The Road Map of Financial Inclusion in India

***Dr.V.Dheenadayalan**

*** Assistant Professor in Commerce, Annamalai University, Tamilnadu**

Abstract

Financial Inclusion (FI) is delivery of banking services at an affordable cost to the vast sections of underprivileged and low income groups. By financial inclusion we mean the provision of affordable financial services, viz., access to payments and remittance facilities, savings, loans and insurance services by the formal financial system to those who tend to be excluded. It is important to recognize that in the policy framework for development of the formal financial system in India, the need for financial inclusion and covering more and more of the excluded population by the formal financial system has always been consciously emphasized. This paper trace out the Reasons for Financial Exclusion , Need, Benefits of Financial Inclusion, The Road Map of Financial Inclusion in India Financial Inclusion Practice in India , An Outcome of Financial Inclusion Measures In India and concluded with suggestion of Banks shall expand financial inclusion initiatives in urban and semi-urban areas by targeting pockets of migrant workers and small vendors and leveraging Aadhaar enrolment for opening bank accounts.

Key Words: Financial Exclusion, Financial Inclusion Practice, Financial Inclusion Measures in India

Financial Inclusion (FI) is delivery of banking services at an affordable cost to the vast sections of underprivileged and low income groups. By financial inclusion we mean the provision of affordable financial services, viz., access to payments and remittance facilities, savings, loans and insurance services by the formal financial system to those who tend to be excluded. It is important to recognize that in the policy framework for development of the formal financial system in India, the need for financial inclusion and covering more and more of the excluded population by the formal financial system has always been consciously emphasized.

The FI quotient of a country is recognized as an important parameter to gauge the country's overall economic and social development. India has emerged as one of the fastest growing economies, the challenge is to spread and sustain the growth rate in different sectors and different sections of the society. There is a huge disparity between the financial services accessible and provided to different sections in our country. Only 40% of the population has an access to financial services in the country. The remaining are financially excluded from the formal sources of finance.

Financial inclusion has been made an integral part of the banking sector policy in India. Reserve Bank is furthering financial inclusion in a mission mode through a combination of strategies ranging from relaxation of regulatory guidelines, provision of innovative products, encouraging use of technology and other supportive measures for achieving sustainable and scalable financial inclusion. During 2010-11 too, the Reserve Bank continued with policy initiatives aimed at expanding the outreach of banking services to remote parts of the country.

The Reserve Bank and the Government of India have been making efforts to increase banking penetration in the country. Some of these measures include the creation of State Bank of India in 1955; nationalization of commercial banks in 1969 and 1980; initiating the Lead Bank Scheme in 1970; establishing regional rural banks (RRBs) in 1975, introducing a Self-help Group (SHG) - Bank Linkage Programme in 1992 and formulating the Kisan Credit Card scheme in 2001. The government also set up national level institutions like NABARD, SIDBI to empower credit to rural areas and small and medium enterprises.

The Reasons for Financial Exclusion

It has been found that financial services are used only by a section of the population. There is demand for these services but it has not been provided. The excluded regions are rural, poor regions and also those living in un-banked areas where it is difficult to provide these financial services. The excluded population then has to depend on informal sector for availing finance that is usually at very high rates.

High cost: It has also been seen that poor living in urban areas don't utilize the financial services as they find financial services are costly and thus are unaffordable. Hence, even if financial services are available, the high costs deter the poor from accessing them. For example, to open a checking account in Cameroon, the minimum deposit requirement is over 700 dollars, an amount higher than the average GDP per capita of that country, while no minimum amounts are required in South Africa or Swaziland. Annual fees to maintain a checking account exceed 25 percent of GDP per capita in Sierra Leone, while there are no such fees in the Philippines. In Bangladesh, Pakistan, Philippines, to get a small business loan processed requires more than a month, while the wait is only a day in Denmark. The fees for transferring 250 dollars internationally are 50 dollars in the Dominican Republic, but only 30 cents in Belgium.

Documental proof: Access to formal financial services also requires documents of proof regarding a persons' identity, income etc. The poor people do not have these documents and thus are excluded from these services. They may also subscribe to the services initially but may not use them as actively as others because of high distance between the bank and residence, poor infrastructure etc.

Lack of Knowledge: **M**any people are not comfortable using formal financial services. The reasons are difficulty in understanding language, various documents and conditions that come with financial services etc.

Financial Inclusion- Need

It is now widely acknowledged that financial exclusion leads to non-accessibility, non-affordability and non-availability of financial products. Limited access to funds in an underdeveloped financial system restricts the availability of their own funds to individuals and also leads to high cost credit from informal sources such as moneylenders. Due to lack of access to a bank account and remittance facilities, the individual pays higher charges for basic financial transactions. Absence of bank account also leads to security threat and loss of interest by holding cash. All these impose real costs on individuals. Prolonged and persistent deprivation of banking services to a large segment of the population leads to a decline in investment and has the potential to fuel social tensions causing social exclusion. Thus, financial inclusion is an explicit strategy for accelerated economic growth and is considered to be critical for achieving inclusive growth in the country.

Financial inclusion means a group of people should take part in growth activities and help to increase economic growth of the country. We cannot say that financial growth has been achieved by opening a bank account, granting huge loan to a single person and closing the account. First, many people have to open an account in a bank, save money regularly so that loans to needy people may be granted on regular basis. It is a process ensuring easy access and usage of financial system for the rich and poor in the country.

Financial Inclusion - A Statistics

Financial inclusion in developing economies is different than that of developed economies. In latter where inclusion is a minority, in former it could be a majority. Elaine Kempson in his research (2006) showed that in Sweden lower than two per cent of adults did not have an account in 2000 and in Germany, the figure was around three per cent. Another research by (Buckland et al (2005) showed that less than four per cent of adults in Canada and five per cent in Belgium, lacked a bank account. Therefore, it is also mentioned in academia that a better way to analyze financial inclusion in developing economies is to actually see financial exclusion.

Benefits of Financial Inclusion

With the financial inclusion, it is expected that the barrier of acceptance to institutional credit will be removed and credit facility will be available to all at reduced interest (as compared to outside loans). As such two sets of benefits are perceived :

(i) Reduction in the interest cost on loan on account of shift from non-institutional sources of credit to institutional sources.

(ii) Net income from the investments made by those who avail credit afresh.

The Road Map of Financial Inclusion in India

The process of financial inclusion in India can be broadly classified into five phases: Phase-I (1950-70), Phase-II (1970-90), Phase-Ill (1990-2005) , Phase-IV (2005 -2010) and Phase V (2010 onwards)

Phase-I :

1950-70: Consolidation of the Banking sector & Facilitation of Industry and Trade

Phase-II:

1970-90: Focus on channelling of credit to neglected sectors and weaker sections

Phase-Ill:

1990-2005: Focus on strengthening the financial institutions as part of financial sector reforms

Phase-IV:

2005 -2010: Financial Inclusion was explicitly made as a policy objective

Phase – V

2010 on wards all public and private sector banks were advised to put in place a Board-approved three-year Financial Inclusion Plan (FIP) and submit the same to the Reserve Bank by March 2010.

Phases in Process of Financial inclusion (FI)

During the **First Phase** (1950-70), the focus was on the consolidation of the Banking sector and facilitation of industry and trade**. Second Phase** (1970-1990) focused on channeling of credit to the neglected sectors of the economy. Special emphasis was also laid on weaker sections of the society. **Third phase** (1990-2005) focused mainly on strengthening the financial institutions as part of financial sector reforms. Financial inclusion in this phase was encouraged mainly by the introduction of Self- Help Group (SHG)-bank linkage programme in the early 1990s and Kisan Credit Cards (KCCs) for providing credit to farmers. The SHG-bank linkage programme was launched by National Bank for Agriculture and Rural Development. (NABARD) in 1992, with policy support from the Reserve Bank, to facilitate collective decision making by the poor and provide 'door step' banking. During the **Fourth Phase** (2005- 2010), the 'financial inclusion' was explicitly made as a policy objective and thrust was on providing safe facility of savings deposits through 'no frills' accounts. The Eleventh Five Year Plan (2007-12) envisions inclusive growth as a key objective. It clearly stated that 'The development of rural India is an imperative for inclusive and equitable growth and to unlock huge potential of the population that is presently trapped in poverty with its associated deprivations' (GoI, 2007)." During the Fifth Phase (2010 onwards) all public and private sector banks were advised to put in place a Board-approved three- year Financial Inclusion Plan (FIP) and submit the same to the Reserve Bank by March 2010. These banks prepared and submitted their FIPs containing targets for March 2011, 2012 and 2013[1]. These plans broadly include self-determined targets in respect of rural brick and mortar branches to be opened; BCs to be employed; coverage of unbanked villages with population above 2,000 as also other unbanked villages with population below 2,000 through branches/BCs/other modes; no-frill accounts opened including through BC-ICT; Kisan Credit Cards (KCC) and General Credit Cards (GCC) and other specific products designed by them to cater to the financially excluded segments.

Financial Inclusion Practice in India

[1] RBI Trend and Progress 2010 -11 . p 37.

In the Annual Policy for 2005-06 , for the first time the word financial inclusion was used and banks were asked to open “no frills” or a basic banking account to all those desirous of opening a bank account. Several other aspects such as simplified Know Your Customer, OTS for loans up to Rs 25000, offering a General Credit Card /simplified overdrafts etc were also covered. A decentralized approach was advocated through targeting 100% financial inclusion district by district involving the DCC and bank and government officials to facilitate enrolment and identification.

Financial inclusion means a group of people should take part in growth activities and help to increase economic growth of the country. First, many people have to open an account in a bank, save money regularly so that loans to needy people may be granted on regular basis. It is a process ensuring easy access and usage of financial system for the rich and poor in the country.

Financial inclusion has been one of the top priorities of the Reserve Bank during the recent years. Accordingly, the Reserve Bank has been encouraging the banking sector to expand the banking network both through setting up of new branches and also through BC model by leveraging upon the information and communication technology (ICT). As a result of all these efforts the status of financial inclusion improved in 2010-11 over the previous year (Table 1).

Table: 1
Progress of Financial Inclusion

Indicator	2009-10	2010-11
Credit-GDP	53.4	54.6
Credit-Deposit	73.6	76.5
Population per Bank Branch	14,000	13,466
Population per ATM	19,700	16,243
Percentage of Population having deposit accounts	55.8	61.2
Percentage of Population having credit accounts	9.3	9.9
Percentage of Population having debit cards	15.2	18.8
Percentage of Population having credit cards	1.53	1.49
Branches opened in Tier 3-6 centers as a per cent of total new bank branches	40.3	55.4
Branches opened in hitherto unbanked centers as a per cent of total new bank branches	5.6	9.7

Source : RBI Trend and progress 2010-11

To strengthen the financial inclusion drive, the Reserve Bank asked banks to cover all villages with more than 2,000 populations with at least one banking outlet by March 2012. In addition, banks were also encouraged to cover the peripheral villages with population less than 2,000. To facilitate the smooth progress of this plan, all banks were advised to put in place board approved financial inclusion plans (FIPs). Banks have already prepared such plans and the Reserve Bank is closely monitoring the implementation of these plans. The progress made under FIPs is provided in Table 2.

An Outcome of Financial Inclusion Measures In India

As a result of financial inclusion measures in India the outcome are presented in the following table

Table: 2
UPSHOT OF FINANCIAL INCLUSION MEASURES IN INDIA

Particulars	End of March		Progress during April 10- March 11
	2010	2011	
Total Number of Customer Service Points deployed	33,042	58,361	25,319
Total Villages Covered	54,757	99,840	45,083
Villages Covered – with population >2000	27,743	53,397	25,654
Villages Covered – with population <2000	27,014	46,443	19,429
Villages covered through Branches	21,499	22,684	1,185
Villages covered through BCs	33,158	76,801	43,643
Villages covered through other modes (Mobile van and ATM)	100	355	255
Urban Locations covered through BCs	423	3,653	3,230
Number of No-Frill Accounts (in millions)	50	75	25
Amount in No-Frill Accounts (Rs.crore)	4,895	6,566	1,652
Number of No-Frill Accounts with OD (in millions)	.13	4	4
Amount in No Frill A/Cs with OD (Rs.crore)	8	199	190
Number of KCCs outstanding (in millions)	20	23	3
Amount in KCCs outstanding (Rs.crore)	1,07,519	1,43,862	36,343
Number of GCCs outstanding (in millions)	.6	1	.4
Amount in GCCs outstanding (Rs. crore)	814	1,308	494

Source : RBI Trend and progress 2010-11

The total number of villages covered by at least one banking outlet grew at 82 per cent in 2010-11 over the previous year. Importantly, in 2010-11, 47 per cent of the total villages covered under FIPs were villages with population less than 2,000. It can be understood from the table that banks have been heavily relying on BCs to expand the banking network in the unbanked areas under FIPs. In 2010-11, almost 77 per cent of the total villages covered were through BCs. The number of 'no-frills' accounts recorded a growth of 50 per cent in 2010-11 over the previous year. The share of 'no-frills' accounts with overdrafts in the total 'no-frills' accounts improved from 0.3 per cent in 2009-10 to six per cent in 2010-11. The number of Kisan Credit Cards (KCCs) and General Credit Cards (GCCs) witnessed growth of 15 per cent and 49 per cent, respectively in 2010-11 over the previous year (Table 2).

No-Frills Accounts – Banks' Progress

In the Annual Policy of RBI for 2005-06, for the first time the word financial inclusion was used and banks were asked to open "no frills" or a basic banking account to all those desirous of opening a bank account with a view to achieving the objective of greater financial inclusion, all banks are advised to make available a basic banking 'no-frills' account either with 'nil' or very low minimum balances as well as charges that would make such accounts accessible to vast sections of population. The nature and number of transactions in such accounts could be restricted, but made known to the customer in advance in a transparent manner. All banks are advised to give wide publicity to the facility of such 'no-frills' account including in the local media indicating the facilities and charges in a transparent manner. It is evident from the table 3 the category wise and year wise progress of no frills accounts in India it showed that year by year the growth of No-Frills Accounts showed a tremendous increases in all sectors of banks in India specially in public sector as well as private sector banks but in foreign banks operating in India are not in line with others.

Table: 3
NO-FRILLS ACCOUNTS – BANKS' PROGRESS

No. of accounts opened by banks as on:

Category	Mar 31, 2006	Mar 31, 2007	Mar 31, 2008	Mar 31, 2009
Public Sector Banks	332,878	5,865,419	13,925,674	2,98,59,178
Private Sector Banks	156,388	856,495	1,879,073	31,24,101
Foreign banks	231	2,753	33,115	41,482

Source : RBI

At end-March 2010, 50.6 million no-frills accounts were opened by the banking system[2]. As of March 2011, 74.4 million No Frill accounts have been opened by domestic commercial banks with outstanding balance of Rs.6,566 crore. Basic banking No Frill accounts have nil or very low minimum balances as well as charges that make such accounts accessible to vast sections of the population[3].

[2] RBI Trend and Progress 2010 p 93
[3] RBI annual Report 2010- 11 p 85

Conclusion:

Financial Inclusion is the process of providing banking services and financial access at an affordable cost to the vast sections of financially disadvantaged and marginal income group of people. It has gained immense attention across the globe due to its social as well as commercial importance. Savings, remittances, insurance and loans are said to be its four pillars. Financial inclusion will play a major role in driving away poverty from the country. The extent of financial exclusion is staggering. Out of every 1000 persons, only 99 had a credit account and 600 had a deposit account as at end-March 2010. This underlined the need to strengthen the financial inclusion drive through well thought out policies. Banks shall expand financial inclusion initiatives in urban and semi-urban areas by targeting pockets of migrant workers and small vendors and leveraging Aadhaar enrolment for opening bank accounts. In India, a day will come when all the Indians will have bank account and everybody will take part in financial inclusion.

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