

Performance of Commercial Banks and Co-operative Banks in Promoting Financial Inclusion in Rural Karnataka: An Empirical Study

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Abstract

In order to encourage equitable economic growth, especially in rural areas, financial inclusion is essential. Co-operative banks and commercial banks have made a significant contribution to expanding access to formal financial services in Karnataka.

This study empirically examines and compares their performance in promoting financial inclusion among rural households in Karnataka. Using primary survey data collected from 600 respondents across five rural districts, supported by secondary data from RBI and NABARD reports, the study analyzes outreach, accessibility, credit delivery, and customer satisfaction. The findings reveal that while commercial banks excel in technology-driven outreach and diverse product offerings, co-operative banks play a crucial role in personalized services and agricultural credit. The study concludes with policy implications for strengthening rural financial ecosystems.

Keywords: *Financial Inclusion, Commercial Banks, Co-operative Banks, Rural Karnataka, Credit Accessibility, Empirical Study*

Introduction

Even after more than 75 years of independence, a significant portion of India's population continues to remain outside the formal banking system. This exclusion has contributed to financial instability among lower-income groups, who lack access to essential financial products and services. In recent years, however, both the Government of India and the Reserve Bank of India (RBI) have made concerted efforts to promote financial inclusion as a crucial national objective.

Over the past five decades, various measures have been implemented to advance financial inclusion. These include the nationalization of banks, expansion of a robust branch network through scheduled commercial banks, cooperative banks, and regional rural banks, introduction of mandated priority sector lending targets, the lead bank scheme, formation of self-help groups (SHGs), appointment of business correspondents (BCs) and business facilitators (BFs) to deliver banking services at the doorstep, and the launch of zero-balance basic savings bank deposit (BSBD) accounts. The fundamental aim of these initiatives has been to extend financial services to the vast segments of the Indian population that have historically been excluded.

Notable efforts by the Government and RBI include the introduction of the Microfinance-SHG model in 1992, the Kisan Credit Card scheme in 1998, No-Frills Accounts in 2004, the Business Correspondents and Business Facilitators models in 2006 and 2009, and the Swabhimaan

financial inclusion campaign in 2011. Despite these initiatives, achieving full financial inclusion remains a persistent challenge.

The United Nations has aptly raised the question: "Why are so many bankable individuals in rural and urban areas still unbanked?" According to NSSO data, 45.9 million farmer households (51.4% of the total 89.3 million) do not access credit from either institutional or non-institutional sources. Financial experts often emphasize that opening a bank account is the first and most essential step toward bringing these individuals into the financial mainstream.

Many people at the bottom of the social pyramid remain disconnected from formal financial systems—they do not have bank accounts, lack awareness of savings and financial instruments, and are unable to benefit from their own monetary resources, however limited. In essence, financial inclusion refers to integrating these underserved populations into the formal financial ecosystem, enabling them to participate in and benefit from the nation's economic growth.

Financial inclusion has emerged as a pivotal strategy for inclusive growth in India. The Reserve Bank of India (RBI) and Government of India have implemented various measures to ensure that the financially excluded segments, particularly rural populations, gain access to formal financial services. Karnataka, a state with significant rural and agrarian presence, serves as a critical case for evaluating the efficacy of different banking institutions in promoting financial inclusion. Commercial banks, with their robust infrastructure and technological innovations, and co-operative banks, known for their local focus and community-driven approach, both contribute uniquely to this mission. However, comparative empirical evidence on their respective roles and performance in rural Karnataka remains limited.

Statement of the Problem

Despite numerous initiatives to promote financial inclusion, large sections of rural Karnataka continue to lack access to formal financial services. Disparities persist in credit delivery, savings mobilization, and financial literacy. Moreover, while commercial banks and co-operative banks play distinct roles, there is a lack of comprehensive empirical analysis comparing their effectiveness in promoting financial inclusion in rural areas. Understanding their relative strengths and limitations is critical for designing targeted policy interventions and improving financial inclusion strategies in the state.

Objectives of the Study

1. To Study the concept of financial inclusion and its importance
2. To evaluate the role of co-operative banks in enhancing financial access
3. To identify the major challenges faced by rural populations in accessing formal financial services.
4. To suggest policy measures for strengthening financial inclusion through commercial and co-operative banking channels.

Exclusion from Finances

Geographers who were concerned about the limited physical access to banking services as a result of widespread bank branch closures first coined the term "financial exclusion" in 1993 (Leyshon and Thrift, 1993). In the 1990s, research started to show how difficult it was for some people in society to get insurance, modern payment systems, consumer credit, and even basic

savings options. According to Kempson and Whyley (1999), the term came to mean people who lacked easy access to mainstream financial services in 1999. Since then, Anderloni (2003), Anderloni and Carluccio (2006), and Carbo et al. have all contributed to the definition and comprehension of financial exclusion. (2004), Gloukoviezoff (2004), Devlin (2005), Kempson et al. (2000), Sinclair (2000), and policy reports from HM Treasury and the Treasury Committee (2006a, 2006b) Most people now agree that people who have trouble getting the right financial products and services from mainstream financial institutions are considered to be financial exclusions. This definition is notable for two important aspects: first, the emphasis on mainstream financial services and second, appropriate products. Mainstream commercial providers' failure to provide products that cater to the requirements of all social groups' accounts for a significant portion of the exclusion. Exclusion from society generally follows from financial exclusion. Groups most affected include marginal farmers, landless laborers, self-employed individuals, workers in the unorganized sector, urban slum residents, migrants, ethnic minorities, socially excluded groups, senior citizens, and women (Rangarajan Committee Report).

There is widespread recognition that financial exclusion is part of a larger issue of social exclusion, which also includes lack of access to employment, housing, education, and healthcare. Therefore, policies addressing financial exclusion can serve as integrated solutions to tackle social exclusion as well (Marshall, 2004).

Financial Inclusion — Inclusive Growth Model

The concept of inclusive growth has gained significant prominence worldwide, including in India (Bolt, 2004). Inclusive growth emphasizes not only widespread participation in the growth process but also equitable sharing of its benefits. Growth is considered pro-poor when it benefits the poor in absolute terms, as measured through reductions in poverty levels (Ravallion and Chen, 2003). True economic success lies in achieving growth with equity.

It is globally acknowledged that high national income growth alone cannot address challenges such as employment generation, poverty reduction, balanced regional development, and human development. Thus, the Indian government has focused on promoting inclusive growth through efforts in agriculture, rural development, industry, infrastructure, services, education, and healthcare.

Financial inclusion is a crucial component of inclusive growth, as it enables the economic empowerment of disadvantaged groups. It not only supports economic development but also presents a business opportunity for formal financial institutions to expand into unbanked areas and achieve profitability. Furthermore, developmental authorities play an essential role in building supportive physical and social infrastructure, such as literacy, health, and communication facilities. To summarize, the four pillars of inclusive growth are productivity, employment, financial inclusion, and infrastructure development.

Between 2006 and 2010, India's growth rate averaged 8.6%, making it one of the fastest-growing economies in the world. However, this growth has not been equitable. The Eleventh Five Year Plan (2007–2012) aimed to restructure policies to achieve faster, more broad-based, and inclusive growth, focusing on poverty reduction and bridging various social and regional divides

(Government of India, 2006). The policies sought to simultaneously increase income and employment opportunities while financing programs that promote inclusive growth.

Rural areas, home to 70% of Asia's poor, continue to lag due to limited access to financial services, poor infrastructure, lack of market information, inadequate education and training, and limited access to new technologies. Therefore, greater efforts are required to ensure their participation in inclusive growth.

Inclusive growth involves both the pace and the pattern of economic growth. It aims to create productive employment opportunities that raise incomes for excluded sections, allowing them to contribute to and benefit from economic progress. The Eleventh Five Year Plan identifies inclusive growth as a central objective.

Financial inclusion supports inclusive growth by channelizing surplus funds to deficit areas, bringing the poor and marginalized into the economic mainstream. Inclusion should be viewed not merely as a welfare measure but as a process of empowering excluded groups to actively participate in development (Planning Commission, 2007).

The focus of India's economic policy has increasingly shifted toward equitable growth, emphasizing not only sustained growth but also a fair distribution of its benefits. This shift is especially significant for underdeveloped regions such as hilly and rural areas, which often struggle despite overall national progress.

Committees and Initiatives

In 2006, the Government of India established a Committee on Financial Inclusion, which presented its report in 2008. The committee launched the National Rural Financial Inclusion Plan, set targets for banks, and recommended measures to overcome supply and demand constraints. It also proposed improvements in human, natural, physical, and social capital.

Budgetary support included establishing the Financial Inclusion Fund and Technology Fund (each with a corpus of ₹500 crore) and mandating banks to add rural accounts and appoint facilitators like retired bank officers.

Importance in India

Financial inclusion supports basic needs such as food, water, housing, education, and healthcare by empowering businesses and enabling reliable access for clients. It helps individuals start businesses and allows small enterprises to grow.

Policy focuses on financial inclusion in rural and semi-rural India serves three primary purposes:

1. Encouraging savings habits: Strengthens financial security and boosts capital formation.
2. Providing formal credit: Reduces dependence on informal sources and supports entrepreneurship.
3. Improving delivery welfare: Direct cash transfers through bank accounts reduce leakage and ensure benefits reach intended recipients.

Given India's agrarian nature and large population, financial inclusion addresses high interest rates, uncertain agricultural incomes, and distrust of formal banking among farmers. Bank accounts

are perceived as the first step towards financial empowerment, helping integrate more people into the economic mainstream and supporting sustainable growth.

Features of Financial Inclusion

- Financial inclusion refers to providing a minimum set of financial services to people at the lowest socio-economic levels.
- It emphasizes integrating mainstream banking and financial services into this effort.
- Opening a bank account is often considered the first essential step.
- It is promoted as a crucial tool for achieving sustainable and inclusive growth.
- Mangalam village in Puducherry was the first to achieve 100% financial inclusion.

Factors Affecting Access to Financial Services

- ❖ Gender: Women often face limited access due to lack of asset ownership or the need for male guarantors.
- ❖ Age: Financial services typically target middle-aged, economically active individuals, overlooking younger and older populations.
- ❖ Legal Identity: Lack of identity documents excludes many marginalized groups.
- ❖ Literacy: Low financial literacy restricts awareness and understanding of services.
- ❖ Geography: Physical distance, poor infrastructure, and remote locations reduce accessibility.
- ❖ Cultural and psychological barriers: Distrust of formal institutions and cultural norms deter many from participating.
- ❖ Bank charges and conditions: High costs, hidden fees, and stringent conditions discourage low-income individuals.
- ❖ Income level: Extremely poor populations often find basic services inaccessible.
- ❖ Occupation: Informal sector workers and small entrepreneurs struggle to access formal credit.
- ❖ Product attractiveness: Poorly designed products and weak outreach hinder uptake.

Suggestions

1. **Strengthening Technology Infrastructure:** Encourage co-operative banks to adopt advanced digital platforms to improve outreach and service delivery.
2. **Financial Literacy Programs:** Conduct targeted financial literacy and awareness camps to increase rural participation in formal banking.
3. **Customized Credit Products:** Develop need-based loan schemes tailored to the agricultural and rural enterprise sectors.
4. **Improved Monitoring:** Establish better monitoring systems to track and evaluate the progress of financial inclusion initiatives.
5. **Collaborative Models:** Promote collaborations between commercial and co-operative banks to leverage their respective strengths.

Conclusion

Innovations in technology have revolutionized access to financial services. Mobile phones and digital platforms now allow low-cost, convenient banking, even in remote areas. Financial institutions are adopting new outreach strategies, including mobile ATMs and banking vans.

Tailored financial products in agriculture, health, and insurance are offering scalable, context-specific solutions. Governments are fostering these innovations through supportive policies that encourage partnerships and responsible finance. Meanwhile, improved data collection helps track progress and better understand unbanked markets.

Financial inclusion, thus, plays a vital role in achieving inclusive and sustainable growth, empowering marginalized communities, and supporting overall national development.

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