a dire need for expanding financial inclusion.

Twenty-three years after economic reforms unfurled in India, the financial sector still suffer from many maladies. There are various socio-cultural, economic issues that hinder the process of financial inclusion. For instance on demand side, it includes lack of awareness and illiteracy. From supply side, lack of avenues for investment such as poor bank penetration, unwillingness of banks to do financial inclusion or high cost involved in financial inclusion seem to be some likely reasons for financial exclusion. Normally the weaker sections of the society are completely ignored by the formal financial institutions in the race of making chunks of profits or the complexities involved in providing finance to the weaker section. It can also 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. Financial inclusion broadens the resource base of the financial system by developing a culture of savings among large segment of rural population and plays its own role in the process of economic development. Further, by bringing low income groups within the perimeter of formal banking sector; financial inclusion protects their financial wealth and other resources in exigent circumstances. Financial inclusion also mitigates the exploitation of vulnerable sections by the usurious money lenders by facilitating easy access to formal credit.

Financial inclusion is an innovative concept which helps to achieve the sustainable development of the country, by making available financial services to the unreached people with the help of financial institutions. The concepts of financial inclusion get popularity from 2000. Financial inclusion is concerned with providing financial and banking services on lower costs to low section and slum people of society. It can be a great weapon to overcome financial backwardness. Access to financial services plays a critical part in development by facilitating economic growth and reducing income inequality. Inclusive financial systems allow poor people to smooth their consumption and insure themselves against the much economic vulnerability they face—from illness and accidents to theft and unemployment. Financial inclusion enables poor people to save and to borrow—allowing them to build their assets, to invest in education and entrepreneurial ventures, and thus to improve their livelihoods. It is likely to benefit disadvantaged groups such as women, youth, and rural communities. For all these reasons financial inclusion has gained prominence in recent years as a policy objective to improve the lives of the poor.

VI. Opportunities and Challenges

Financial Inclusion - Opportunities

1. With the help of financial inclusion concept, by saving small amounts over time, poor people can arrange funding for the lump investment needed in businesses like for purchasing equipments or buying goods at a wholesale price.
2. By fostering financial inclusion and encouraging saving habits can also provide funds for searching more productive sources of employment by providing access to easy finance and banking services to even in rural areas.

3. Electronic benefit transfer (EBT): With the help of EBT and information and communication technologies, banks can transfer social benefits electronically to the bank account of the beneficiary and can deliver government benefits at the doorstep of beneficiaries, thus reducing dependence on cash and lowering transaction costs.

4. For achieving commercially sustainable universal access, banking systems will be updated to new technologies like EBT to ensure the availability of financial services to all sections at a reduced cost and enhanced benefits like makes banking convenient which ensures being able to transact near where they live and work and ensuring trust among the peoples that they are putting their money with such organizations that seem to care for them and who they feel are going to be there for them when they need them the most.

5. Financial inclusion provides opportunities to the banking sector to cut across various strata’s of society, regions, gender, and income and encourage the public to embrace banking habit. Reserve Bank of India has intervened for the success of financial inclusion by introducing various enactments, financial literacy drives, leveraging technology etc.

6. Financial inclusion paves a way for growth and development by ensuring timely and quick availability among the needy sectors.

7. Financial inclusion will provide not only safe savings, but also offer many other allied services like insurance cover, entrepreneurial loans, payments and settlement facilities etc.

8. With an increase in business opportunities, national income of our country will also increase, which in turn results in increased GDP.

9. With the help of KYC norms and UID financial inclusion process speeds up the banking process which reduces the cash and noncash costs to both banks and customers.

10. Financial access will also attract global market players in our country that will result in increasing business and employment opportunities.

11. Financial inclusion will help the poor in meeting various needs with the help of a wide range of financial services which are readily available and affordable also. Financial services will provide tools which will help in providing easy financing facilities in many fields like microenterprises’ investments in new production technologies, helping in farmers’ purchasing productivity-enhancing inputs such as fertilizers, labourers’ search for better job opportunities, or children’s education and to mitigating people’s exposure to large Lifecycle events or unpredictable risks.

Thus, financial inclusion offers plenty of opportunities for growth and development in India

**Financial inclusion – challenges:**

The path of financial inclusion is full of various challenges like:

1. Financial services are used only by a section of the population; the excluded sections are rural, poor areas where it is difficult to provide these financial services which are mainly relying on informal sector (moneylenders etc.) for availing finance that is usually at exorbitant rates. The main challenge of financial inclusion is to include the rural and poor people in the coverage area.

2. Financial illiteracy is also one of the challenges in the area of financial inclusion. Lack of basic education prevents the people to have an access from financial services.

3. Poor living even in urban areas does not fully utilize the financial services as they find them costly and unaffordable which deter the poor from accessing them.

4. Another challenge in the area of financial inclusion is that access to formal financial services requires various documents of proof regarding persons’ identity, income, birth certificates, etc. But poor people generally lack these documents and thus are devoid of these services.

5. Poor and rural sections may sometimes subscribe these financial services initially, but may not use them as active as others due to high distance between the bank and residence, poor infrastructure etc. 6. Low income level is another challenging area in the process of financial inclusion because they think banks provides services only to rich class.

6. Due to difficulty in understanding formal languages, various documents and many formalities in banking procedure people are not comfortable in using financial services.
7. Many people who live in remote localities find it difficult to reach the areas where banks are generally situated.
8. Many people, who lack basic knowledge and education, do not know the importance of financial products like insurance, finance, bank accounts, cheque facilities etc is also the challenge in the implementation of financial inclusion.
9. Many financial institutions not able to justify on commercial grounds the establishment of broad-based infrastructure to serve poor households so they sometimes pull back to their physical presence in rural or poor areas and also place some restrictions to discourage the custom of poor people (e.g. high minimum account balances). As a result, they also pass the access cost on to customers, who had to travel to distant branches and face long queuing time. As a result, many poor people reject financial institutions that serve the middle and upper classes.

2. References

12. Reaching Out: Access to and use of banking services across countries, Thorsten Beck, Asli Demirguc-Kunt and Maria Soledad Martinez Peria, World Bank Policy Research, WPS 3754, World Bank, 2005 # - As per Trends and Progress of Banking in India, RBI, 2006-07 (Appendix Table III.35), end March 2007 there were 27,088 ATMs of Scheduled Commercial Banks in India.