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FINANACIAL INCLUSION AND INDIAN BANKING SYSTEM -A WAY FORWARD

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ABSTRACT

The nature of financial inclusion in India or other developing countries is different from developed countries. The number of financially excluded people is much larger in India compared to developed countries. Numerous studies on financial inclusion are done in developed countries; the researches concluded that the larger population is excluded from the financial facilities. In India, though the concept of financial inclusion is an old phenomenon, recently it is coming into prominence. It is estimated that, 40% of population is deprived of basic financial amenities. The present paper is an effort in throughing light on financial inclusion and banking in India. The Several steps have been taken by RBI and GOI to include more and more people under the umbrella of basic financial services.

Key Words: Financial Inclusion, Financial Exclusion, RBI, Economic Growth.

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BACKGROUND

Financial Inclusion is the process of ensuring access to appropriate financial products and services needed by all sections of the society in general and vulnerable groups such as weaker sections and low income groups in particular at an affordable cost in a fair and transparent manner by mainstream institutional players. In other words, 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 saving or current account with any bank. In reality it includes loans, insurance services and much more.

Rangarajan’s committee on financial inclusion defines it 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. By financial inclusion we mean the provision of affordable financial services, viz., access to payments, remittance facilities, savings, loans and insurance services by the formal financial system to those who tend to be excluded. It is important to recognize that in the policy framework for development of the formal financial system in India, the need for financial inclusion and covering more and more of the excluded population by the formal financial system has always been consciously emphasized. Bank nationalization in India marked a paradigm shift in the focus of banking as it was intended to shift the focus from class banking to mass banking. The rationale for creating Regional Rural Banks was also to take the banking services to poor people.

The importance of an inclusive financial system is widely recognized in policy formulation and recently financial inclusion has become a policy priority in many countries. Initiatives for financial inclusion have come from the financial regulators, the governments and the banking industry. Legislative measures have been initiated in some countries.

OBJECTIVES

The paper has been conceived with the following objectives in mind:

i. To understand the magnitude of financial exclusion and present scenario of financial inclusion in India
ii. To explain the role of financial inclusion in the economic growth of India
iii. To analyse growth and impact of financial inclusion in India
iv. To examine the role of banking sector in financial inclusion.
v. To suggest some possible solutions set for financial inclusion in India.

RESEARCH METHODOLOGY

The present study is exploratory in nature to provide a clear guidance for empirical research. It is also descriptive where the focus is on fact-finding investigation with adequate interpretation. For this purpose secondary data were collected. The secondary data were collected through newspapers, magazines, books, journals, conference proceedings, Government reports and websites.

MAGNITUDE OF FINANCIAL EXCLUSION INDIA

- In India, almost half the country is unbanked.
- Only 55 per cent of the population has deposit accounts and 9 per cent have credit accounts with banks.
- India has the highest number of households (135 million) excluded from Banking.
- There was only one bank branch per 16,000 people.
- In India, there are only 33495 rural branches in around 6 lakh villages.
- Only a little less than 20% of the population has any kind of life insurance
- Just 18 per cent of the population had debit cards and less than 2 per cent had credit cards.

The picture will be clearer, if we compare the number of bank branches with the number of villages; financial exclusion is not only limited to rural areas but predominant in urban areas also. A large proportion of urban poor is outside the coverage of basic financial facilities.

PRESENT INDIAN SCENARIO

In India the focus of the financial inclusion at present is confined to ensuring a bare minimum access to a savings bank account without frills to all. Internationally, the financial exclusion has been viewed in a much wider perspective. Having a current account or savings account on its own is not regarded as an accurate indicator of financial inclusion. Bank nationalization in India marked a paradigm shift in the focus of banking as it was intended to shift the focus from class banking to mass banking. The rationale for creating Regional Rural Banks was also to take the banking services to poor people. The new Branch Authorization Policy of Reserve Bank encourages banks to open branches in these under-banked states and the under-banked areas in other states.

The main reason behind financial exclusion is the lack of regular or substantial income which leads to a disqualification for granting a loan. The proximity of the financial service providers and the residence of the unserved people is another fact for financial exclusion. Apart from the above factors the non-awareness of banking products among the persons, easier access to the local moneylenders, stringency of banking norms etc. can also be triggered as a reason for financial exclusion.

There is currently a perception that there are a vast number of people, potential entrepreneurs, small enterprises and others, who are excluded from the financial sector, which leads to their marginalization and denial of opportunity for them to grow and prosper. Financial inclusion is not only essential because of its implications for the welfare of citizens but it needs to be stressed that it has to be an explicit strategy for fostering faster economic growth in a more inclusive fashion.

The Government of India has expressed its explicit concern on the issue of overall inclusion in the development process through its various initiatives such as the National Rural Employment Guarantee Scheme, the Bharat Nirman programme, the Sarva Shiksha Abhiyan, and the like. A committee on financial inclusion (Chairman: Dr. C. Rangarajan) was also constituted by the Government of India in June 2006 to recommend a strategy to achieve higher financial inclusion in the country. Unlike several central banks, which focus solely on inflation, many developed and emerging economies, including ours, focus also on growth.

DATA ANALYSIS AND INTERPRETATION

Financial inclusion denotes delivery of credit and other financial service at cost to the vast sections of the disadvantaged and low income groups. The objective of financial inclusion is to extend the scope of activities of the organized financial system to include within its ambit people with low income. Through credit, attempt should be made to lift the poor from one level to another so that they come out of poverty. To through light on above facts, the secondary data has been collected from the different sources and analyzed.

Table 1-Growth of scheduled commercial banks across India

	2003		2005		2007		2009		2010		2011	
	Num	%	Numb	%	Num	%	Num	%	Num	%	Numb	%

	ber		er		ber		ber		ber		er	
Rural	32283	47	30790	44	30409	41	31598	38	32529	37	33602	36
Semi-urban	15135	22	15325	22	16770	22	19337	23	21022	24	23048	25
Urban	11566	17	12419	18	14202	19	16726	20	18288	21	19156	21
Metropolitan	9516	14	11839	17	13272	18	15236	18	16364	19	17274	19
Total	**68500**	**100**	**70373**	**100**	**74653**	**100**	**82897**	**100**	**88203**	**100**	**93080**	**100**

Source: Compilation by researcher from various sources

Analysis of the above table shows the presence of Commercial Banks at rural and semi-urban area. As can be seen from Table 1, the representation of branch banking has reduced over the years. This is alarming in 2003, 47% of the total branches were in rural areas, which came down to mere 36% in 2011. Whereas the percentage of banks have been increased in semi-urban, urban and metropolitan cities.

Table 2- Excluded Population from the Financial Services

Country	**Population Excluded (in million)**
China	263
Africa	230
Rest of Asia	162
India	135
Latin America(Excluding Brazil)	28
Brazil	14
Middle East	20
East Europe	19
West Europe	I8

Source: Microfinance World January/March 2011

The above table no.2 reveals that the population excluded is a phenomenon all over. Even the developed countries people have excluded from financial services. The access to finance for the unbanked is not a strange and frightening concept for the Indian Economy. Access has always been available through intermediaries like Self Help Groups and Mutual Financial Institutions.

Table 3- Percentage of Indian Earners Having Bank Account

Annual Income (Rs.)	Urban	Rural	Total
Up to 50,000	34.1	26.8	28.3
50,000 to 1,00,000	75.5	71.2	73.0
1,00,000 to 2,00,000	91.8	87.4	89.9
2,00,000 to 4,00,000	95.5	93.6	94.9
More than 4,00,000	98.0	96.3	97.6
Overall	61.7	38.0	44.9

Source: Report on Currency and Finance 2008-10

The table 3 depicts that though financial exclusion is widespread, the situation is more severe in case of low income group people in India. The other group of income earners have much aware of keeping their money safe and have bank accounts.

Table 4- Sources of loan (percent of indebted earners)

Annual Income (Rs.)	Banks	Money lenders	Other institutional and Non institutional sources	Total
Up to 50,000	13.0	34.9	52.1	100
50,000 to 1,00,000	34.5	19.6	45.9	100
1,00,000 to 2,00,000	49.3	12.0	38.7	100
2,00,000 to 4,00,000	51.6	11.8	36.6	100
More than 4,00,000	62.8	5.5	31.7	100

Source: Report on Currency and Finance 2008-10

From the table 4, it is understood that the percentage of indebted earners in case of banks has been increased according to the increase in the level of earning ability, whereas in case of money lenders it is completely opposite. It is very much evident from the above table that financial inclusion and level of income is very much positively correlated. This is because of the fact that the majority of the people in the low income bracket are more dependent on non institutional and other private sources. This proportion declines sharply as the annual income increases.

MEASURES BY RBI AND GOI TOWARDS FINANCIAL INCLUSION

- **Co-operative Movement**: Opening of cooperative banks in rural, semi-urban, and urban areas to bring large number of people under the aegis of banking services.
- **Nationalization of Banks**: After the nationalization of banks in sixties, the spread of banking services has reached to remote areas. Thousands of new bank branches are opened.

- **Lead Bank Scheme**: The Lead Bank Scheme (LBS) was introduced in 1969 under the recommendation of Gadgil Study Group. Under the scheme, each district was allotted to a bank to act as Lead Bank. The lead banks acted as facilitator for expansion of branch banking and credit expansion.
- **Regional Rural Banks (RRB):** The RRBs were first come into existence in mid-seventies. RRBs played an important role in spreading banking services in rural areas. Starting from a single bank branch in 2nd October, 1975, today around 15475 branches are operating across India
- By setting up of state bank of India, establishing Service area approach and self help groups.
- Provision of No-Frills Banking Account with Overdraft facility
- Usage of Regional Language in all the banking institutions
- Entrepreneurial Credit such as General Credit Card, and Kisan Credit Card
- Extensive use of information technology for banking services
- Initiating Financial Literacy programmes.

BANKING SECTOR- A FACILITATOR OF FINANCIAL INCLUSION

The Government of India and RBI has taken concrete steps to expedite the process of Financial Inclusion. Recently Government of India has adopted a movement called "Swabhiman" to bring basic financial services to all 73,000 unbanked villages with over 2,000 populations by March 2012. In response to that different banks have taken initiatives to fulfill the dream. ICICI bank has come up with a joint venture with Aircel to expendite the process. Union Bank of India has set a target to serve 1880 unbanked villages; this number is 1,144 for Andhra Bank. This has been facilitated the banks to adopt different strategies, such as:

- Encouraging agents and intermediaries
- Using technology
- Providing basic low cost financial services
- Emphasizing financial literacy
- Simple loan product for general products and process
- Facilitation of low cost remittance products.

As Financial Inclusion is not a lucrative source of income, banks are basically going for financial inclusion after getting an impetus from RBI. The banks are also faced with some challenges in this process. These problems stem from the demand side and supply side of the financial services. The problems relating to demand side can be listed as, Lower financial literacy, Lack of awareness and the unfriendly attitude of the banks.

On the other hand, in the supply side, the cost of transaction and customer acquisition is high and it is not at all cost-effective. In spite of these problems, banks are taking steps as mentioned for financial inclusion.

FUTURE DIRECTIVES

In order to make financial inclusion successful, a win-win solution set is to be provided to the parties, the provider and the beneficiary. In other words, it should be a viable investment alternative to the financial institutions and should also be an attractive one to the borrowers. The financial institutions, especially the banks, can accelerate the financial inclusion process by:

(i) Increasing enrolment of SHGs through bank linkage programme.

(ii) Designing appropriate product on the basis of the requirement of a particular group of borrower.

(iii) Leveraging technology to reduce the opportunity cost of financial inclusions in the rural areas.

(iv) Applying business facilitator and correspondent model more intensively.

(v) Inspecting the infrastructure of rural branches of the banks.

Financial inclusion is a strategy to achieve the inclusive growth provided it is supported by various factors like real initiatives from banks and financial institutions, technological development, financial literacy and so on. The role of Central Government and RBI regarding policy making and the role of state governments with respect to land settlement rights, providing economic and social infrastructures etc. are also very crucial. The time has come to implement policies and schemes adopted by various authorities for rural India to uplift its standards of living and to include it within the periphery of basic financial services. Attempts therefore should be made at the grass root level to implement those ideas keeping in mind the panoramic view of inclusive growth prevailing in India.

BENEFITS OF INCLUSIVE FINANCIAL GROWTH

The Financial Inclusion thus meant for the Landless Laborers, Urban slum dwellers, Farmers, disabled, migrants, employees of unorganized sectors and self employed for the purpose of following benefits:

1. **No frill accounts**: Privatization of banking has seen high amount of balance in the accounts where the banks are providing various benefits. Simple banking accounts were not available for the common people to transact through banks. Government intervention and through public sector banks, no frill accounts were introduced for the people who want to avail the scheme.
2. **Overdraft facility**: The farmers and agricultural laborers are more of such needs when they need the finances for buying seeds, pesticides etc. for a short term and they have the capacity to pay off. Already some banks have introduced micro finance facilities in their rural branches where such facilities have been addressed.
3. **Easier credit facilities:** Credit cards and instalments are very much required financial products which the rural mass need for their use. The banks were not using credit cards or hire-purchase schemes to the agricultural labors, urban slum dwellers etc. Some public sector banks have now started issuing credit cards in rural sectors and some sectoral cards like Kisan Card etc. are being issued to get such benefits.
4. **Investment awareness:** This is the most important aspect of the financial inclusion. The benefits of credit as well as the ways and means to invest their surplus need to be explained to the poor and common mass so that they can best avail of the facility. Ministry of Corporate Affair and ICWAI has already joined hands for continuing such campaigns to the common people.
5. **Growth with equity:** In the path of superpower we the Indians need to achieve the growth of our country with equality. It is provided by inclusive finance.
6. **Get rid of poverty:** To remove poverty from the Indian context everybody will be given access to formal financial services. Because, if they take loans for business or education or any other purpose they get the loan to pave way for their development.
7. **Easy Financial Transactions:** Inclusive finance will provide banking related financial transactions in an easy and speedy way.
8. **Safe financial services**: People will have safe savings along with other allied services like insurance cover, entrepreneurial loans, payment and settlement facility, etc.

9. **Inflating National Income**: Boosting up business opportunities will definitely increase GDP and this will be reflected in our national income growth.
10. **Global Player**: Financial access will attract global market players to our country that will result in increasing employment and business opportunities.
11. **Low cost Financial Services** : Providing Financial Services to the people who do not have the habit of regular savings but have potential for savings once the savings habit is cultivated in them like providing the benefits of SIP and Recurring Deposit account or small savings schemes etc.
12. **Old age Pension:** General rural population is dependent on the daily labor or on their daily earning and do not have the means or schemes for saving for the old age. Suitable pension schemes available in the market, if made available, and educating the people for contributing in the same shows better future prospects. Govt. of India's initiative of National Pension Scheme is a good step towards this direction.
13. **Electronic Fund Transfer:** Transfer of fund from one place to another becomes a problem even in this 21st century. It is very much crucial for a person with limited means to wait for the fund when he actually needs them for education, hospitalization and, in some cases, during emergencies. RBI has taken a step towards this by introducing RTGS and NEFT facilities in banking. Still a lot more improvements are required.
14. **Insurance**: Till date very little percentage of Indian population is having cover of Life through Life Insurance. This is primarily due to high premium rate. As a matter of practice, the LIC policies, in general, are having with profit policies and term insurances were never preached by LIC to the common mass. Opening up of the sector to private parties has actually developed this sector where more and more people took Life Insurance through Term Plans where higher covers are available with low premium.

Opening up of economy has given us the scope to expand ourselves and now, through financial inclusion we can reach to the common and rural mass and deliver the world class financial benefits which they can use for their good.

THE WAY FORWARD

The banks should come out of inhibited feeling that very aggressive competition policy and social inclusion which are mutually exclusive. As demonstrated elsewhere, the mass banking with no-frills etc. can become a win-win situation for both. Basically, banking services need to be “marketed” to connect with large population segments and these may be justifiable promotional costs. The opportunities are plenty:

- In the context of India becoming one of the largest micro finance markets in the world, especially in the growth of women’s savings and credit groups and the sustaining success of such institutions which has been demonstrated by the success of SEWA bank in Gujarat, low cost banking is not necessarily an unviable venture or proposition.
- It may be useful for banks to consider franchising with other segments of financial sector such as cooperatives, RRBs etc. so as to extend the scope of financial inclusion with minimal intermediation cost.
- Since large sections of low income groups’ transactions are related to deposits and withdrawals, with a view to containing transaction costs, simple to use, cash dispensing and collecting machines akin to ATMs, with operating instructions and commands in vernacular would greatly facilitate financial inclusion of the semi-urban and rural populace.

CONCLUSION

The main reason for financial exclusion is the lack of a regular or substantial income. In most of the cases people with low income do not qualify for a loan. The proximity of the financial service is another fact. The loss is not only the transportation cost but also the loss of daily wages for a low income individual. Most of the excluded consumers are not aware of the bank’s products, which are beneficial for them. Getting money for their financial requirements from a local moneylender is easier than getting a loan from the bank. Most of the banks need collateral for their loans. It is very difficult for a low income individual to find collateral for a bank loan. Moreover, banks give more importance to meeting their financial targets. So they focus on larger accounts. It is not profitable for banks to provide small loans and make a profit. Financial inclusion is a great step to alleviate poverty in India. But to achieve this, the government should provide a less perspective environment in which banks are free to pursue the innovations necessary to reach low income consumers and still make a profit. Financial service providers should learn more about the consumers and new business models to them.

Financial service providers should learn more about the consumers and new business models to reach them. New entrants to the banking system need households at their doorstep. There has been a burst of entrepreneurship across the country, spanning rural, semi-urban and urban areas. This has to be nurtured and financed. It is only through growth of enterprises across all sizes that competition will be fostered. To conclude, I wish to stress that, with increasing liberalization and higher economic growth, the role of banking sector is poised to increase in the financing pattern of economic activities within the country. Financial inclusion will strengthen financial deepening and provide resources to the banks to expand credit delivery. Thus; financial inclusion will lead to financial development in our country which will help to accelerate economic growth.

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