Research Paper Commerce

Financial Inclusion in India-a Retrospective

Biju John, M. Associate Professor Dept. of Commerce and Management Studies St.Thomas' College Thrissur – Kerala.

Dr. Mary Joseph, T. Former Director School of Management Studies Cochin University of Science and Technology

ABSTRACT

India has been striving to grow at a faster pace during the recent years and the economic growth to be sustainable, it requires all sections of the society included and participating in the growth process. Financial inclusion is one of the methods through which Inclusive Growth can be achieved in India where large sections are unable or incompetent to participate in the Financial System. Agriculture sector continues to be an important segment of the our economy with more than 50% of the country's population depending on it for a living and contributing 14% share in the Gross Domestic Product. Moreover it provides employment to nearly1/3 rd of the work force in the country. Small and Marginal farmers constitute 80% of the farmers in India. A large segment of the small and marginal farmers still continue to be deprived of the formal sources of credit and other essential financial services like insurance, savings and payment services. Commercial banks being the purveyor's of nation's credit has got a great deal of responsibility in extending the financial services to this sector in order to provide the fruits of economic development to this segment of Indian economy. Hence an attempt is made to assess the nature of inclusive financing from the supply side and to identify the nature and extent of availability and use of financial services and issues in inclusive financing particularly that of the small and marginal farmers.

KEYWORDS Financial inclusion, Agriculture sector, Commercial banks, economic growth

Introduction

Our nation was able to grow at a faster rate during the past decade among the growing economies of the world attracting lot of international attention. But this higher economic growth is more confined to some affluent sections and failed to take care of the well being of the large number of deprived and marginalized sections due to various structural rigidities. Moreover economic growth to be sustainable, it requires all sections of the society included and participating in the growth process. Financial inclusion is one of the methods through which Inclusive Growth can be achieved in India where large sections are unable or incompetent to participate in the Financial System. Also financial inclusion is inevitable in creating economic opportunities to the poor, sustaining it, overcome the risk associated with it and continue to participate so that they become successful economic agents to the growth process of the country. Keeping this in mind Government, RBI, banks and other financial institutions are making policy interventions to accommodate the vulnerable in to the financial system.

Need for Financial Access

Financial access is gradually being recognized as an important input to economic development. Finance and its access, to enable individuals to do what they desire to do, is gradually being recognized as a significant aspect of economic development and also been suggested as a tool for achieving the different Millennium Development Goals (Claessens and Feijen 2007). Access to finance can be defined as "availability of a supply of reasonable quality of financial services at reasonable costs, where reasonable quality and reasonable cost have to be defined relative to some objective standard, with costs reflecting all pecuniary and non pecuniary costs" (Claessens 2006). It can also be defined as the "absence of price and non-price barriers"(Demirguc - Kunt and Levine 2008). Access to finance and resources in India has always been skewed in favour of the affluent and this does not happen just in the process of development but through a sinister design perpetuated through irrational social order. Low access to financial resources leads to increased income inequalities, poverty, and low growth rates. Access to finance and inclusive financial system which includes all groups of people, poor and middle class as well, has been advocated to reduce inequalities and poverty in developing countries(World Bank 2008). Beck, Demiurgic - Kunt et al. (2009) observed that, "without inclusive financial systems, poor individuals and small enterprises need to rely on their personal wealth or resources to invest in their education, become entrepreneurs, or take advantage of promising growth opportunities" .In more recent years the debate expanded to include the notion of financial "exclusion" as a barrier to economic development and the need to build inclusive financial systems (Beck et al., 2008) . Recent empirical evidence using household data indicates that access to basic financial services such as savings, payments and credit can make a substantial positive difference in improving poor people's lives (Dupas and Robinson 2009).

Financial Inclusion

Access to Finance by the poor and vulnerable groups is a prerequisite for poverty reduction and an integral part of our effort to promote inclusive growth. 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 include within its ambit people with low incomes. Further, access to finance will empower the vulnerable groups by giving them an opportunity to have a bank account, to save and invest, to insure their homes or to partake of credit, thereby facilitating them to break the chain of poverty. The banking industry in India has recognized this imperative and has undergone certain fundamental changes over the last two decades. Reforms since the early nineties in the banking sector have facilitated increasing competition, the development of new generation private sector banks as well as technological breakthrough in diverse financial products, services and delivery channels. With the recent development in technology, both delivery channel and access to financial services have transformed banking from the traditional style to a system supplemented by other channels like Automated Teller Machines (ATM), Credit/Debit cards, Internet banking, Online money transfer etc. The irony, however, is that access to such technology is restricted only to certain segments of the society. There is a growing divide, with an increased range of personal finance options for a segment of high and upper middle income population and a significantly large section of the population who lack access to even the most basic banking services.

Financial Inclusion – Definition

By Financial Inclusion, we mean delivery of banking services and credit at an affordable cost to the vast sections of disadvantaged and low Income groups. Report of the committee on financial inclusion headed by Dr. C Rangarajan defines financial inclusion as 'the process of ensuring access to financial service and timely and adequate credit where needed by vulnerable groups such as weaker sections and low income groups at an affordable cost. Financial services in this context include the provision of savings, loans, insurance, payments and remittance facilities by the formal financial system to those who tend to be excluded.

In India, while the use of the term financial inclusion in above context may be of recent origin, the effort to bring poor under the fold of formal credit system have been going on since nationalization or even earlier. Deliberate policies of central government and RBI for opening of one of the biggest branch network in rural and semi urban areas has been a major step towards financial inclusion. Various poverty alleviation programmes with credit support from the banks have contributed substantially in this direction, despite many shortcomings.

Literature review

A survey of the existing literature on 'Financial Inclusion' was done for this work. Some of the prominent studies relating to financial access, availability, use and financial inclusion are reviewed as follows:

Allen et al (2012) reports that greater ownership and use of accounts is associated with a better enabling environment for accessing financial services, such as lower account costs and greater proximity to financial intermediaries. Policies targeted to promote inclusion such as requiring banks to offer basic or low-fee accounts, exempting some depositors from onerous documentation requirements, allowing correspondent banking, and using bank accounts to make government payments may be especially effective among those most likely to be excluded. They suggests that policies to reduce barriers to financial inclusion may expand the pool of eligible account users and encourage existing account holders to use their accounts with greater frequency and for the purpose of saving. Dr. K.C. Chakrabarty (2006) has observed that financial inclusion needs to be done in quickest possible time. With maximum outreach in a cost effective manner through appropriate technological and business delivery interventions and by providing adequate linkage and infrastructure with effective participation by all the stake holders. Dr. N.A. Mujamdar (2006) has reported that it may be possible for banks to reach by themselves to all the segments may have to utilize some institutions as intermediaries. Inclusive growth in the real sector would seem to depend, to considerable extent, on the success with which the rural credit delivery system extends its support to the process. R. Bhaskaran (2006) has concluded in his study that banks should be proactive such that poor can terms what the poor needed, given their meager and compulsory requirements. Financial inclusion will happen if loan products are structural with flexibility in delivery and affordable rates of interest. V. Leeladhar (2006) in his study has reported that banks need to redesign their business strategies to incorporate specific plans to promote financial inclusion of low income group treating it both a business opportunity as well as a corporate social responsibility. It may appear in the first instance that taking banking to the section constituting "the bottom of the pyramid", may not be profitable but it should always be remembered that even the relatively low margins on high volumes can be a very profitable proposition. Y.S.P. Thorat (2006) in his report on 'Rural Credit In India: Issues and Concerns' has observed that the financial health of commercial banks has improved in terms of parameters such as capital adequacy, non performing loan and return on assets consistent with International Standards for classification of advances and prudential norms being applied in almost all the areas. However, commercial banks being more focused on profitability tend to cherry pick and give comparatively less priority to marginal and sub marginal farmers.

Scope and Significance of the study

Agriculture sector continues to be an important segment of the economy with more than 50% of the country's population depending on it for a living and contributing 14% share in the Gross Domestic Product. Moreover it provides employment to nearly1/3 rd of the work force in the country. Small and Marginal farmers constitute 80% of the farmers in India. A large segment of the small and marginal farmers still continue to be deprived of the formal sources of credit and other essential financial services like insurance, savings and payment services. Commercial banks being the purveyor's of nation's credit has got a great deal of responsibility in extending the financial services to this sector in order to provide the fruits of economic development to this segment of Indian economy. This paper is an attempt made to assess the nature of inclusive financing from the supply side and to identify the nature and extent of availability and use of financial services and issues in inclusive financing particularly that of the small and marginal farmers.

Objectives of the Study

The specific objectives with which this study deals with are the following.

- To examine the extent of availability and access of financial services provided by commercial banks.
- To identify the major constraints faced by the borrowers in the access of financial services.

Financial Inclusion in India-Role of Commercial Banks

The role of banks as a catalyst of social development has been articulated by eminent economists of the past and present. Apart from acting as financial intermediaries and facilitators of rapid economic growth banks were also expected to ensure social justice by providing cheap credit to the disadvantaged and other weaker sections of the society. Banking sector reforms initiated in this country as a measured, gradual, continuous and steady process provided for achievements like improvement in the financial health of banks, improved asset quality, reduction in interest spread, improvement in profitability and so on with its direct positive effect on aggregate welfare.

India has a long history of working to expand Financial Inclusion. Since the reforms in the financial sector initiated in our country about two decades ago, tremendous changes are taking place in the banking sector. 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. The Indian Banking Industry today is quite robust and strong to be able to take on the challenges of achieving greater financial inclusion.

Financial Inclusion: The Present Scenario

The global financial crisis has brought the need for financial inclusion into greater focus worldwide as it is believed that widespread incidence of financial exclusion was one of the factors that precipitated the financial crisis. Out of the roughly 600,000 habitations in the country, only about 5% have a commercial bank branch. India has the highest number of households (145 million) excluded from banking and there is a low ratio of one bank branch per 16,000 people. The number of branches per lakh of population was 6.33 as of March 2010 in India as compared to 25-45 for developed countries. Only 13% of our population has debit cards and only 2% has credit cards.

Table: 1 Financial Inclusion in India –An Overview

Population particulars	Percentage
Habitations in the country with a commercial bank branch	5% (30,000 out of 600000)
Bank accounts (savings)	57%
Life insurance	10%
Non-life insurance	0.6%
Debit cards	13%
Credit cards	2%

Source: Reserve Bank of India Bulletin, April 2011

Table 1 provides a set of summary statistics relating to the penetration of various categories of financial products. First, the relatively low penetration of bank branches must be highlighted - only 30,000 out of 6, 00,000 habitations have a banking presence. The other statistics in Table 1 provide some indication of the size of the opportunity. However, the statistics presented suggest that, apart from savings accounts, which have about 57 per cent penetration, there are several other financial products that might meet existing consumer requirements, such as insurance, which have very low penetration. Similarly, debit cards, which facilitate the use of technology, thereby reducing the dependence of bank customers on physical branches, may help to significantly expand the capacity of the banking network without necessarily setting up more branches.

Table 2 Geographical Spread of Bank Branches as on 31-March 2013

Bank Group	Rural	Semi-urban	Urban	Metropolitan	Total
Public Sector Banks	23286	18854	14649	13632	70421
Private Sector Banks	1937	5128	3722	3797	14584
Foreign Banks	8	9	65	249	331
Regional Rural Banks	12722	3228	891	166	17007
Total	37953 (37.08)	27219 (26.59)	19327 (18.88)	17844 (17.43)	102343 (100)

Source: Reserve Bank of India Annual Reports Various Years.

Table 2 reveals the geographical spread of the commercial bank branches as on 31st March 2013.The total commercial bank branches has surpassed the figure of one lakhs as during the period. Public sector banks lead the tally with more than seventy thousand commercial bank branches. Out of all commercial bank branches only 37.08 % of branches are located in rural areas. Among the public sector bank branches, 33.06% are located in rural areas whereas in the case of private sector banks only 13.28% of the branches are located in rural areas. Even in the case of regional rural banks almost one fourth of the branches are not located in rural areas.

Table: 3 Bank-wise credit disbursed to Agriculture (Rupees in crores)

Year / Bank	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12
Cooperative	42480	48258	46192	63497	78121	87963
Share (%)	18.52	18.95	15.30	16.51	16.68	17.21
RRBs	20435	25312	26765	35218	44293	54450
Share (%)	8.91	9.94	8.87	9.16	9.46	10.65
Commercial	166485	181088	228951	285799	345877	368616
Share (%)	72.57	71.11	75.83	74.33	73.86	72.13
Total (1+2+3)	229400	254658	301908	384514	468291	511029
Source: Commercial bank data-IBA, Reserve Bank of India						

Table 3 depicts that bank credit to agriculture which has a 13.7 percentage share in GDP and the mainstay for more than one half of the nation's population during the past years reveals that the commercial banks are consistently maintaining their share of more than seventy percentage in the banking sector .

Table: 4
Number of ATMs in the country as on 31st March

Year ending 31st March	Rural	Semi-Urban	Urban	Metropolitan	Total
2011	7316 (9.33)	19149 (24.44)	25704 (32.79)	26217 (33.44)	78386 (100)
2012	8639 (9.02)	22677 (23.69)	31006 (32.40)	33364 (34.86)	95686 (100)
2013	11564 (10.14)	27710 (24.30)	36111 (31.67)	38629 (33.88)	114014 (100)

Source: Commercial bank data-IBA, Reserve Bank of India

The spread of the number of ATMs in the country as shown in table 4 reveals that only one tenth of them are located in rural areas .Moreover during the past three year period there is not much improvement in this situation. However it is worth noting that the total number of ATMs in the country surpassed the total number of commercial bank branches in the nation during the year 2013.

Financial Inclusion Plan - Summary progress of all banks including RRBs

In January 2010, the Reserve Bank advised all public and private sector banks to submit a three-year Financial Inclusion Plan (FIP) starting in April 2010. They were advised to devise FIPs congruent with their business strategy and comparative advantage and to make FIPs integral part of their corporate plans. The implementation of these plans was closely monitored by the Reserve Bank on a monthly basis through a quantitative reporting format. The qualitative aspects of the FIPs were monitored through a qualitative report submitted by banks every quarter. A snapshot of the progress made by banks under the 3-year FIP (April 2010-March 2013) on key parameters is given below:

Table: 5 Banking Outreach In Villages

Particulars	Year ended Mar 2010	Year ended Mar 2011	Year ended Mar 2012	Year ended March 2013	Progress April 2010 -March 2013
Banking Outlets in Villages - Branches	33,378	34,811	37,471	40,837	6 7,459
Banking Outlets in Villages - BCs	34,174	80,802	1,41,136	2,21,341	1,87,167
Urban Locations covered through BCs	447	3,771	5,891	27,143	26,696
Banking Outlets in Villages -TOTAL	67,694	1,16,208	1,81,753	2,68,454	2,00,760

Source: Reserve Bank of India, Trend and Progress of Banking in India, Various Issues

The above table 5 shows that the total banking outlets in villages have increased to nearly 2,68,000 from 67,694 outlets in March 2010.The data reveals that there has been considerable improvement in the operation of Business Correspondents and during the three year period their performance has multiplied almost six times in villages.

Table: 6
Basic Savings Bank Deposit Accounts: Progress during the F I P Period 2010-2013

Particulars	Year ended Mar 2010	Year ended Mar 2011	Year ended Mar 2012	Year ended March 2013
BSBDA through branches (No. in millions)	60.19	73.13	81.20	100.80
BSBDA through branches Amt. in Rs.billions)	44.33	57.89	109.87	164.69
BSBDA through BCs (No. in millions)	13.27	31.63	57.30	81.27
BSBDA through BCs (Amt. in ` billions)	10.69	18.23	10.54	18.22
BSBDA Total (No. in millions)	73.45	104.76	138.50	182.06
BSBDA Total (Amt. in ` billions)	55.02	76.12	120.41	182.92
OD in BSBDA (No. in millions)	0.18	0.61	2.71	3.95

Source: Reserve Bank of India, Trend and Progress of Banking in India, Various Issues

The Reserve Bank of India directed banks to offer a Basic Savings Bank Deposit Account (BSBDA) that will offer the following a variety of facilities to such as ATMs,no minimum balance, electronic transactions, no levy for non-operative accounts ,etc. and the existing 'no-frills' accounts should be converted to BSBDA.Table 6 highlights that 109 million Basic Savings Bank Deposit Accounts (BSBDAs) have been added, taking the total number of BSBDA to 182 million. Basic savings bank deposit accounts opened through business correspondents shows a remarkable fivefold increase during the period. But, regarding the banking transactions through basic savings bank deposit accounts opened through business correspondents is not showing encouraging progress. The figures show it has increased only less than two times during the period.

Moreover the Progress of KCCs, GCCs and ICT- based BC Transactions reveals that there has been considerable progress in the issuance of KCCs, GCCs and ICT- based BC. About 490 million transactions have been carried out in ICT-based accounts through BCs during the three-year period Although there has been reasonable progress in the penetration of banking services and opening of basic bank accounts, the number of transactions through ICT-based BC outlets is still considered very low. To continue the process of ensuring access to banking services to the excluded, banks have been advised to draw up a 3year FIP for the period 2013-16.

Survey Findings
In order to assess the extent of financial inclusion and to understand the challenges in ensuring inclusive finance, a survey was conducted among one hundred small and marginal farmers in Thrissur district. Besides its cultural background, Thrissur is mainly an agricultural district and the predominance of small and marginal land holdings is seen in the district with progressive fragmented pattern of land holdings. Agriculture continues to be the main economic activity of the district. More than half of the income is generated from agriculture and Allied activities and 55% of the workers are having full time employment in this important sector. 74 percentage of land holding are with the small and marginal farmers. Whereas, almost an overwhelming 98.8 percentage of the farmers belong to this category. Large farmers who comprises of only a small fraction of 0.04 percentage holds 8% of the total operational holdings. The one hundred samples selected consisted of 86 marginal and 14 small farmers.

The average family size of marginal farmers was bigger than small farmer's .Regarding the educational status there are no illiterates among both the category of samples. Those with higher secondary education are more in both the cases of respondents. Majority of the marginal farmers engage in non - farm work (62.79) to supplement their agricultural income. It is noteworthy that the larger percentage of the both the categories of farmer households are having other main sources of livelihood than agriculture with only 42.8% of small farmers and 32.55% of marginal farmers depending mainly on agriculture.

Usage of savings account is more prevalent among the small farmers than the marginal farmers. Even 10 marginal farmers reported not to have a SB account.59% of small and marginal farmers has availed formal sources of credit. A significant portion of small farmers (78.5) availed formal credit compared to only 55.8% in the case of marginal farmers. Similarly formal savings is also much more prevalent among small farmers (85.7) when compared to 37.2% in the case of marginal farmers. Dependence on informal money lenders for credit was high in the case of marginal farmers. It was 87.2% and 57.1% in the case of marginal farmers and small farmers respectively. Moreover 38% of households have availed both formal and informal sources of credit. Half of the households belonging to the small and marginal farmers use ATM cards with an ATM usage of 85.7 % in the case of small farmers. Furthermore hardly any of the marginal farmers uses a credit card and it is prevalent in only 14.25% of the respondents belonging to the small farmer category.

Only less than one-third among the small and marginal farmers availed life and health insurance. However micro insurance facility was utilized by more than half (54%) of the respondents. Micro insurance coverage was more prevalent among marginal farmer category as this is often provided along with agricultural loans. Life and health are reported to be major risks among the small and marginal farmers. Past debts, Education expenses, Crop failure and employment loss occupies the subsequent positions respectively. Ignorance of insurance is the major constraint in having insurance. A major portion of the marginal farmer respondents (75.6%) were unaware of the various aspects of insurance facilities available.70% of the total samples reported that they are ignorant about the benefits of being insured. High level of premium and improper product design are the other major challenges in availing insurance.

Conclusion

The agenda of financial inclusion has been given top priority by the Government of India and the Reserve Bank of India with a more focused and structured approach. In recent times some of the efforts of the banking sector are beginning to show the first signs of success. Financial inclusion is, therefore, already happening in pockets across the country, and needs to be expedited along the length and breadth of the country. RBI's relentless recent efforts in this direction is beginning to work and one can see that the move to achieve 100% financial inclusion in Phase I of the financial inclusion plan is beginning to gain momentum with each passing month. RBI and GOI are very closely monitoring the progress of implementation of the FIPs of commercial banks and are encouraging them to achieve what once seemed to be a gigantic task in a vast country like India. Even though banks are commercial entities, they must not lose sight of the fact that being purveyors of nation's credit, they have a great corporate social responsibility for inclusive growth. In this scenario, the commercial banks must identify the huge business potential and opportunities available by serving a large proportion of masses even at low margins. The various challenges and issues with regard to financial inclusion in India have to be converted into opportunities by the banking sector for the development and prosperity of our nation. In the light of the above, it may be concluded that the banking sector being the nation's flagship vehicle must initiate further innovations in their collective efforts with the regulators, NGO's and financial intermediaries in the march to achieve comprehensive and sustainable inclusive growth.

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