



FINANCIAL INCLUSION IN INDIA CHALLENGES AND ISSUES

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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.

Key Words: *Financial Inclusion, Financial Exclusion, Business Correspondents, KCCs, GCCs.*

I. 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.

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 find out the approaches adopted by banks, steps taken by the regulatory bodies and various government initiatives to achieve financial inclusion.
4. To analyze the past years performance and achievements towards reaching out to the unbanked areas under financial inclusion.

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, kempson 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.

According to the European Commission, Financial exclusion is: „A process whereby people encounter difficulties accessing or using financial services and products in the mainstream market that are appropriate to their needs and enable them to lead a normal social life in the society in which they belong.

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.

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.

IV. FINANCIAL INCLUSION

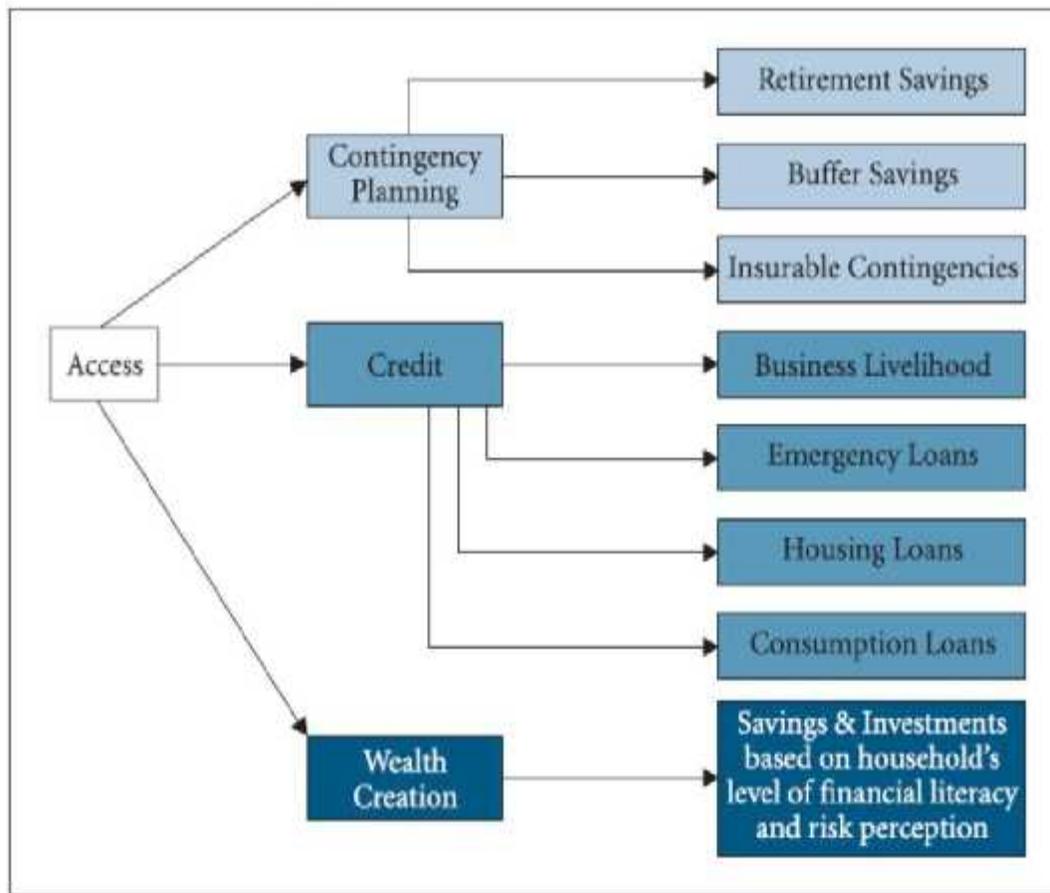
4.1 Concept and Definition of Financial Inclusion

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.”*² Financial inclusion does not stand for delivery of financial services for all at all cost. But it means that the delivery of financial services and products at affordable costs of excluded sections of population and low income groups. It plays a crucial role to remove away the poverty from the country. Financial inclusion is to provide equal opportunities to vast sections of population to access mainstream financial services for better life, living and better income. It provides path for inclusive growth.

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.

Figure 2: Household Access to Financial Services



Source: A Hundred Small Steps a Report of the Committee on Financial sector reforms by Raghuram G. Rajan

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.

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 labourers 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.

V. VARIOUS APPROACHES TO ACHIEVE FINANCIAL INCLUSION

In India, various measures taken by banks, GOI and RBI for financial inclusion plan. Figure 3 highlighted currently adopted financial inclusion approaches.

Figure 3: Financial Inclusion : Currently adopted Approaches



5.1 Product Based Approach: Reserve bank of India has been proactive, liberal and supportive while making policies so as to enable financial institutions to come up with innovative products for enabling a common man to get the benefit of the financial inclusion plan. Some products developed for fulfillment of this approach have been mentioned in this paper.

- i. No- Frills Account (NFAs):- This concept was introduced by RBI in November 2005 to provide access to basic banking services by financially excluded peoples. Under this approach banks open accounts with zero balance or very minimum balance requirement for the under-privileged. In 2012, the banks under RBI guidelines came-up with a better version of the no-frill accounts where they would open Basic Savings Bank Deposit Accounts (BSBDAs) for all individuals with the facility of debit card, cheque book, internet banking, overdraft limits at minimal charges. However, the number of transactions could be restricted so as to prevent misuse of such accounts.
- ii. Kisan Credit cards (KCCs):- Under this scheme banks issue smart cards to the farmers for providing timely and adequate credit support from single window banking system for their farming needs. During 2012-13 (up to December 2012), public and private sector banks issued 1.2 million smart cards as KCCs.

5.2 Bank Led approach

- i. Self Help Group - Bank Led Initiative (SLBP):- The SLBP or Self Help Group – Bank Linkage Program has been the major institutional based innovation in India for enabling access and covering the gap of reaching financially excluded population of the country in the last two decades. In this model, the banks involve themselves with a group of local people with the idea of enabling them to pool up their savings. The same is deposited with the bank against which the bank also provides a certain amount of credit facility. The group takes a decision to whether to lend to any member of the group. The bank provides the framework, accounting services and support to the group to manage their deposits and lending. Thus the model has an approach of savings first, lending later. The banks do not have a risk in such lending as the borrower’s reputation and peer pressure in the group would reduce the risk of bad loans considerably. However, The model has some issues that affect the program
 - a. Inadequate outreach in many regions.
 - b. Delays in opening of SHG accounts and disbursement of loans.
 - c. Impounding of savings by banks as collateral.
 - d. Non-approval of repeat loans by banks even when the first loan was repaid.
 - e. Multiple memberships.
 - f. Borrowings by SHG members within and outside SHGs.
 - g. Adverse consequences of unhealthy competition between NGO promoted SHGs.
 - h. Government promoted/subsidy oriented SHGs and limited banker interface.
 - i. Monitoring of the SHGs.

While the basics of the SHGs being savings led credit product remain true even today, recent developments have given rise to the need for relook in the approach and design of this fairly successful model leading to SHG - 2.

The basic features of SHG - 2 are

- a. Voluntary savings apart from compulsory savings
- b. Allowing the sanction of a cash credit / overdraft system of lending for SHGs for a longer operational tenure, and
- c. Graduating selected members of the group that have entrepreneurship potential into a joint liability groups for borrowing larger amounts.

ii. Business Facilitators (BFs)/Business Correspondents (BCs):- The BC/BF model is a model which based on information and communication technology (ICT). In this model the intermediaries or BC/BFs are technologically empowered by the banks to provide the last mile delivery of financial products and services. Initially created by the banks themselves and later with improvisations and RBI policy support, the model on the back of innovative technologies is bridging the connectivity gap between the service seekers, i.e., under-served public, and the service providers, i.e., the banks. However, a number of issues both for the partner banks and also for the regulators have surfaced since the start of this model. Some of them being

- a. Profitability of the BFs/BCs
- b. Banks and their BFs/BCs are exposed to huge risk of cash management
- c. The training and hand-holding of the BFs/BCs to enhance the trust level of the end customers
- d. Adoption of technology
- e. Compatibility and integration of technology used by the banks and their BFs/BCs.

5.3 Regulatory Approach

- i. Simplified KYC Norms: - Under current KYC norms, a customer has to provide number of documents for opening an account as per RBI guidelines. However, the people living in rural areas face problem in fulfilling these norms. To enable banks to tap in this huge opportunity of rural banking in unbanked areas and to meet the objective of financial inclusion, RBI has relaxed a number of norms for accounts opened by people who plan to keep balances not exceeding Rs.50, 000 and whose total credit in all the accounts taken together is not expected to exceed Rs.100, 000 in a year. Small accounts can now be opened on the basis of an introduction from another account holder who has satisfied all the KYC norms.
- ii. Simplified bank saving account opening: - The account opening form has been simplified to ease the opening of account by the poorer sections, street hawkers and other migratory labours of the society.
- iii. Bank branch authorization: - RBI has permitted banks to open branches without taking authorization, thus deviating from its normal norms, in tier 3 to 6 city, towns, or villages. This would enable the government, regulator and the banks to speed up the drive for financial inclusion and this make available the financial services to the unbanked population of the country.

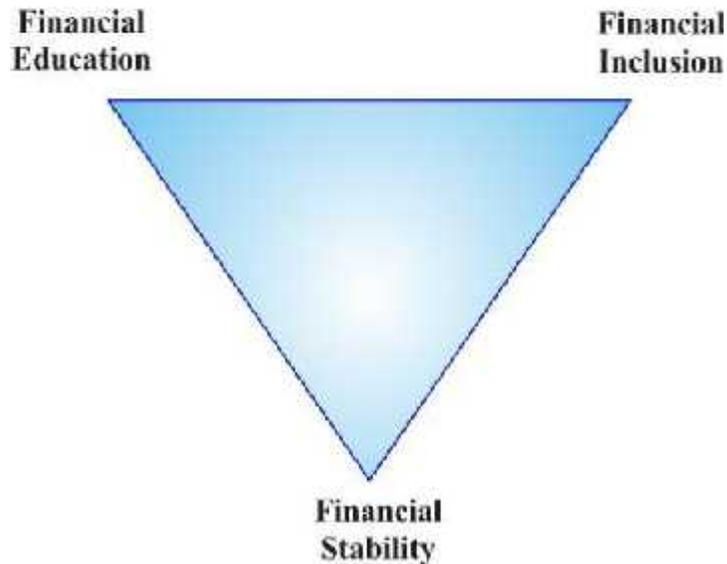
5.4 Technology Based approach

- i. Mobile Banking :- One of the most remarkable developments in terms of innovation in order to harness the full power of technology, the banks have tied up with mobile operators to provide financial services like bill and utility payment, fund transfer, ticket booking, shopping etc. Some examples of this model are m-Pesa by Vodafone and Airtel Money.
- ii. Kiosk / ATM based banking: - In some states, the state government has taken initiatives for providing kiosk based model for access to financial services. Also banks have used the technology to enable their ATMs to virtually act like a 24x7 branches.
- iii. Branchless Banking: - Some of the leading banks have come up with this concept where there would be an online system with chat facility assisting the person to make use of various electronic machines for depositing and withdrawing cash and cheques. However this initiative is in a very initial stage and has a limitation in terms of initial Cost for banks and literacy / knowledge for the rural population and hence this concept is currently limited to urban and semi-urban areas.

5.5 Knowledge Based Approaches

Financial education, financial inclusion and financial stability are three elements of an integral strategy to empower people to make effective use of the financial services network. While financial inclusion works from supply side, financial education feeds the demand side by promoting awareness among the people regarding the needs and benefits of financial services offered by banks and other institutions. These two strategies together promote greater financial stability.

Figure 4: The Financial Tripod



- i. Financial Stability Development Council (FSDC) has explicit mandate to focus on financial inclusion and financial literacy simultaneously.
- ii. RBI had issued guidelines on the financial literacy Centres (FLC) on in June 2012 for setting up FLCs. It was advised that the rural branches of scheduled commercial banks should increase efforts through conduct of outdoor Financial Literacy Camps at least once a month. Accordingly, 718 FLCs had been set up as at end of March 2013. A total of 2.2 million people had been educated through awareness camps / choupals, seminars and lectures during April 2012 to March 2013.

5.6.Governments Initiatives

The government has taken various initiatives indirectly through the regulators, government promoted schemes through its various ministries. Some such initiatives have been listed below.

- i. Induction of SHG-2:- The original SHG as initialized by NABARD had certain limitations. This led to NABARD preparing a strategy to revitalize the SHG movement leading with the induction of SHG-2 model.
- ii. Women SHGs Development Fund: - The Union Budget 2011-2012 proposed a “Women’s SHG’s Development Fund” with a corpus of Rs. 500 crore. The GoI created this fund to empower women and promote their SHGs. The responsibility of managing the fund is of NABARD. It managed the same through two of its major microfinance funds, namely Financial Inclusion Fund (FIF) and the Financial Inclusion Technology Fund (FITF).

VI.PERFORMANCE AND ACHIEVEMENTS TOWARDS REACHING OUT TO THE UNBANKED AREA UNDERFINANCIAL INCLUSION PLANS (All SCBs including RRBs)

In January 2010, all public and private sector banks adopted board – approved financial inclusion plans (FIPs) for next three years which started April 2010 to march 2013. RBI advised to all SCBs, to incorporate FIPs with their business strategy to financially nurturing to all excluded population in India. RBI and SCBs have adopted a structured approach to achieve financial inclusion through FIPs containing self set targets with measurable and monitor able outcomes. Below mention table shown last three years considerable performance in the path of financial inclusion.

Table 1: Progress under Financial Inclusion Plans, All SCBs including RRBs

| No. | Variable | Mar-10 | Mar-11 | Mar-12 | Mar-13 | Absolute Change (2010-2013) | Percentage change (2010-2013) |
|-----|---|--------|---------|---------|---------|-----------------------------|-------------------------------|
| 1 | Banking Outlets in Villages > 2,000 | 27,949 | 30,607 | 33,188 | 35,483 | 8,534 | 30.5 |
| 2 | Banking Outlets in Villages <2,000 | 29,745 | 49,602 | 69,465 | 149,601 | 119,856 | 403.9 |
| 3 | Banking Outlets in Villages – Franchise | 24,478 | 14,811 | 4,411 | 40,877 | 16,399 | 67.4 |
| 4 | Banking Outlets in Villages – ECs | 24,174 | 80,802 | 141,136 | 221,241 | 197,067 | 814.7 |
| 5 | Banking Outlets in Villages - Other Modes | 141 | 305 | 3,148 | 6,076 | 6,114 | 4,334.70 |
| 6 | Banking Outlets in Villages – Total | 67,694 | 116,268 | 181,739 | 268,434 | 200,740 | 296.6 |
| 7 | Urban Locations covered through ECs | 447 | 3,771 | 5,802 | 27,143 | 26,696 | 5,972.30 |
| 8 | Basic Savings Bank Deposit Account (BSBDA) through branches (No. in million) | 60 | 73 | 81 | 101 | 41 | 67.5 |
| 9 | Basic Savings Bank Deposit Account (BSBDA) through branches (Amt. in ' billion) | 44 | 58 | 119 | 162 | 120 | 271.3 |
| 10 | Basic Savings Bank Deposit Account (BSBDA) through BCs (No. in million) | 13 | 32 | 57 | 81 | 68 | 512.4 |
| 11 | Basic Savings Bank Deposit Account (BSBDA) through BCs (Amt. in ' billion) | 11 | 8 | 11 | 18 | 8 | 72.7 |
| 12 | BSBDA Total (in million) | 73 | 105 | 138 | 182 | 109 | 147.9 |
| 13 | BSBDA Total (Amt. in ' billion) | 55 | 66 | 130 | 180 | 125 | 227.3 |
| 14 | OD facility availed in Basic Savings Bank Deposit Account (No. in million) | 0.2 | 1 | 3 | 4 | 4 | 2,094.40 |
| 15 | OD facility availed in Basic Savings Bank Deposit Account (Amt. in ' billion) | 0.1 | 0.1 | 1 | 2 | 1.9 | 1,450.00 |
| 16 | KCCs Total (No. in million) | 24 | 27 | 30 | 34 | 9 | 39 |
| 17 | KCCs Total (Amt. in ' billion) | 1,240 | 1,600 | 2,068 | 2,421 | 1,181 | 111.5 |
| 18 | GCCs Total (No. in million) | 1 | 2 | 2 | 4 | 3 | 161.2 |
| 19 | GCCs Total (Amt. in ' billion) | 25 | 35 | 42 | 75 | 50 | 117.4 |
| 20 | ICTA/Cs-EC Total Transactions (No. in million) | 57 | 84 | 156 | 236 | 224 | 391.4 |
| 21 | ICTA/Cs-EC Total Transactions (Amt. in ' billion) | 7 | 58 | 97 | 234 | 227 | 3,276.80 |

Note: Absolute and percentage variation could be slightly different as numbers have been rounded off to million/billion.
Source: Report on Trend and progress of banking in India 2013-13

No. of Branches, BCs and other modes of banking outlets in villages

Due to RBI's take intensively efforts in financial inclusion areas, the number of bank branches including RRBs increased of from 33,378 in March 2010 to 40,837 in March 2013. Banking outlets through BCs has been also increased from 34,174 in March 2010 to 2,21,341 in March 2013 and other modes of banking outlets in villages has increased rapidly from March 2010 to march 2013.

RBI also advised to all banks to provide small overdrafts facilities in BSBD accounts. Therefore up to March 2013, 4 million BSBD accounts availed OD facility of 2 billion.

Kisan Credit Cards (KCC) and General Credit Cards (GCC) Issued:-

Under FIPs RBI advised to banks to issue smart cards to farmers for availing timely and adequate credit facilities, up to March 2013 Banks has been issued 34 million KCCs and provided credit (Graph - 3). Banks also provide GCCs to Non - farm entrepreneurs to fulfill their credit needs as per revised guidelines in Dec."13. Up to March 2013 banks had issue 4 million GCCs.

To provide cost effective banking services for excluded areas the RBI suggested, to all SCBs to provide ICT based banking services. The Number of ICT based transactions in year of 2013 is 250 million and amount of these transactions in same year is 234 billion.

VII. CONCLUSION

Even though enough efforts are being made by all stake holders viz Regulator, Government, Financial Institutions and others, the efforts are not yielding the kind of result expected. The regulator has to create a suitable regulatory environment that would keep the interest of all the stakeholders.

The concern of banks about profitability is to be addressed by the regulator as the entire process of financial inclusion would be a kind of social work in the first few years. The concerns of the government about the reach, feasibility and implement ----ation of government policies to the last mile needs to be addressed. The easy availability of financial services to the last mile



user, the people in tier 3 to tier 6 in entirety needs to be addressed.

The bank's concerns can be addressed by leveraging ICT, designing innovative products and service models. A structured expansion and appropriate regulatory norms addressing the bank's concern and inclusion of NBFCs, MFI and SHG in the last mile connectivity of people to financial services could resolve the people's concern. Also bank use intensive mobile banking services to deliver banking and financial services to the people.

For achieve targets of FIP, it's needs to empowering MSMEs through provide timely and adequate finance because MSME's are the best medium for achieving inclusive growth which generate local demand and consumption, provide employment to millions of fresher's.

The aadhar card could be the answer to the government's concern as the bank accounts can be linked to the holder's aadhar number; however the sheer scale makes it difficult. Alternate to the same could be use of the vast postal office network at the disposal of the government. The post offices can easily reach the end user and vice-versa as the infrastructure is already in place. Regulatory bodies, banks and Government should intensively work on create awareness by educating people about finance.

Thus, Innovative products, out of the box service models, effective regulatory norms and leveraging technology together could change the landscape of the current progress of the much needed and wanted, Financial Inclusion Program.

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