

An Overview of Financial Inclusion and rural development in India

Gomathy M

Research Scholar, MBA, M.Phil

Abstract: Inclusive growth is possible only through proper allocation and accessing of all the resources from top to bottom. Financial inclusion is an innovative concept which makes alternative techniques to promote the banking habits of the rural people because, India is The largest rural people consist in the world. The Eleventh Five year Plan (2007-12) envisaged inclusive growth as a key objective as well as a strategy for economic development. Financial inclusion is aimed at providing banking and financial services to all people in a fair, transparent and equitable Manner at affordable cost. The main objectives of this study were to know the rural development taken by the banks for financial inclusion, to examine the difficulties involved in the adoption of financial inclusion and also to enhance the extent of financial inclusion. The data required for the study was collected from both primary and secondary sources. The total numbers of samples were 50. The study was conducted among the banks in thiruvallur District. The banks should encourage the people to access banking services by ways of no frills account, financial inclusion campaign and business correspondent. The government should encourage the banks to adopt financial inclusion by means of financial assistance, advertisement and awareness programs etc. to achieve the aim of 11th plan of Inclusive Growth. Households with low income often lack access to bank account and have to spend time and money for multiple visits to avail the banking services, be it opening a savings bank account or availing a loan, these families find it more difficult to save and to plan financially for the future. This paper is an attempt to discuss the overview of financial inclusion and rural development in India.

Key Words: Financial Inclusion, Reserve Bank, Inclusive Growth, Financial services, General Credit Cards (GCC), Electronic Benefit Transfer (EBT).

I. Introduction

It has been universally accepted today that the objective of Inclusive growth cannot be attained without Financial Inclusion. This has led to a paradigm policy shift for financial inclusion for economic growth. "The new rural finance paradigm is premised on the fact that rural people are bankable." (Nagarajan and Meyer, 2006) In fact, access to affordable finance enables the poor and vulnerable groups to undertake economic activities and take advantage of growth opportunities for economic empowerment. Hence, developing an inclusive financial system to provide equal opportunities to all in accessing financial services at affordable costs is a pre-condition for achieving accelerated economic growth along with a reduction in income inequality and poverty. Without an inclusive financial system, poor and vulnerable section of the community and small and petty enterprises would not be in a position to take advantages of growth opportunities. And rural communities remain the largest unserved market for financial services. Ensuring their financial inclusion can unlock the considerable economic potential of rural areas.

Rural communities are highly underserved. Traditionally, formal financial institutions have avoided or failed to offer sustainable services in rural areas (e.g. rural or agricultural development banks). Thus, informal or semi-formal financial institutions as well as alternative providers like traders or input suppliers have become major providers of financial services. However, these informal providers often have weak institutional and managerial capacity; and operating in isolation from the financial system has let some of these providers charge steep interest rates. People living in rural areas may need access to financial services to purchase agriculture inputs; obtain veterinary services; maintain infrastructure; contract labor for planting/harvesting; transport goods to markets; make/receive payments; manage peak season incomes to cover expenses in low seasons; invest in education, shelter, health; or deal with emergencies. Reserve Bank of India vision for 2020 is to open nearly 600 million new customers' accounts.

Financial Inclusion: Conceptual Framework

Financial services or products provided by banks, finance companies, postal saving banks, credit unions, insurance companies and micro-finance institutions and other formal financial institutions generally form the basis for financial inclusion. The financial services Rendered by the informal sources such as money lenders, traders etc do not come under the purview of financial inclusion as they are limited in supply and

exploitative in nature. The formal financial institutions help mobilize savings and efficient allocation of funds for development.

In most developing countries, a large segment of the population particularly low income and vulnerable section of the society has very little or no access to financial services from formal financial system. It is estimated that globally over two billion people are currently excluded from the access to financial services (UN, 2006). They normally depend on their own limited resources or informal sources of finance at an exploitative term. Unless the financial system is inclusive, the benefit of financial services is likely to elude many individuals and enterprises and thereby, denying much of the population the benefit of growth opportunities.

The Vision Of Inclusive Financial System Would Be Characterized By:

- Access at reasonable cost of all households and enterprises to the range of financial services for which they are 'bankable' including savings, credit, leasing and factoring, mortgages, insurance, pensions, payments and local and international transfers.
- Sound institutions guided by appropriate internal management systems, industry performance standards and performance monitoring by the market, as well as by sound prudential regulation where required;
- Financial and institutional sustainability as a means of providing access to financial services over time.
- Multiple providers of financial services, so as to bring cost effective and a wide variety of alternatives to customers (UN, 2006).

Broadly, financial inclusion means access to finance and financial services for all in a fair, transparent and equitable manner at an affordable cost. In a perfect competitive financial market, there are no frictions. It is financially inclusive and facilitates efficient allocation of financial resources and welfare by providing a whole range of efficient financial services. Hence, there is no problem of financial exclusion in an inclusive perfect financial system.

II. Review of Literature

- ★ Joseph Massey (2010) said that, role of financial institutions in a developing country is vital in promoting financial inclusion. The efforts of the government to promote financial inclusion and deepening can be further enhanced by the pro-activeness on the part of capital market players including financial institutions. Financial institutions have a very crucial and a wider role to play in fostering financial inclusion. National and international forum have recognized this and efforts are seen on domestic and global levels to encourage the financial institutions to take up larger responsibilities in including the financially excluded lot.
- ★ Mandira Sarma and Jesim Paise (2008) suggest that the issue of financial inclusion is a development policy priority in many countries. Using the index of financial inclusion developed in levels of human development and financial inclusion in a country move closely with each other, although a few exceptions exist. Among socio-economic factors, as expected, income is positively associated with the level of financial inclusion. Further physical and electronic connectivity and information availability, indicated by road network, telephone and internet usage, also play positive role in enhancing financial inclusion.
- ★ Michael Chibba (2009) noted that Financial Inclusion is an inclusive development and Poverty Reduction strategy that manifests itself as part of the emerging FI-PR-MDG nexus. However, given the current global crises, the need to scale-up Financial Inclusion is now perhaps more important as a complementary and incremental approach to work towards meeting the MDGs than at any other time in recent history.
- ★ Oya Pinar Ardic et al (2011) explained that using the financial access database by CGAP and the World Bank group, this paper counts the number of unbanked adults around the world, analyses the state of access to deposit and loan services as well as the extent of retail networks, and discusses the state of financial inclusion mandates around the world. The findings indicate that there is yet much to be done in the financial inclusion arena. Fifty-six percent of adults in the world do not have access to formal financial services.

III. Objective of the Study

The purpose of the study is to evaluate the need of Financial Inclusion in India. In order to achieve this objective the following issues have been examined:

1. To evaluate the role of different Financial Institutions towards Financial Inclusion.
2. To examine the extent of financial exclusion in rural India
3. To enquire into the role of microfinance in helping the rural population in the case of financial inclusion.

IV. Scope for Further Research

In financial inclusion, there are a few potentially interesting areas for future research –viz.

- a. The most appropriate delivery model (which banks are still trying to figure out) for different geographical regions given their unique characteristics,
- b. The unbanked segments- bait in rural, urban or metropolitan areas is largely served by the un-organized sector even today. Research into the products, practices and procedures of this unorganized sectors an absolute imperative, to identify and understand the same which the bottom of the pyramid populace finds so convenient and comfortable to deal with. This could throw up valuable leads for the organized sector – banks and financial institutions to follow,
- c. Further, in order to measure the intensity of money lenders especially in rural areas, research agencies should, inter alia, conduct a census of money lenders in rural India.

V. Methodology

The data required for the study was collected from secondary sources. Data published by various institutions such as Government of India, World Bank, Consultative Group to Assist the Poor (CGAP), Reserve Bank of India (RBI), National Bank for Agriculture and Rural Development (NABARD, State Level Bankers" Committee (SLBC), etc are used for the purpose of the present paper.

VI. Analysis

Rural communities could make use of a wide range of financial services like...

- savings
- money transfer services
- insurance products
- loans
- leasing
- factoring
- loan guarantees
- venture capital
- investment funds
- Mainstreaming access to insurance services for rural communities -
- PWDS India

Since 2008 the ILO's (international labor office) Micro insurance Innovation Facility has supported the Palmyrah Workers' Development Society (PWDS) in Tamil Nadu. PWDS works with rural families in the informal economy lacking access to social and health security and whose income is often at risk by health shocks that force families towards emergency loans and debt. PWDS's beneficiaries are self-help groups comprising over 350,000 families. The project pilots a business model for mainstreaming access to insurance services for rural communities. The model identifies, strengthens and leverages existing relationships and channels that build on trust. It tests the efficacy of existing self-help groups' federations as 'insurance service providers', by helping them build an insurance team to link between the communities and the insurers. Starting with health, the project is to develop an information and document flow within the federation-community system to provide low cost premium collection and claims servicing. The goal is to develop a self-sustaining retail distribution that provides relevant products to low-income communities.

- Promote a savings and insurance culture among rural populations through awareness campaigns, financial education trainings or experience/testimony-sharing among insured and uninsured people.
- Support savings mobilization by prudential regulation of deposit-taking financial intermediaries. Do not crowd-out savings mobilization by supply of public and donor resources.
- Avoid pressuring informal or semi-formal institutions to become regulated large formal institutions. Informal institutions have unique advantages that can be leveraged by linking them to formal finance.
- Integrate rural finance into the broader financial system development agenda. For example, the Ministry of Finance in Uganda, under the participation of industry stakeholders, created a "Microfinance Outreach Plan" to motivate financial institutions to expand their services in rural areas.
- Support index-based insurance products like weather-based crop insurance by providing accurate statistical data (e.g. on regional rainfall) and infrastructure (e.g. weather stations) to collect data and make it available to insurers.
- Integrate financial components in interventions like entrepreneurship development or local economic development.
- Improve infrastructure to lower transaction costs (e.g. in communications, electricity, transportation).

VII. Financial inclusion initiatives

- Advised all banks to open Basic Saving Bank Deposit (BSBD) accounts with minimum common facilities such as no minimum balance, deposit and withdrawal of cash at bank branch and ATMs, receipt/ credit of money through electronic payment channels, facility of providing ATM card.
- Relaxed and simplified KYC norms to facilitate easy opening of bank accounts, especially for small accounts with balances not exceeding Rs. 50,000 and aggregate credits in the accounts not exceeding Rs. one lakh a year. Further, banks are advised not to insist on introduction for opening bank accounts of customers. In addition, banks are allowed to use Aadhar Card as a proof of both identity and address.
- Simplified Branch Authorization Policy, to address the issue of uneven spread bank branches, domestic SCBs are permitted to freely open branches in Tier 2 to Tier 6 centers with population of less than 1 lakh under general permission, subject to reporting. In North-Eastern States and Sikkim domestic SCBs can open branches without having any permission from RBI. With the objective of further liberalizing, general permission to domestic scheduled commercial banks (other than RRBs) for opening branches in Tier 1 centers, subject to certain conditions.
- Compulsory Requirement of Opening Branches in Un-banked Villages, banks are directed to allocate at least 25% of the total number of branches to be opened during the year in un-banked (Tier 5 and Tier 6) rural centers.
- Opening of intermediate brick and mortar structure, for effective cash management, documentation, redressal of customer grievances and close supervision of BC operations, banks have been advised to open intermediate structures between the present base branch and BC locations. This branch could be in the form of a low cost simple brick and mortar structure consisting of minimum infrastructure such core banking solution terminal linked to a pass book printer and a safe for cash retention for operating larger customer transactions.
- Public and private sector banks had been advised to submit board approved three year Financial Inclusion Plan (FIP) starting from April 2010. These policies aim at keeping self-set targets in respect of rural brick and mortar branches opened, BCs employed, coverage of un-banked villages with population above 2000 and as well as below 2000, BSBD accounts opened, KCCs, GCCs issued and others. RBI has been monitoring these plans on a monthly basis.
- Banks have been advised that their FIPs should be disaggregated and percolated down up to the branch level. This would ensure the involvement of all stakeholders in the financial inclusion efforts.
- In June 2012, revised guidelines on Financial Literacy Centers (FLCs). Accordingly, it was advised that FLCs and all the rural branches of scheduled commercial banks should scale up financial literacy efforts through conduct of outdoor Financial Literacy Camps at least once a month, to facilitate financial inclusion through provision of two essentials i.e. "Financial Literacy" and easy 'Financial Access'. Accordingly, 718 FLCs have been set up as at end of March 2013. A total of 2.2 million people have been educated through awareness camps, seminars and lectures during April 2012 to March 2013.

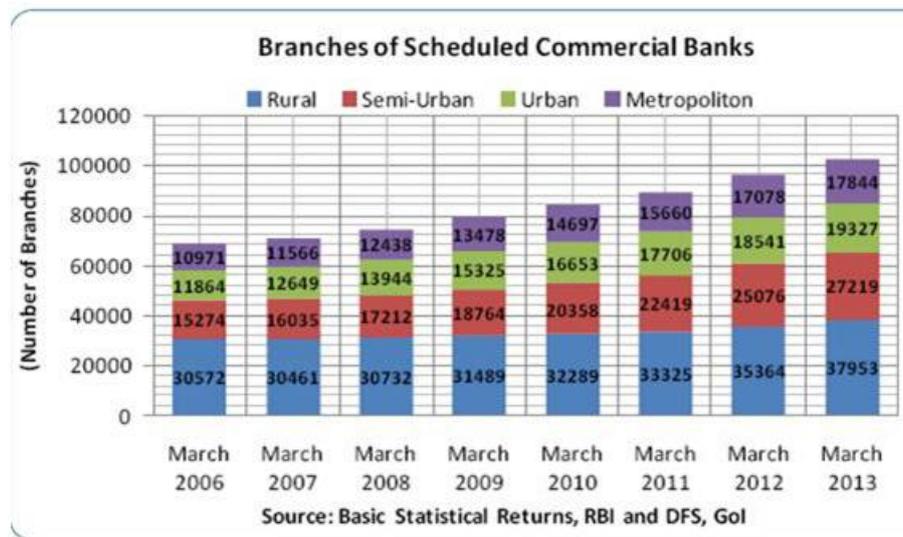
VIII. Provide an enabling environment

- ❖ Abolish or do not reinstate interest rate ceilings that do not allow full cost recovery for financial service providers, especially those who service rural and remote populations. Private providers may be forced out of operation in the rural market or grow more slowly, thus leaving clients with limited choice.
- ❖ Abstain from direct credit schemes or subsidised first-tier government lending programmes. It is common that governments and project management units lack the technical skills and political independence needed to manage these schemes, which are often associated with low recovery rates. Also, they may offer below-market interest rates that crowd-out private providers and when the programme discontinues, clients remain with a limited choice.
- ❖ Increase financial literacy of rural communities through financial education in school and training curricula so they are empowered to take informed financial decisions in their households and in their businesses

Increase capacity of financial institutions to serve rural and remote areas:

- Strengthen management capacity and governance of informal and semi-formal financial service providers, like Savings and Credit Cooperatives (SACCOs), village banks or informal savings groups, for instance through community training on how to set up and manage member-owned institutions.
- Link informal providers to formal financial institutions. Local member-owned institutions have the flexibility and accountability (entailing trust) needed to penetrate remote areas, but their potential is limited due to their isolation. When linked to the financial system, they can expand the range of services offered.
- Develop alliances among various types of institutions, for instance channel life or health insurance through local hospitals or provide credit along the agricultural value chain (e.g. via rural trader shops, or agricultural processing firms).

- Facilitate portfolio diversification of financial institutions to mitigate risk stemming from concentrated agricultural portfolios. Consider the risk in financial portfolios resulting from climate change.
- Regularly assess if supply for financial services meets demand.



- Due to RBI's concerted efforts since 2005, the number of branches of Scheduled Commercial Banks increased manifold from 68,681 in March 2006 to 1, 02,343 in March 2013, spread across length and breadth of the country (above chart).
- In rural areas, the number of branches increased from 30,572 to 37,953 during March 2006 to March 2013. As compared with rural areas, number of branches in Semi-urban areas increased more rapidly.
- Through the Microfinance for Decent Work Action Research Programme (MF4DW), launched in 2008, the ILO is studying the impact of innovations in microfinance on poor households and their businesses. MF4DW is working with 16 microfinance institutions across the world on reducing child labor, improving working conditions and risk management strategies, encouraging formalisation, or increasing job creation.
- Through the Micro insurance Innovation Facility, launched in 2008, the ILO seeks to increase the availability of quality insurance for the developing world's low-income families, the majority of whom live in rural areas, to help them guard against risk and overcome poverty. It provides grants to support organizations develop innovations in the micro insurance sector, and offers a range of customized services to support micro insurance consultants and providers deliver value to the poor.

IX. Discussion Of Results

The process of financial inclusion is an attempt to bring within the ambit of the organized financial system the weaker and vulnerable sections of society. Financial inclusion can be defined as the delivery of credit and other financial service at an affordable cost to the vast sections of the disadvantaged and low income groups. The objective of financial inclusion is to extend the scope of activities of the organized financial system to include, within its ambit, people with low incomes. Through graduated credit, attempts must be made to lift the poor so that they come out of poverty. Financial inclusion may, therefore, be defined as the process of enabling access to timely and adequate credit and other financial service by vulnerable groups, such as weaker sections and low income groups at affordable cost. The target for National Rural Financial Inclusion Plan (NRFIP) is to provide access to comprehensive financial services to at least 50% (55.77 million) of the excluded rural cultivator and non cultivator households, across different States by 2012 through rural/ semi urban branches of Commercial Banks and Regional Rural Banks.

X. Recommendations

1. Banking technology has progressed fast enough and more importantly the realization that the poor is bankable has arrived. Various immediate measures which government of India should implement or which are under implementations but should be executed in a more effective manner
2. Strengthen agency banking micro finance institutions, business facilitators and business correspondents. Our very old post offices will be an ideal channel to pursue the future long term goals of agency banking especially in rural India.

3. Achieve synergies between the technology providers and banking channels to expand reach. Application developers will be required to synergize core banking with micro financial applications.
4. Have interest rate ceilings specified for NGO/MFI for they tend to charge higher rates of interest in a sugar coated form. These legalities can be introduced once an NGO/MFI enters into partnership with a bank.
5. The government should include financial literacy in the curriculum of schools and colleges. The government should also raise the Financial Inclusion Fund and a Financial Inclusion Technology Fund to reach banking services to the unbanked areas. The government should pay all the social security payments through the bank account of the beneficiary.
6. The banks should offer all forms in the regional language of the customers. The banks must create awareness among the people concerning the significance of banking services by advertisement and financial inclusion campaign. ATMs are one of the most cost effective ways of reaching the rural poor. Thus, new biometric ATMs have to be established to assist the customers who are unable to memorize PIN. The banks should constitute Grievance Redressal Machinery to redress the customer's discontent promptly. And also it should offer no frills account in order to turn unbankable into bankable. The banks should appoint a business correspondent to disseminate its service to the unreached area. Technology can play a major role in reducing the cost of availing financial services. Thus, banks should adopt advanced technology to open up new avenues for service delivery.

XI. Conclusion

It is beyond doubt that after nationalization of banks in 1969, the reach of CBs, RRBs, Co-operative credit institutions have remarkably increased in rural areas but a group of society remains ignored from the financial services. The progress in rural India and emerging developments are providing banks an immense opportunity to grow their business and bring prosperity to the aspiring poor through financial inclusion. Rising rural incomes, growing consumption, public policy focus on inclusive growth rollout of several Govt. schemes Research journal's Journal of Commerce Vol. 2 | No. 1 February | 2014 ISSN 2348-0955 6 www.researchjournali.com aimed at rural India. Payment of wages / social security payments / other benefits through EBT directly into bank Accounts creating several opportunities for banks to play an active role in rural India. To conclude banks should take a step forward to formulate specific plans to enhance Financial Inclusion of unbanked section of the society. At the same time they should device the strategies to reduce their transaction cost to actively participate in the process of Financial Inclusion treating it as Business Opportunity and Corporate Social Responsibility.

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