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Financial Inclusion in India: An Emerging issue in Indian Economy

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Abstract:
Financial Inclusion is the delivery of financial services at an affordable cost to hitherto unbanked environments, especially the low-income and under-privileged. The Government of India and Reserve bank of India have taken initiatives to spread banking services such as expanding the number of rural bank branches, allowing the banking correspondent model and adoption of CBS technology. While it is a daunting challenge in size and scope, financial inclusion is also a great social and business opportunity. An attempt has been made in this paper to study the various financial inclusion models used in India - the challenges and a way out.

Keywords: Financial Inclusion, Financial Services, Banking Correspondent, RBI, Lead Bank.

Introduction:
The process of economic growth must try to take participation from all sections of society, especially when it is on high growth line. In developing countries, the serious threat to economic progress is the lack of access to financial services for small or marginal farmers & weaker sections of the society. (Garg, Agarwal, 2014). The recent developments in banking technology have transformed the banking sector 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. But the important point is that access to such technology is restricted only to certain segments of the society. Many of research articles and surveys clearly show that large numbers of population not only in India but also whole world does not have an access to basic banking and financial services. This is termed "financial exclusion". So, these people, especially, those living on low incomes, should be provided with mainstream financial services and products such as bank accounts which are used for making payments and keeping money, affordable credit, insurance and other financial services, etc. (Garg, Agarwal, 2014).

Objectives of the study:
The objective of this paper is to review in detail the available literature on Financial Inclusion In India & to learn and analyse:

Primary objectives:
1.To study the financial inclusion & its need in India.
2.To Identify strategies adopted by Reserve Bank of India(RBI) & Government of India for strengthening financial inclusion.

Secondary Objectives:
1.To study models of Financial Inclusion used in India.

Research Methodology:
For the fulfilment of the above objectives, data has been collected from books, SSRN, Yahoo Finance, online available data, RBI's online portal etc. It is descriptive in nature.

Literature Review:
Concept & Definition of Financial Inclusion:
Financial inclusion is one of the most important aspects in the present scenario for the development of economies. This term Financial Inclusion was firstly 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 concept for Indian economy. RBI had already been taken various initiatives (such as Bank Nationalisation in 1969, establishment of RRBs and introduction of SHG- bank linkage programs) to provide financial accessibility to the unbanked groups. (Garg, Agarwal, 2014). 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." So,financial inclusion does not mean the delivery of financial services for all at all cost.

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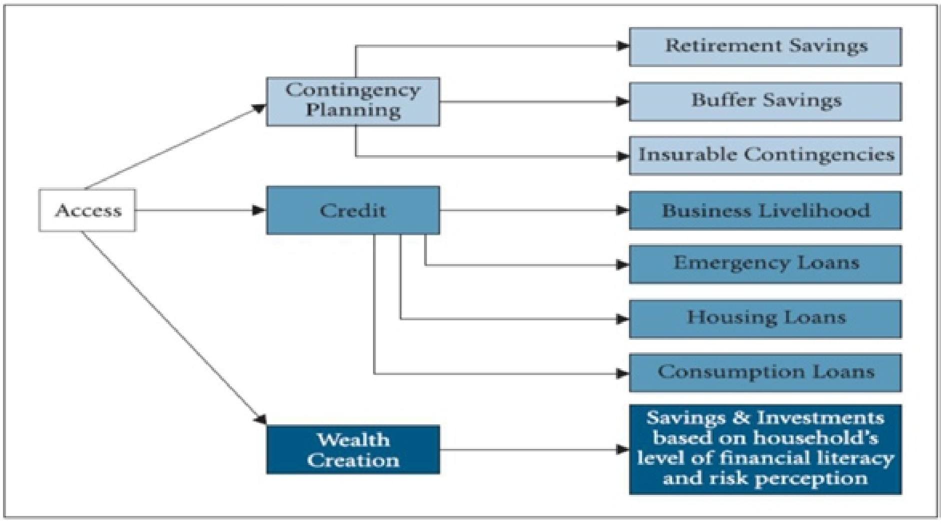
But it means that the delivery of financial services and products to excluded sections of population and low income groups at affordable costs. It plays a crucial role to remove away the poverty from the country. Financial inclusion is to provide equal opportunities to large sections of population to access mainstream financial services for better income, life & living. It provides direction for inclusive growth. (Garg, Agarwal, 2014).

Financial inclusion can also be described as availability of affordable financial services, such as saving, credit, insurance services, access to payments and remittance facilities by the formal financial systems to the excluded segment of the society. So, financial inclusion refers to access to wide range of financial product and services such as loan, equity & insurance products at affordable cost. (Garg, Agarwal, 2014).

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 finance for several purposes like creating buffer, retirement, saving against unpredictable situations and take products for insurable contingencies. Household also needs access to credit for housing, consumption, livelihood creation and their emergencies. So, it clearly shows that households require financial services to access a wide range of saving and investment products for their wealth creation but it is all depends upon their level of financial literacy. (Garg, Agarwal, 2014).

Evolution of Financial Inclusion in India:

The term financial inclusion is not a revolutionary term for India. Though it is discussed more now than before but the roots of financial inclusion were laid down in 1969 itself when the banks were nationalised by government of India and the awareness about it and the necessary actions to promote the financial inclusion were very limited till 2005 since then it has got a boost for the benefits that it brings. (Gwalani, Parkhi, 2014).

The evolution of financial inclusion in India has been carried out in various phases.

1) The first Phase was the Nationalization of Banks in 1969 which was taken to strengthen financial delivery. Government also launched various innovative programs for generating self-employment. As a result of which the branches of commercial banks & the regional rural banks (RRBs) increased from 8,321 in the year 1969 to 68,282 branches as at the end of March, 2005 and also the average population per branch office decreased from 64,000 to 16,000 during the same period. (Gwalani, Parkhi,2014)

2)In the second phase (during nineties), various reforms and change in regulatory norms were taken by Government of India to strengthen the financial sector. (Such as introduction of Self Help Groups (SHG), Kisan Credit Card & bank linkages). As a result of it government was able to provide credit benefit to the masses. (Gwalani, Parkhi,2014)

3)The current phase started from 2005 onwards. Under this phase RBI & Government had taken many initiatives to improve India's position. Its main focus was on extension & larger coverage. (Gwalani, Parkhi, 2014)

Why Financial Inclusion is important in India?

Financial Inclusion is an important aspect in India because of the following:

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I.Provide Platform for creating a habit to save money:

The lower income people has been living under the constant financial pressure mainly because of the absence of savings. Presence of banking services & products aim to create in them, a habit to save money. Capital formation in India is also expected to be boosted once the financial inclusion aspect is properly implemented because the people move away from traditional methods of investing savings in land, building etc. (Bhandawat,2012)

II.Bridge gaps & leaks in public subsidies and welfare programmes:

The money which send by the government to the poor people does not actually reach them. This money is consumed by the corrupt government officers in between & it does not reach to the intended parties. So, government is trying to transfer cash directly to beneficiaries through their bank accounts rather than subsidizing products & making cash payments. This effort of government is expected to reduce subsidy leakage & provide benefit only to the real beneficiary. All these efforts require an affordable & efficient banking system that can reach to all people. That's why we need financial inclusion. (Bhandawat,2012)

III.Providing formal credit opportunities:

So far, the population who do not have bank account are totally dependent on informal channels of credit such as friends, moneylenders & family. So availability of adequate & transparent credit at affordable costs from formal banking channels will bring prosperity in the countryside & will also increase output. For example: Micro- finance sector provides easy & affordable credit to the poor people of India. (Bhandawat,2012)

Models of Financial Inclusion Used In India

I.Lead Bank System:

Under this Scheme, each district had been assigned to different banks (public and private) to act as a consortium leader to coordinate the efforts of banks in the district. (Such as branch expansion & credit planning). Under this scheme, it was aimed that all villages above 2000 population will be provided access to financial services by March 2012. Villages below 2000 population will be covered in an integrated manner. It is also aimed at to provide banking & financial services to the people living in urban & metro cities. (Gwalani,Parkhi,2014)

II.Correspondent Banking:

In January, 2006, The Reserve Bank of India had permitted banks to use intermediaries as Business Facilitators (BFs) or Business Correspondents (BCs) for providing financial and banking services. The BCs are allowed to conduct banking business as agents of the banks at places other than the bank premises. As per the recent norms, various categories of individuals, corporate for profit companies, kirana shops etc. are allowed to become Business Correspondents' of banks. (Gwalani, Parkhi, 2014)

III.Banking on mobile:

As we know, the use of mobiles are very high in India. So, RBI allowed the mobile banking in October, 2008. 32 Banks were allowed to provide the facility of mobile banking. But still the object of achieving financial inclusion with the help of technology looks far beyond the target. To improve the situation, technology infrastructure with comprehensive credit information was created with the help of "The Financial Inclusion Technology Fund" of INR 5000 million. So, mobile banking is a reliable model to reach out to the people. (Gwalani, Parkhi, 2014)

IV.Microfinance Model:

India is the world's best laboratory for micro-finance because there are various micro- credit models operating in India such as Self Help Groups. (Gwalani, Parkhi, 2014)

Barriers to Financial Inclusion in India

I)High Cost:

It has been found that poor people living in urban or rural areas don't use the financial services provided to them because they find that financial services are costly & thus are unaffordable. So, even if the financial services are available to them, they don't use it because of high costs. (B.Singh, Tandon,2011)

II)Financial Exclusion:

Financial exclusion is also a barrier to financial inclusion. It means that financial services are used only by a section of the population. Financial services are demanded by people but it has not been provided. Rural regions, poor regions & those living in area where the services are difficult to provide are deprived of access to financial services. So, the excluded section borrow the funds from the moneylenders at high rate. This leads to a vicious circle. It implies two things:

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•Firstly, high cost of finance means that first poor person has to earn much more than someone who has access to lower cost finance.
•Secondly, the major portion of the earnings goes to the moneylenders & the person can never come out of the poverty. (B.Singh, Tandon,2011)

III)Behavioural aspects:

It is found that many people are not comfortable in using formal financial services because they find difficulty in understanding language, various documents & conditions that come with financial services etc. So, the financial illiteracy is one of the major barrier to financial inclusion. (B.Singh, Tandon, 2011)

IV)Non- price Barriers:

The following are the non- price barriers to financial inclusion:
•To use the formal financial services, person requires documents of proof regarding his identity, income etc. & the poor people don't have these documents, so they are excluded from the services.
•Initially if they subscribe to the services, they don't use them actively as others do because of high distance between bank & residence, poor infrastructure etc. (B.Singh, Tandon,2011)

Various approaches to achieve Financial Inclusion in India:

Use of Models is by no way sufficient till proper regulatory and policy changes are made in the financial system in the country. So, In India, various measures have taken by banks, Government of India and Reserve Bank of India for financial inclusion plan.

Product Based Approach:

While making policies, Reserve Bank of India has been so liberal & supportive so that the financial institutions can come up with the innovative financial products & enable a common man to get the advantage of the financial inclusion plan. Some products which were developed to the fulfilment of this approach are following:

•No Frills Account (NFAs): The concept of No Frills Account was introduced by RBI in November 2005 to provide access to basic banking services by financially excluded people. Under this approach banks open accounts for the under-privileged with zero balance or very minimum balance . In 2012, the banks under RBI guidelines came-up with a better idea of the no-frill accounts where they would open Basic Savings Bank Deposit Accounts (BSBDAs) for all individuals with the facility of debit card, internet banking , cheque books, overdraft limits at minimal charges.

•Kisan Credit Cards (KCCs): Under this scheme banks issue smart cards to the farmers for providing timely and adequate credit support for their farming needs. During 2012-13 (up to December 2012), public and private sector banks issued 1.2 million smart cards as KCCs. (Garg, Agarwal,2014)

•General Purpose Credit Cards (GCC): In 2005, Reserve Bank of India issued guidelines to banks regarding GCCs. It provided that GCCs will facilitate credit up to Rs. 25000/- to rural and semi urban people based on assessment of household cash flows & without any collateral requirement.(Garg, Agarwal,2014)

•Saving account with Overdraft facility: Banks have been advised to provide overdraft (OD) facility in saving account and also Small Overdrafts in No-frills accounts. The limit of overdraft would be set up by bank on the basis of transactions in the account. This would help the customers to get the credit at lower rates. (Garg, Agarwal,2014)

Bank Led Approach:

Self Help Group - Bank Led Initiative (SLBP or Self Help Group:

Bank Linkage Program has been started in India to cover the gap of reaching financially excluded population of the country. 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.

Basic features of self-help groups are:

•Voluntary savings apart from compulsory savings

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•Graduating selected members of the group that have entrepreneurship potential into a joint liability groups for borrowing larger amounts. (Garg, Agarwal, 2014)

Regulatory Approach:

•Simplified KYC (Know your Consumer) Norms:
Under current KYC norms, a customer has to provide number of documents for opening an account as per RBI guidelines. So, the people living in rural areas face problem in fulfilling these norms. To meet the objective of financial inclusion & to enable the banks to get the huge opportunity of rural banking , 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. (Garg, Agarwal,2014)

•Simplified bank saving account opening:
The account opening form has been simplified so that poorer sections, migratory labours & other street hawkers of the society can easily open the account in banks. (Garg, Agarwal,2014)

•Bank branch authorization:
RBI has permitted banks to open branches without taking authorization. So this would enable the government & the banks to speed up their efforts for financial inclusion & also make available the financial services to the poor section of the society. (Garg, Agarwal, 2014)

Technology Based approach:

•Mobile Banking: One of the most remarkable developments in terms of innovation is the full use of technology. Banks have shaken hands with mobile operators to provide financial services such as ticket booking, shopping etc. (Garg, Agarwal,2014)

• ATM based banking: In some states, the state government has taken initiatives for providing ATM based model for access to financial services. . Also banks have used the technology to enable their ATMs to virtually act like a 24x7 branches. (Garg, Agarwal,2014)

•Branchless Banking: It is a 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. But this concept is bringing by the leading banks & it is in a very initial stage. Also, there is a limitation in terms of initial cost for banks & literacy for the rural population. So, this concept is not widely used in urban & semi- urban areas. (Garg, Agarwal,2014)

•Aadhaar Enabled payment services: In this system, any Indian citizen having an Aadhaar number updates his account with the same. All accounts having Aadhaar number updated are to be reported to RBI, which in turn reports it to various government departments. So, while making payments to people for working under initiatives like MGNREGA or various subsidy schemes, the departments use this information for directly crediting the money to the beneficiary's account. This not only reduces the delay in the benefits being received by the end user, but also reduces the chances of corruption in the distribution of the benefits under schemes. So, this would encourage the customers to use his Aadhaar card number to excess various financial services. (Garg, Agarwal, 2014)

Knowledge Based Approaches:

Financial education, financial inclusion and financial stability are three elements of an integral strategy to encourage people to make effective use of the financial services. 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:

• Financial Stability Development Council (FSDC) focus on financial inclusion and financial literacy simultaneously.
• 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.

Government Initiatives:

The government has taken various initiatives indirectly through the regulators, government promoted schemes through its various ministries. Some of its initiatives are:

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•Women SHGs Development Fund: The Union Budget 2011-2012 proposed a "Women SHGs Development Fund" with an amount of Rs. 500 crore. The Government of India created this fund to empower women & promote their SHGs. (Garg, Agarwal,2014)

•Swarnjayanti Gram SwarozgarYojana(SGSY): It is a scheme which follows the pattern of forming SHGs of rural poor households. It is designed to promote self- employment oriented income generating activities for the Below Poverty Level (BPL) households in rural areas. (Garg, Agarwal, 2014)

•. National Rural Livelihood Mission (NRLM): It is established in June 2010 by the Ministry of Rural Development (MoRD), Government of India. This mission is based on the success of Indira KrantiPatham (IKP), a poverty alleviation program being implemented in Andhra Pradesh. The main strategies of NRLM are to:

» Improve monitoring & evaluation process.
» Introduce interest subsidy for encouraging repayments of loans
» Provide flexibilities to states for designing specific action plans for poverty alleviation. (Garg, Agarwal,2014)

• The Mahatma Gandhi National Rural Employment Guarantee Scheme (MGNREGS): This scheme aims to guarantee at least one hundred days of wage employment in a financial year to a rural household whose adult members volunteer to do unskilled manual work so that the livelihood of the rural people can be enhanced. As the payments are made through the bank/ post office accounts, in 2010-11, nearly 10 crore bank/ post office accounts have been opened. (Garg, Agarwal, 2014)

•Aadhaar- Unique Identification Authority of India (UIDAI): In 2009, Government of India has taken an initiative to provide an individual identification number to every citizen of India. It established the UIDAI to issue these cards on behalf of the Government of India. . This number which is provided by UIDAI will serve as a proof of identity and address, anywhere in India. The Aadhaar number will also enable people to have access to services such as banking, mobile phone connections and other government and non-government services. (Garg, Agarwal,2014)

• PradhanMantri Jan DhanYojana: PradhanMantri Jan DhanYojana has been announced recently to further Financial Inclusion in India. This scheme has been launched with the objectives of :

» Providing universal access to Banking Facilities
» providing basic banking accounts with overdraft facility
» Financial literacy programs
» Unorganised sector pension schemes &
» RuPay Debit card to all households.

Conclusion & Recommendations:

Access to financial services such as savings, insurances is extremely important for the poverty alleviation & development of India. In order to achieve the goal of total financial inclusion in India, policymakers, banks, NGOs & regulators have to work together. (B. Singh, Tandon, 2011). They will have to adopt such type of policies through which they can reach to the poorer & backward sections of the country & enable them to access of the financial services & products. Also, they have to ensure that the unbanked people have at least one bank account & they may get the financial services at affordable costs.

Way Forward

Innovation: Banks have to think and act differently and make themselves more flexible so as to meet even the smallest requirements of the rural population. Banks need to move from a cost centric model to a revenue generating model by offering large number of deposit, credit and other products and services. The products and services should be designed in such a way that it suits the needs of people in unbanked rural areas. (United Nations Conference on Trade &Development, 2014)

Transactions: During the first phase of financial inclusion initiative, the only motive was the opening of bank accounts for large number of individuals in the rural areas. Then, going forward the idea is to enable more transactions in these accounts by providing more credit products, which will help the rural people to avail credit at comparatively lower rates of interest. So, banks have been advised to link all the individuals to the banking system. (United Nations Conference on Trade &Development, 2014)

Collaborated Efforts: Total Financial Inclusion cannot be achieved without the active involvement of all stakeholders like RBI, other financial regulators, banks,

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governments, NGOs, civil societies, etc. The current policy objective of inclusive growth with financial stability cannot be achieved without ensuring universal financial inclusion. Banks alone will not be able to achieve this unless an entire support system will help in this mission. All the stakeholders need to join hands and make it possible. (United Nations Conference on Trade &Development, 2014)

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