Journal of Accounting and Finance
Volume 28, No. 1
October 2013-March 2014

Gauging the Potential of Financial Inclusion: Evidence From Indian Scenario

Sanjeev Sharma

Abstract

Financial inclusion refers to the process of extending financial products and services at an affordable cost to the weaker and vulnerable sections of the society in a visible and fair manner. Financial inclusion envisages low-cost banking services to the financially excluded population and regions of the country. 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. The objective of financial inclusion is to extend the scope of activities of the organised financial system to include within its ambit people with low incomes. It attempts to lift the poor from one level to another so that they come out of poverty. In India, the basic concept of financial inclusion is having a saving account or current account with any bank. In reality it includes loans, insurance services and much more. Financial Inclusion in developing countries is different than that of developed countries. In latter where inclusion implies a minority whereas in case of former it means a majority. In advanced economies, Financial Inclusion is more about the knowledge of fair and transparent financial products and a focus on financial literacy. In emerging economies, it is a question of both access to financial products and knowledge about their fairness and transparency. 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. It has proved a major breakthrough in accessibility of banking services to the vast rural population of the country. This was a significant effort towards financial inclusion, which led to the spread of bank branches in unbanked rural and semi-urban areas. Revamping of cooperative banking structure, directed credit policy like priority sector lending and the micro-finance effort taken by National Bank for Agriculture and Rural Development, Kisan Credit Card Scheme and Swarnajayanti Gram Sworozgar Yozna scheme of subsidised finance are some of the measures taken in the direction of financial inclusion. Unfortunately, in spite of enhanced outreach of banks in rural and semi-urban areas and the implementation of direct credit, farmers & rural artisans still did not receive adequate credit from banks during post-liberalisation period. 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 reach them. Financial exclusion is not the just an Indian centric problem- this is a global conundrum as well. On 29th December, 2003, on the occasion of International Year for Microcredit, Former Secretary General of the United Nations Kofi Annan remarked, "The stark reality is that most poor people in the world still lack access to sustainable financial services, whether it is *savings, credit or insurance. The great challenge before us is to address the constraints that exclude people from full participation in the financial sector. Together, we can and must build inclusive financial sectors that help people improve their lives."*

The present study has made a humble attempt to gauge the potential of financial inclusion in penetration of banking services in rural and urban areas and its impact on the quality of life of people in these areas. The study also highlighted various financial inclusion policies that have been adopted in India to increase the expansion of banking services to remote parts of the country. The study has been able to conclude that a multi-pronged strategy has to be adopted to enhance the outreach of banking services across all sections of the society.

Keywords: *Financial inclusion, Vulnerable Groups, Micro finance, Financial exclusion, No-frill accounts, Kisan Credit Cards, General Credit Cards, And Self Help Groups.*

Introduction

Economic development in a country is not possible without people's active participation. People of a developed country should not only enjoy the benefits but they generally generate those benefits as well. If growth benefits only the rich and higher income earner segment of the society, it is not possible and cannot be termed as development. The banking industry has shown tremendous growth in volume and complexity during the last few decades. Despite making significant improvements in all the areas relating to financial viability, profitability and competitiveness, there are concerns that banks have not been able to include vast segment of the population, especially the underprivileged sections of the society, into the fold of basic banking services. Access to finance by the poor and vulnerable group is a prerequisite for poverty reduction and social cohesion. This has to become an integral part of our efforts to promote inclusive growth.

Financial inclusion refers to the process of extending financial products and services at an affordable cost to the weaker and vulnerable sections of the society in a visible and fair manner. Financial inclusion envisages low-cost banking services to the financially excluded population and regions of the country. 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.

The objective of financial inclusion is to extend the scope of activities of the organised financial system to include within its ambit people with low incomes. It attempts to lift the poor from one

level to another so that they come out of poverty. In India, the basic concept of financial

inclusion is having a saving account or current account with any bank. In reality it includes loans, insurance services and much more. Financial Inclusion in developing countries is different than that of developed countries. In latter where inclusion implies a minority whereas in case of former it means a majority. In advanced economies, Financial Inclusion is more about the knowledge of fair and transparent financial products and a focus on financial literacy. In emerging economies, it is a question of both access to financial products and knowledge about their fairness and transparency.

Financial Inclusion in the Global Context

Financial exclusion is not the just an Indian centric problem- this is a global conundrum as well. On 29th December, 2003, on the occasion of International Year for Microcredit, Former Secretary General of the United Nations Kofi Annan remarked, "The stark reality is that most poor people in the world still lack access to sustainable financial services, whether it is savings, credit or insurance. The great challenge before us is to address the constraints that exclude people from full participation in the financial sector. Together, we can and must build inclusive financial sectors that help people improve their lives."

According to United Nations, the basic purpose of Financial Inclusion is to have:

a) Access of financial services at a reasonable cost to all households and enterprises;

b) Sound financial institutions guided by appropriate internal management system and performance standards and monitored by the market as well as by prudential regulations.

c) Financial and institutional sustainability to provide access to financial services over time;

d) To bring cost effectiveness through multiple providers of financial services.

The United Kingdom was one of the first countries to realize the importance of financial inclusion. The UK government set up the Financial Inclusion Fund of £120 million to promote financial inclusion. On 21st February 2005, it has set up The Financial Inclusion Task Force to monitor progress on financial inclusion and to make suitable recommendations. The Task Force has identified the following three priority areas of Financial Inclusion:

a) Access to banking

b) Access to affordable credit

c) Access to face to face advisory services.

To meet these minimum requirements of Financial Inclusion, the UK government has taken initiatives such as Credit Unions, Post Office Card Account, Saving Gateway, Community Finance Learning Initiatives, etc.

United State of America has framed a civil rights law known as Community Reinvestment Act (1997) which prohibits discrimination by banks against low and moderate income neighborhoods. The Act makes it obligatory for the banks to serve the needs for the credit and banking services of all the communities in which they operate.

Similarly, France has made a Law on Exclusion (1998) in which a person's right to have a bank account is emphasized. Even the developing world like Bangladesh, Indonesia, African and South American countries have made tremendous efforts in reaching the underprivileged people through specially designed program me like micro-finance program me, etc. Gramin Bank initiative taken by Bangladesh, Bank Royat in Indonesia and Banco Sol in Bolivia are some of the significant strides towards financial inclusion through micro-finance programme.

Financial Inclusion in the Indian Context

In India, growth with equity has been the central objective right from the inception of the planning process. 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. It has proved a major breakthrough in accessibility of banking services to the vast rural population of the country. This was a significant effort towards financial inclusion, which led to the spread of bank branches in unbanked rural and semi-urban areas. This is vital for sustaining long term equitable development since a large proportion of households areas do not have access to basic banking facilities. Unfortunately, the fruit of bank nationalization was not fully reaped. In spite of enhanced outreach of banks in rural and semi-urban areas and the implementation of direct credit, farmers & rural artisans still did not receive adequate credit from banks during post-liberalisation period. The first-ever Index of Financial Inclusion to find out the extent of reach of banking services among 100 countries, India has been ranked 50. Only 34% of Indian individuals have access to or receive banking services. In spite of the best efforts made by the Government and Reserve Bank over the past few years the situation has not shown much improvement in comparison to some of the advanced and developing countries (**Table-1**)

Table-1 Cross Country Comparison of Select Indicators of Financial Inclusion

Country	*Number of Branches (per 0.1million adults)*	*Number of ATMs (per 0.1million adults)*	*Bank loan as per cent of GDP*	*Bank deposits as per cent ofGDP*
India	10.64	8.90	51.75	68.43
Australia	29.61	166.92	128.75	107.10
Brazil	46.15	119.63	40.28	53.26
France	41.58	109.80	42.85	34.77
Mexico	14.86	45.77	18.81	22.65
United States	35.43	N/A	46.83	57.78
Korea	18.80	N/A	90.65	80.82
Philippines	8.07	17.70	21.39	41.93

Source: Financial Access Survey 2011, IMF.

The main reason for such 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 money lender 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.

Initiatives Taken by RBI Towards Financial Inclusion

In recent years, there has been a growing emphasis by the Government and Reserve Bank of India on providing formal financial services to the unbanked/under-banked areas. With the objective of expanding the outreach of banking services to remote part of the country, Reserve Bank of India has adopted multi-pronged strategies. In order to achieve the objective of universal financial inclusion, banks have been directed to use a combination of strategies, which include:

(a) provision of basic banking products;

(b) relaxation of branch authorization policy;

(c) introduction of the Business Correspondent/Business Facilitator (BF) model;

(d) directing commercial banks to open at least 25 per cent of their total branches in hitherto unbanked areas of the country;

(e) relaxation of existing regulatory guidelines in the form of lenient Know Your Customer (KYC) norms;

(f) enhanced use of technology; and

(g) setting up financial literacy and credit counseling centers in districts to achieve greater outreach.

Keeping in view the goal of bringing banking services to an identified 72,800 villages with a population above 2,000 by March 2012, and thereafter progressively to all villages over a period, banks were advised that while preparing their Annual Branch Expansion Plan, they should allocate at least 25 per cent of the total number of branches proposed to be opened during a year to unbanked rural (Tier V and Tier VI) centers. With the aim of providing enhanced banking services in Tier II centers, the general permission being granted to domestic scheduled commercial banks for opening branches in Tier III to Tier VI centers was extended to opening branches in Tier II centers (with population of 50,000 to 99,999 as per Census 2001) without the need to take permission from the Reserve Bank in each case, subject to reporting (Annual Report, RBI 2011-12)

In January 2006, the Reserve Bank permitted commercial banks to make use of the services of non-governmental organizations (NGOs/SHGs), micro-finance institutions and other civil society organizations as intermediaries for providing financial and banking services. These intermediaries could be used as business facilitators (BF) or business correspondents (BC) by commercial banks. In order to facilitate financial inclusion further, RBI has decided to permit inter-operability at the retail outlets or sub-agents of Business Correspondents *(i.e.,* at the point of customer interface), provided the technology available with the bank that has appointed the BC supports inter-operability, subject to the following conditions:

(i) the transactions and authentications at such retail outlets or sub-agents of BCs are carried out on-line;

(ii) the transactions are carried out on a core banking solution (CBS) platform; and

(iii) The banks follow the standard operating procedures to be advised by the Indian Banks' Association (IBA).

However, the BC or its retail outlet or sub-agent at the point of customer interface would continue to represent the bank that has appointed the BC.

Evaluating Progress of Financial Inclusion Initiative by RBI

a) Opening of branches in villages with population more than 2000

To achieve the objective of inclusive growth, the Reserve Bank has given high priority to the agenda of financial inclusion over the past few years. Initiatives were taken by the Reserve Bank in recent years to expand banking services to remote areas of the country.

The Table 2 shows the progress of banks in providing banking facilities in the villages having population more than 2000

Table 2: Progress in Roadmap for Providing Banking Outlets in Villages with Population of more than 2000

(As on March 31, 2012)

Region	*No. of villages covered (March 2010)*	*Bamking outlets opened in village with population> 2000 during March 2010- March 2012*				*Total no. of villages covered (March 2012)*	*Banking penetration in villages in March 2012 as multiple of position of March 2010*
		Branches	*BC*	*Other Modes*	*Total*		
Northern	4,363	241	7,868	67	8,176	12,539	2.9
North-Eastern	1,093	382	2,795	7	3,184	4,277	3.9
Eastern	6,767	444	19,019	579	20,042	26,809	4.0
Central	6,935	491	19,256	535	20,282	27,217	3.9
Western	3,409	208	6,849	816	7,873	11,282	3.3
Southern	5,894	727	13,587	328	14,642	20,536	3.5
All-India	28,461	2,493	69,374	2,332	74,199	1,02,660	3.6

Source: Report on Trend and Progress of Banking in India 2011-12

As at end-March 2012, 99 per cent of the identified villages have been provided with banking outlets. Four States, *viz.*, Uttar Pradesh, Bihar, West Bengal and Andhra Pradesh accounted for more than 50 per cent of these newly opened banking outlets. On a positive note, all identified villages in the north-eastern region have been provided with banking outlets. Region-wise analysis of the progress made in banking penetration indicated that significant progress has been made in eastern as well as north-eastern region on this front. Bank group-wise analysis of new banking outlets in identified villages revealed that public sector banks as well as RRBs played a key role in expanding the banking network in rural India.

b) Progress Of Financial Inclusion Plans

As a policy initiative RBI has advised all public and private sector banks to put in place Board approved three-year financial inclusion plans (FIPs) from April 2010 onwards. The FIP should broadly contain self-set targets with respect to:

i) opening rural brick and mortar branches;

ii) deployment of BCs;

iii) coverage of villages with population of more than 2000 as also other un-banked villages with population below 2,000 through branches/BCs/other modes;

iv) opening no-frills accounts including through BC-ICT;

v) issuing Kisan Credit Cards (KCCs) and General Credit Cards (GCCs), and other specific products designed by them to cater to the financially excluded segments.

The **Table 3** discloses the progress made by banks during last three years:

Table 3: Progress under Financial Inclusion Plans

Sr. No.	Particulars	As On 31st March,2011	As On 31st March,2012	As On 31st March,2013
1.	Banking Outlets in Villages > 2,000	66,605	1,12,288	1,19,453
2.	Banking Outlets in Villages < 2,000	49,603	69,465	1,49,001
3.	Total Banking Outlets in Villages of Which	1,16,208	1,81,753	2,68,454
	3.1 Branches	34,811	37,471	40,837
	3.2 BCs	80,802	1,41,136	2,21,341
	3.3 Other Modes	595	3,146	6,276
4.	Urban Locations covered through BCs	3,771	5,891	27,143
5.	ICT Based A/Cs- through BCs (No. in millions)	32	57	81
6.	ICT Based A/Cs- Transactions (No. in millions)	84	156	250
7.	ICT Based A/Cs- Transactions (Amount in billions)	58	97	234
8..	Number of No-Frills Accounts (in millions)	105	139	182
9.	Amount in No-Frills Accounts (in billions)	76	120	183
10.	Number of No-Frills Accounts with OD (in millions)	1	3	4
11.	Amount in No-Frills Accounts with OD (in billions)	0.3	1	2
12.	No. of KCC outstanding (in millions)	27	30	34
13.	Amount in KCC outstanding (in billions)	1,600	2,068	2,623
14.	No. of GCC outstanding (in millions)	2	2	4
15.	Amount in GCC outstanding (in billions)	35	42	76

Source: Compiled from Report on Trend and Progress of Banking in India 2012-13

An analysis of the above table shows that the progress made by banks in achieving FIP during the last three years has been impressive. The table shows that there has been a tremendous growth in number of banking outlets having population less than 2,000 for the year ended March 31, 2013 in comparison to March31, 2012. It shows that penetration of banking has increased multi-fold in rural areas. As at end-March 2013, villages covered through BCs constituted more than 82 per cent of the total villages covered under the FIP. This indicates move towards the widespread acceptance of BC model of financial inclusion by banks as well as consumers in rural India. Further, *Volume of transactions through ICT-based accounts increased steadily*. No-frills accounts enable small customers to avail of hassle-free credit in the form of in-built overdraft facility. The total number of no-frills accounts had surpassed 180 million in 31st March, 2013 and had shown a growth of over 50% in 2012 & 2013. One welcome development noticed in this regard is that, the number of ICT-based accounts as percentage of no-frills accounts has witnessed steady increase in the last three years, indicating increased acceptance of ICT-based products among rural customers.

c) **Progress Of SHG Bank Linkage Programme and Micro-Finance**

The self-help group (SHG) - bank linkage programme started in 1992 as a pilot project initiated by NABARD and involving three agencies, *viz.*, the SHGs, banks and NGOs. Though progress under the SHG-bank linkage programme was slow during the initial years of commencement, it started expanding rapidly after 1999. The analysis of **Table 4** shows that though the number of SHGs maintaining savings accounts with banks decreased during 2012-13, compared with the previous year, yet total amount of SHG savings outstanding in banks has increased. Further, the table clearly reveals that micro-finance institutions have emerged as an important conduit of channeling credit to the rural parts of the country, due to their widespread reach in these areas as well as the ability to offer customized financial products, suited to the needs of average rural customers.

Table 4: Progress of Micro-finance Programmers

(As at end-March)

Item	*Self Help Groups**							
	Number (in millions)				*Amount (in billions)*			
	2009-10	*2010-11*	*2011-12*	*2012-13(P)*	*2009-10*	*2010-11*	*2011-12*	*2012-13(P)*
Loans disbursed by banks	1.6 (0.3)	1.2 (0.2)	1.2 (0.2)	1.2 (0.2)	145 (22)	145 (25)	165 (26)	206 (22)
Loans outstanding with banks	4.9 (1.3)	4.8 (1.3)	4.4 (1.2)	4.5 (1.2)	280 (63)	312 (78)	363 (80.5)	394 (86)
Savings with banks	7.0 (1.7)	7.5 (2.0)	8.0 (2.1)	7.3 (2.1)	62 (13)	70 (18)	66 (14)	82 (18)

Item	***Micro-Finance Institutions***							
	Number (in millions)				*Amount (in billions)*			
	2009-10	*2010-11*	*2011-12*	*2012-13(P)*	*2009-10*	*2010-11*	*2011-12*	*2012-13(P)*
Loans disbursed by banks	691	469	465	426	81	76	53	78
Loans outstanding with banks	1,513	2,176	1,960	2042	101	107	115	144

Notes: 1. *: Figures in brackets indicate the details about SHGs covered under Swarnajayanti Gram Swarozgar Yojana (SGSY). 2. P: Provisional data.

Source: NABARD.

Conclusion

Financial inclusion refers to the process of extending financial products and services at an affordable cost to the weaker and vulnerable sections of the society in a visible and fair manner. Financial inclusion envisages low-cost banking services to the financially excluded population and regions of the country. Financial Inclusion in developing countries is different than that of developed countries. In latter where inclusion implies a minority whereas in case of former it means a majority. In advanced economies, Financial Inclusion is more about the knowledge of fair and transparent financial products and a focus on financial literacy. In emerging economies, it is a question of both access to financial products and knowledge about their fairness and transparency. Revamping of cooperative banking structure, directed credit policy like priority sector lending and the micro-finance effort taken by National Bank for Agriculture and Rural Development, Kisan Credit Card Scheme and Swarnajayanti Gram Sworozgar Yozna scheme of subsidised finance are some of the measures taken in the direction of financial inclusion. Unfortunately, in spite of enhanced outreach of banks in rural and semi-urban areas and the implementation of direct credit, farmers & rural artisans still did not receive adequate credit from banks during post-liberalisation period. 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 reach them. Thus, a multi-pronged strategy has to be adopting ted to enhance the outreach of banking services across all sections of the society.

References

Chakrabarty K.C. (2013), Deputy Governor, RBI. Keynote address on "Financial Literacy and Financial Inclusion-India Way", March 6.

Goplan V. (2011), "Financial Inclusion: Current Status in India", The Management Accountant, February, Vol.46 No.2.

Khan Harun R. (2012), Deputy Governor, RBI. Keynote address on "Financial Inclusion & Payment System: Recent Trends, Current Challenges and Emerging Issues", November 25.

Klapper and Demirguc-Kunt (2012), 'Measuring Financial Inclusion: The Global Findex Database', World Bank Policy Research Paper 6025.

Michael Chibba (2009), "Financial Inclusion, Poverty Reduction and the Millennium Development Goals", European Journal of Development Research Vol. 21,

Pati A. P. (2009), "Enhancing Financial Inclusion: The Catalytic Role of Self Help Group", The Management Accountant, May, Vol.44, No. 05.

The Report on Trend and Progress of Banking In India, RBI 2010-11, 2011-12, 2012-13.

www.rbi.org.in

www.nabard.org.in

Dr Sanjeev Sharma, Post Graduate Department Of Commerce & Business Management, Hindu College, Amritsar, Punjab, India.