Research Paper Management

Financial Inclusion - Performance, Restructuring Financial System and Future Reforms of microfinance – A Panoramic view Inhibitors and Facilitators Rural Bank Managers in Indian scenario

*Akhil Goyal

* Assistant professor, Institute of Management & Computer Science, NIMS University, Jaipur

ABSTRACT

The purpose of this paper is to examine the role of micro finance in the empowerment of people and the realization of financial inclusion and Access to finance by the poor and vulnerable groups is a prerequisite for poverty reduction and social cohesion in India. Financial inclusion program has received utmost priority from the policy makers and has resulted in major policy initiatives in order to reach to the unbanked masses. An understanding of the inhibitors and facilitators of financial inclusion is crucial to meet the financial inclusion objective yet; few studies have investigated into the inhibitors and facilitators of financial inclusion program (FIP). Micro finance in India is still in its nascent. Microfinance yet remains a powerful tool for development. Micro finance refers to small saving, credit and insurance services extended to socially and economically disadvantaged segments of society. The SHG -bank linkage and financial through MFIs approaches is no doubt an effective instrument by which poor can access hassle free formal credit without any collateral security and simultaneously improve their thrift habit. At present a large part of microfinance activity is confined to credit. For development microfinance in India there is a need for sincere intervention by the promotional agencies particularly banks and block authorities in the area of awareness' building, skill development and training with the involvement of formal and informal sectors institutions. In depth structured interview method was used to collect data from the informants. Grounded theory approach was used to explore new themes concerning the inhibitors and facilitators of FIP. Six distinct themes emerged from the data concerning the inhibitors of FIP. The themes emerged were:- (1) perceived non-viability of the FIP for commercial bank; (2) Technical and operational risk; (3) Poor infrastructure to support FIP; (4) trust deficit/loss amongst poor towards bank (5) financially illiterate and ignorant and avoidance of target group (6) inadequate incentive for FIP . Four distinct themes emerged from the data concerning the facilitators of FIP-(1) Bankers positive attitude towards FIP (2) Aggressive policy initiatives by polices.(3)peer pressure/ motivation amongst unbanked (4) successful linkage of social banking to FIP.

Keywords : Financial Inclusion, microfinance, literacy, trust and commercial bank.

Financial inclusion-Conceptual Introduction

Financial inclusion denotes delivery of financial services at an affordable cost to the vast sections of the disadvantaged and low-income groups. The various financial services include credit, savings, insurance and payments and remittance facilities. 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, the attempt must be to lift the poor from one level to another so that they come out of poverty.

Financial Inclusion or inclusive financing is the delivery of financial services at affordable costs to sections of disadvantaged and low income segments of society. Unrestrained access to public goods and services is the sine qua non of an open and efficient society. It is argued that as banking services are in the nature of public good, it is essential that availability of banking and payment services to the entire population without discrimination is the prime objective of public policy. The term "financial inclusion" has gained importance since the early 2000s, and is a result of findings about financial exclusion and its direct correlation to poverty. Financial inclusion is now a common objective for many central banks among the developing nations.

In India, despite the growing recognition among bankers and policy makers regarding the role of Financial Inclusion(FI) for the inclusive growth of the economy, a few studies have investigated into the inhibitor and facilitators of FI . In order to fill the aforementioned gap, this study investigates into the perspective of rural bank mangers towards the inhibitors and facilitators of financial inclusion program. Specific research issues examined are:

(1) What are the inhibitors to the successful implementation of financial inclusion policy?
(2) What are the facilitators for the successful implementation of financial inclusion policy?
(3) What are the possible strategies to reach to the unbanked households?

Financial inclusion in India-

The Reserve Bank of India has set up a commission (Khan Commission) in 2004 to look into financial inclusion and the recommendations of the commission were incorporated into the mid-term review of the policy (2005–06). In the report RBI exhorted the banks with a view of achieving greater financial inclusion to make available a basic "no-frills" banking account. In India, Financial Inclusion first featured in 2005, when it was introduced, that, too, from a pilot project in UT of Pondicherry, by K C Chakraborthy, the chairman of Indian Bank. Mangalam Village became the first village in India where all households were provided banking facilities. In addition to this KYC (Know your Customer) norms were relaxed for people intending to open accounts with annual deposits of less than Rs. 50,000. General Credit Cards (GCC) were issued to the poor and the disadvantaged with a view to help them access easy credit. 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. The bank asked the commercial banks in different regions to start a 100% financial inclusion campaign on a pilot basis. As a result of the campaign states or U.T.s like Pondicherry, Himachal Pradesh and Kerala have announced 100% financial inclusion in all their districts. Reserve Bank of India's vision for 2020 is to open nearly 600 million new customers' accounts and service them through a variety of channels by leveraging on IT. However, illiteracy and the low income savings and lack of bank branches in rural areas continue to be a road block to financial inclusion in many states. Apart from this there are certain in Current model which is followed. There is inadequate legal and financial structure. India, being a mostly agrarian economy, hardly has schemes which lend for agriculture. Along with microfinance we need to focus on Micro insurance too In its platinum jubilee year, the Reserve Bank of India (RBI) wants to connect every Indian to the country s banking system.

RBI is currently working on a three-year financial inclusion plan and is discussing this with each bank to see how to take this forward, KC Chakrabarty, deputy governor, RBI said. "Nearly forty years after nationalization of banks, 60% of the country's population does not have bank accounts and nearly 90% do not get loans," he pointed out .

Despite heightened focus on financial inclusion, Indian banks still somewhat failed to bring the under- and un-banked into the mainstream banking fold.

India has currently the second-highest number of financially excluded households in the world. Approximately, 40% of India s population have bank accounts, and only about 10% have any kind of life insurance cover, while a meager 0.6% have non-life insurance cover.

According to UNITED NATIONS, "A financial sector that provides 'access to credit for all "bankable" people and firms and to savings and payments services for everyone. Inclusive finance does not require that everyone who is eligible use each of the services, but they should be able to choose use them if desired.

REPORT OF THE COMMITTEE ON FINANCIAL INCLUSION IN INDIA (Chairperson: C. Rangarajan) (2008) "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."

As per "TREASURY COMMITTEE, HOUSE OF COMMONS, UK, (2005) "Ability of individuals to access appropriate financial products and services. "

'Major Three Aspects of Financial Inclusion' Make people to Access financial markets

Access credit markets

Learn financial matters (financial education).

Financial Inclusion Includes Accessing Of Financial Products and Services Like-

- Savings facility
- Credit and debit cards access
- Electronic fund transfer
- All kinds of commercial loans
- Overdraft facility
- Cheque facility
- Payment and remittance services
- Low cost financial services
- Insurance (Medical insurance)
- Financial advice
- Pension for old age and investment schemes
- Access to financial markets
- Micro credit during emergency
- Entrepreneurial credit
- Financially Excluded People The financially excluded sections largely comprise Marginal farmers
- Landless labourers
- Oral lessees
- Self employed and unorganized sector enterprises
- Urban slum dwellers
- Migrant.

Inhibitors themes in Financial Inclusion Program (FIP)

Theme		Representative Comments
Theme 1	1) perceived non-viability of the FIP for commercial bank	"No, when only poor people will visit your bank than you will become poorer than them. It is not intelligent business acumen"
Theme 2	Technical and Operational risk	"In rural area we have to do everything on our own, and problem we face is that the customer may refuse that no I have not filled in this voucher. It creates problem for banker"
Theme 3	Poor infrastructure to support FIP	"Overload of work in branches, hence taking time out to do a high labor job is very difficult for the bank officials, and also the branches are sometimes understaffed hence it puts extra pressure to their working…"
Theme 4	trust deficit/loss amongst poor towards bank	"Firstly they get their passbook filled in, then they check how much money they have received by withdrawing the deposit.
Theme 5	financially illiterate and ignorant and avoidance of target group	".People don't know why they are visiting us to open bank account there is a fear also, and thumb impression concept creates suspicion and doubt in the mind of the rural people"
Theme 6	inadequate incentive for FIP	"In the beginning the VLE was happy but after sometimes he was a little apprehensive that how much I will benefit as he was not making much benefit from the services he was offering"

Facilitators of FIP-

Facilitators themes in Financial Inclusion Program (FIP)

Theme		Representative Comments
Theme 1	Bankers positive attitude towards FIP	"I personally believe that it is not viable but the satisfaction which is derived brings in the feeling of social service and I like to help these people who have a lower standard of living"
Theme 2	Aggressive policy initiatives by RBI	"Yes we were fully informed through guideline books….."
Theme 3	Peer pressure/ motivation amongst unbanked household	" if I can guide one or two of them, they will guide others"
Theme 4	Successful linkage of social banking to FIP	"We have been opening NAREGA financial inclusion accounts"

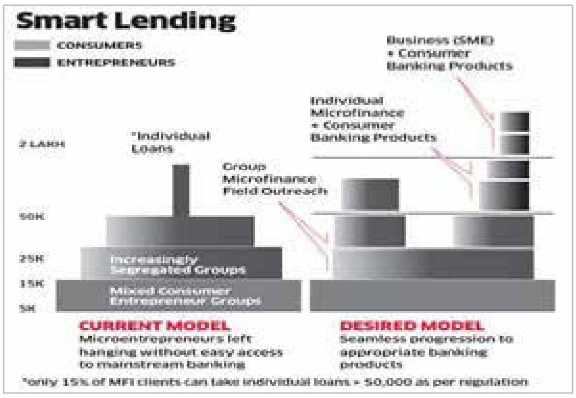
Microfinance: Time to move towards financial inclusion

The numbers that describe India's economy are mindboggling. Just one-tenth of the population participates in the formal economy. Of these, only about 35 million pay taxes. That's less than 3%.No wonder then that our economy produced a GDP of only $1.42 trillion at last count, about the same as that of the city of Tokyo which has a population of 35 million. There are simply too few producing value and wealth in India and so there is not enough to go around.

The financial inclusion agenda so far has been largely focused on redistribution of wealth while what is required is inclusion in the creation of wealth. Financial inclusion so far has meant debt distribution and nofrills bank accounts.

Microfinance has been one major channel of debt distribution to the poor. While the original assumption was that these loans were for investment in micro enterprise, the Malegam committee report in 2010 indicates that 75% of the loans went towards consumption. Contrast this with the distribution of bank debt in India where less than 20% were consumer loans.

Debt on its own does not grow economies. This begs the question: what kind of financial inclusion agenda can enable participation of the greater population in the economy as wealth creators? When the wealth and therefore total credit in the system is limited - and it is - it is most effective when it can be directed towards innovation and productive output



Money is a catalyst of progress but only when placed in the context of the right reaction. In the informal sector this means directing it towards the genuine microentrepreneur , not just any self-employed person. Here's why: in developed countries only 6-7 % of employed adults are entrepreneurs compared to developing countries like India where it is between 30% and 45%.

Developed economies are characterized by larger enterprises that take advantage of division of labour, specialization and economies of scale. These synergies allow each participating individual to create more wealth such that revenues and even income per employee are far greater than what a comparable micro enterprise can achieve. The current model of microfinance lending focuses largely on two aspects: reducing the cost of lending and ensuring responsible repayment by using a group lending model with a peer pressure element.

Unlike the formal economy where businesses are registered and documented, there are no records in the cash economy that can be used to evaluate business intent, asset ownership or track record. Consequently, the microfinance strategy has been to cast a wide net treating every borrower virtually the same. Those who are more successful are constrained in their access to credit by the lesser needs of the group.

Furthermore, regulation caps their access to credit at Rs 50,000 with no easy passage into mainstream banking products. Microfinance lending in India is directed almost entirely at women. This has its benefits in empowering women in the management of household finances. In many parts of India men are thought to squander money more readily on vices while women tend to spend more responsibly for the family.

On the other hand, while some women are genuine entrepreneurs , many more of the entrepreneurs with the ability to scale are men. This is for the simple reason that historically and culturally men tend to have higher mobility and therefore access to markets. They should not be excluded. Mature microfinance clients represent a pool of creditworthy customers who could transition into the banking system. However there is no mechanism for such a transition.

MFIs, while having no incentive to pass them along to the bank, also cannot offer them expanded credit. This can only be remedied if there is a progression of products for the micro entrepreneur from a microfinance group loan to individual business loans that expand to meet their growth needs. This is best done if there is a close relationship between banks and MFIs where there is a sharing of customer credit history and profile data.

Banks might set up or acquire as subsidiaries MFIs that operate as lower cost, outreach operations, sifting out the entrepreneurs from the consumers. The microfinance model itself needs to become more effective at identifying micro entrepreneurs and micro enterprise risk. This could be done with approaches that understand the psychometric and behavioral profiles of entrepreneurs. It is when the potential of entrepreneurship among the other 1.1 billion is unlocked that the rest of the country can be productively engaged and therefore financially included.

Govt may introduce Micro-finance Bill in Budget Session-
The government is likely to introduce a Bill that seeks to make it mandatory for all micro-finance institutions to be registered with the Reserve Bank of India in the Budget Session of Parliament.

The Finance Ministry has sent the draft Bill to the Law Ministry for approval and will subsequently seek Cabinet's nod, official sources said.

The ministry hopes to table the Bill in the upcoming Budget Session of Parliament, sources said. The Budget Session is expected to commence in mid-March.

The draft Micro Financial Sector (Development and Regulation) Bill, 2011, circulated for public comments in July last year had proposed that the RBI will be regulator for the sector.

In an earlier Bill, it was proposed that the National Bank for Agriculture and Rural Development (Nabard) would be the regulator of the sector.

The government introduced the Micro Financial Sector Bill in the Lok Sabha in March, 2007. However, the Bill lapsed when the term of the 14th Lok Sabha expired in 2009. The latest draft Bill proposes to make it mandatory for micro-finance institutions to be registered with the Reserve Bank and have minimum net-owned funds of Rs 5 lakh. In addition, a Micro-Finance Development Council will be set up to advice the government on formulation of policies, schemes and other measures required in the interest of orderly growth and development of the sector and microfinance institutions with a view to promote financial inclusion. The council will comprise members not below the rank of Executive Director from NABARD, National Housing Bank, the RBI and SIDBI. In addition, joint secretaries from the Ministry of Finance and the Ministry of Rural Development will also be its members.

The draft Bill also proposes that any micro-finance institution which is not a company registered under the Companies Act, 1956, and which becomes a systemically important microfinance institution shall convert its institution into a company registered under the Companies Act, 1956, with or without a licence, under Section 25 of the Act.

This should happen within six months from the date of the balance sheet that shows the MFI has become a systematically important micro-finance institution in terms of the rules prescribed by the central government, the draft Bill said.

The RBI may pass an order directing a micro-finance institution to cease and desist from carrying out micro-finance activities if it is found acting in manner prejudicial to the interest of its clients or depositors.The Reserve Bank will cancel the certificate of registration granted to a micro-finance institution if it fails to comply with the directives or conditions, the draft Bill states

Conclusion
The Indian economy at present is at a crucial juncture, on one hand, the optimists are talking of India being among

the top 5 economies of the world by 2050 andon the other is the presence of 260 million poor forming 26 % of the total population. The enormity of the task can be gauged from the above numbers and if India is to stand among the comity of developed nations, there is no denying the fact that poverty alleviation & reduction of income inequalities has to be the top most priority. India's achievement of the MDG of halving the population of poor by 2015 as well as achieving a broad based economic growth also hinges on a successful poverty alleviation strategy.

The paper argues for mainstreaming of impact assessment and incorporation of local factors in service delivery to maximize impact of SHG –Bank linkage programmed on achievement of MDGs and not letting go this opportunity. As in any other sunrise sector, microfinance companies are regarded with some awe, but that awe is definitely mixed with apprehension. Sector participants should invest more time with other stakeholders (government, media, people at large), educating them about the microfinance business, the Benefits it brings, the need for private capital, and (all-important this context),

Based on the findings of the study, three major research directions emerge is:-

(1) How to increase the level of financial literacy amongst poor in an affordable manner?
(2) How to overcome the problem of trust deficit amongst unbanked customer towards commercial banks?
(3) How to promote FIP in an affordable manner? Further, future research targeted to model the inhibitors and facilitators of financial inclusion program and its impact on the financial well being of the unbanked customer would be invaluable, as well as studies which incorporate data collection to permit empirically validating of the model will further validate the findings of the study.

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