State of Financial Inclusion in India: A Retrospective Review

Akash Kumar Arya*
Swastika Tripathi**

ABSTRACT

As we know that financial inclusion is responsible for the inclusive growth of any nation and there are many more studies and researches have done in the field of financial inclusion.

Rangarajan committee, NachiketMor committee and various scholars like K C Chakraborty etc. propounded a large contribution towards the domain of financial inclusion. Various factors responsible for financial exclusion are pointed out by these experts. As it is a known fact that finance is the life blood for the survival and development of the economy as well as community. Financial Inclusion or inclusive financing is the effort to provide low-cost banking and financial services to the disadvantaged people of the economy. In current scenario financial inclusion is proved to be an effective tool for the government to boost up the growth of India and GDP as well.

Financial inclusion means delivering (at least the basic and core) financial services to those who have no access to these services, at an affordable cost and on timely basis.

Researcher jots down a retrospective view of financial inclusion in this paper. The researcher highlights the major tools and approaches of RBI to accelerate the growth of Indian economy through financial inclusion. Concept of financial tripod is also a highlight of the paper.

Key Words: *Financial Inclusion, Financial Exclusion, Financial Stability, Financial Tripod.*

INTRODUCTION

Finance is known as the life blood for the survival of an economy and it is an essential element of an economy for the development of community and the economy as a whole. The sustainable development of any economy could be achieved by the inclusive growth and inclusive growth is a result of financial inclusion. Financial Inclusion or inclusive financing is the effort to provide low-cost banking and financial services to the disadvantaged people of the economy. Being the second largest economy in the world India has a large number of working (employed) persons having no access to financial services which are delivered by the various financial institutions.

Financial inclusion means delivering (at least the basic and core) financial services to those who have no access to these services, at an affordable cost and on timely basis.

**Ph. D. Scholar, School of Business Management, IFTM University, Moradabad, Uttar Pradesh*
*** Ph.D. Commerce, Supervisor*

Financial Inclusion is the effort to provide low-cost banking and financial services to the disadvantaged people of the economy. Being the second largest economy in the world India has a large number of working (employed) persons having no access to financial services which are delivered by the various financial institutions.

Financial Inclusion could be defined as the process of providing access to financial products and services to all the needed sections of the society in general and also to the vulnerable groups (also called as disadvantaged people) such as low income population and weaker sections in particular, and also provide these services at an affordable cost in a transparent and fair manner by responsible and mainstream institutional players, such as GOI and RBI in India.

For a layman, the basic concept of financial inclusion is having only bank account but in reality it includes several other services such as bank loans, insurance services, remittance services etc.

Though India had achieved 7-8 % of GDP growth, yet as per International Poverty line, half of the population lives below poverty line. This economic growth is representing half of the Nation Population. Imagine the Economic Success, if the other half is brought above the poverty line! This could only happen with Financial Inclusion. To achieve the goal of Financial Inclusion, RBI has adopted various strategies like Branch Banking, Business Correspondences etc. To bridge the Gap in achieving financial inclusion the major efforts should be on Consumer protection and Consumer literacy.

As per the progress record, the emphasis has been on both Financial Inclusion,explained as the widen financial institutions and financial services crosswise the country to the weak group of society and Financial Depth,distinct as the percentage of credit to GDP at various levels of the economy, But the wide-ranging situation remain disgraceful on a regional and sectorial basis, rather non-satisfactory. A study suggest that approximate 90 % of small and medium businesses have no access to formal financial services and nearby 60 % of the population in India do not have a functional bank account. Either their accounts are dormant or have been closed due to any reason. This means if the population needs credit, it has to depend on the informal sector for lending money or avail any other service. On the savings front, difficulties of access combined with an absence of a positive real return on financial savings, has accelerated the move away from financial assets to physical assets and unregulated providers. Savings as a proportion to GDP has fallen from 36.8 per cent in 2007-08 to 30.8 per cent in 2011-12 and the financial savings of households have declined from 11.6 per cent of GDP to 8 per cent during the same period(RBI's June 2013,Financial Stability Report). From this there is clear indication of demand of Compatible Formal Financial Services by small businesses and household sector combined with an eagerness to pay for them. The challenge is to get compatible with the formal financial system to build up a strong supply response which needs to be strengthened visibly.

The Nachiket Mor Committee on Financial Inclusion has focused its attention on framing a clear vision and design principles with comprehensive monitoring framework to track the progress of Financial Inclusion and Financial deepening in India.

OBJECTIVES OF THE STUDY

1. To study financial inclusion and its importance.
2. To find out various phases of financial inclusion.
3. To study the state of financial inclusion and the current status of financial inclusion in India.
4. To analyse the three pillars of financial inclusion in Indian economy.

RESEARCH METHODOLOGY

The research methodology is descriptive analytical in nature. For this study the data has been collected through books, Newspapers, Research Articles, Research Journals, Articles of RBI, reports of Ministry of Corporate Affairs etc.

FINANCIAL INCLUSION

There are several factors that affect access to formal banking system in any country. They include culture, financial literacy, gender income and assets, proof of identity and so on. The RBI has taken several measures since Independence to improve access to affordable financial services through financial education, leveraging technology and generating awareness.

Financial inclusion aims to promote the sustainable development in the economy and also to generate employment opportunities in the nation (especially for the rural population). The latest NSSO survey report reveals that more than 80 million people are categorized as disadvantaged person in India due to no access to basic financial services such as having a bank account, credit payment and remittance services. As far as the first Index of Financial Inclusion is concerned (to find out the extent of reach of financial services) among 100 countries, India ranked 50. There is a long journey to become financial inclusive economy for India. Most of the BPL families and low income group do not have access to financial services due to many reasons such as no formal document available with them, lack of knowledge, and dependency on informal money lending system etc. since these disadvantaged persons depend on the informal system for their credit and saving requirements, they are treated as financially excluded. Thus, to obtain sustainable development and inclusive growth, these financially excluded persons has to be brought within the ambit of financial services.

In present scenario, financial inclusion plays a critical role for the inclusive growth of the Indian economy. This concept is not new one in Indian economy. After the nationalization of banks in 1969, RRBs have been established and SGH-bank linkage programs were started by the RBI to spread the financial accessibility to the disadvantaged and unbanked population.

The basic objective of financial inclusion is to gain access for the disadvantaged people to the full domain of financial services at the reasonable cost.

In other words financial inclusion includes attaching the weaker section of the society with the financial (banking) services at a lower cost. These services include opening a bank account at low MAV (Monthly Average Value) and QAV (Quarterly Average Value), and to enlarge the investment safely and continually.

All the efforts of government, like PradhanMantri Jan DhanYojana etc., aimed at to enlarge the investment of the general public and to raise the revenue of government.

So the financial inclusion results in the contribution of economic growth and economic development.

PradhanMantri Jan DhanYojana is known as a milestone to achieve a stage of financially inclusive economy. This scheme is launched with a view to provide minimum 75 billion bank accounts to the weaker and disadvantaged people of the economy, in the financial year 2014-15.

In addition to this scheme, Reserve bank of India had introduced various services like providing no-frills account, providing relaxation in the KYC (know your customer) norms, and opening bank branches in those areas which are categorised as unbanked rural centres. Here the term no-frills account means providing a bank account without attaching any other supplementary services or charging extra charges for those. So the core bank account is known as no-frills account.

From time to time RBI introduces various measures to balances the growth of economy with the help of various money measurement tools. But various studies show that these tools attract only urban population. In order to cover the rural and disadvantaged population, some other attractive tools are necessary which provides basic banking services to them and also the supplementary services at a lower cost.

Report of the Committee on Financial Inclusion in India (Chairperson C.Rangarajan) (2008) defines Financial Inclusion as "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." The Report of the committee on financial inclusion headed has observed that financial inclusion must be taken up in a mission mode and suggested a National Mission on Financial Inclusion (NMFI) comprising representation of all stakeholders for suggesting the overall policy changes required, and supporting the stakeholders in the domain of public, private and NGO sectors in undertaking promotional initiatives.

Nationalization of Banks in India proves a landmark in the achievement of financial inclusion, as it was intended to transfer the focus from individual class banking to the mass banking system.

The importance and usage for creating Regional Rural Banks was also to bring the banking services to untouched poor people. The importance of a financially inclusive system has an important role in the formulation of policiesand most recently financial inclusion has become a policy priority in many countries. Various initiatives have come from the policy regulators (like the governments and the banking industry) for financial inclusion. Legislative measures have been initiated in some countries.

By financial inclusion we mean the provision of affordable financial services, viz., and access to payments, 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.

Financial inclusion termed as delivering banking and financial services at the less cost to weak group of society and to tap unbanked area with the objectives of in calculating habits of saving among vulnerable group, to endow with formal credit facilities and to plug the gaps and leakages in public subsidies & welfare programs to weaker sections of society withthe belief to unleash the unbanked potential in India which result in the beginning of the revolution of prosperity and growth, if achieved.

Numerous definitions of financial inclusion have emerged from time to time, all of them reckoning the need for delivery of banking and financial services, at an affordable cost and to the disadvantaged people who have no access to financial products and services and also to the people who pertain to below poverty line and low income groups.

The Indian economy switched gears in the early part of this century and has been growing at a healthy pace since then. Financial inclusion is certainly not just a recent phenomenon. The earliest effort at financial inclusion in India can be traced back to 1904, when the co-operative movement began in the country. A focal event in its evolution was the nationalization of 14 major commercial banks in 1969, and the lead bank scheme was subsequently introduced. Over the past few decades, the Indian banking industry has shown tremendous growth in volume and complexity. It is observed that despite having significant improvements in the areas of financial viability, competitiveness and profitability, banks could notbrought the vast segment of the population, especially the disadvantaged and underprivileged, into the ambit of basic financial services. There are several factors that affect access to formal banking system in any country. These factors are culture, gender, financial literacy, proof of identity, remoteness of residence (distance between the household residence and the bank branch), income and assets etc. To increase access to these affordable financial services, the Reserve Bank of India has taken several steps since independence like financial education, generating awareness and leveraging technology, relaxation in the banking norms etc. The ultimate objective of financial inclusion is to promote sustainable development and employment generation for a majority of population.

STEPS TOWARDS FINANCIAL INCLUSION

The major phases towards the achievement of the financial inclusion in Indian economy comprises of three stages, which are as follows:

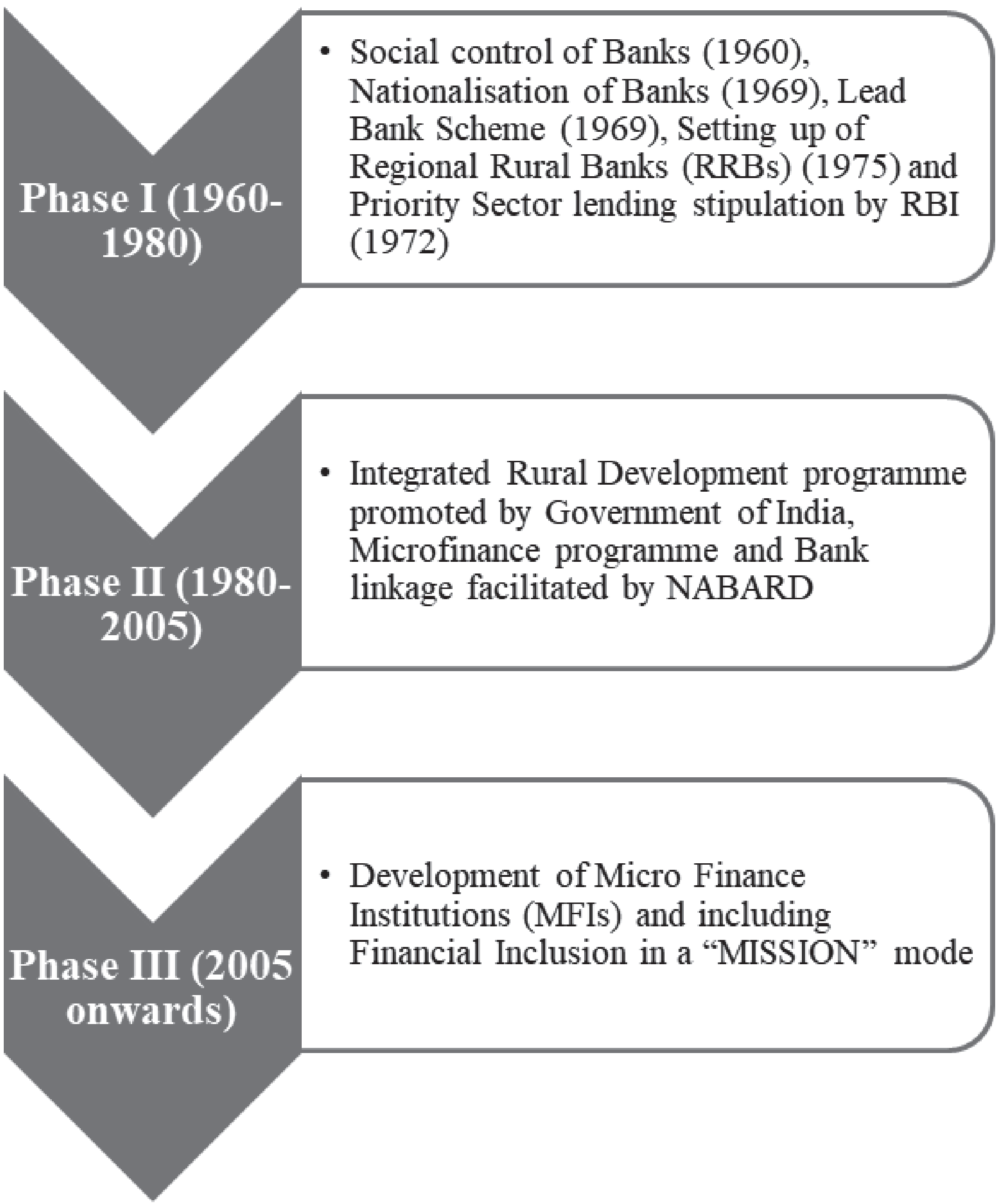

Figure: Phases of Financial Inclusion

FINANCIAL EXCLUSION

Financial Exclusion is known as the lack of access on the financial services by certain consumers to appropriate, fair and low cost, and safe financial products/ services from main stream institutions. In case of countries having large rural population like India, Financial Exclusion has become a geographic dimension as well.
Lack of awareness and education, inaccessibility, distance and lack of proper infrastructure are the major barriers to financial inclusion.

AmartyaSen (2000) propounded that poverty is not merely having insufficient income, but also the absence of wide variety of capabilities, which also includes security and capability to participate in economic and political systems.

Consequently, the disadvantaged, poor and deprived people are required to provide much essential financial products/ services and also the assistance in order to remove their conditions of poverty.

Accordingly, appropriate policy support should be there to channelize the financial resources towards the development and upliftment of economy. Financial inclusion aims to connect people with banking services with consequential benefits, on the same time it ensures that the financial system plays its due role in promoting inclusive growth. On the other hand, financial inclusion and development creates the conditions for the growth when access to easy and safe financial services with affordable credit by the poor and weaker groups andlagging sectors are channelized. It will help in accelerating the growth and reducing poverty and income disparities in India.

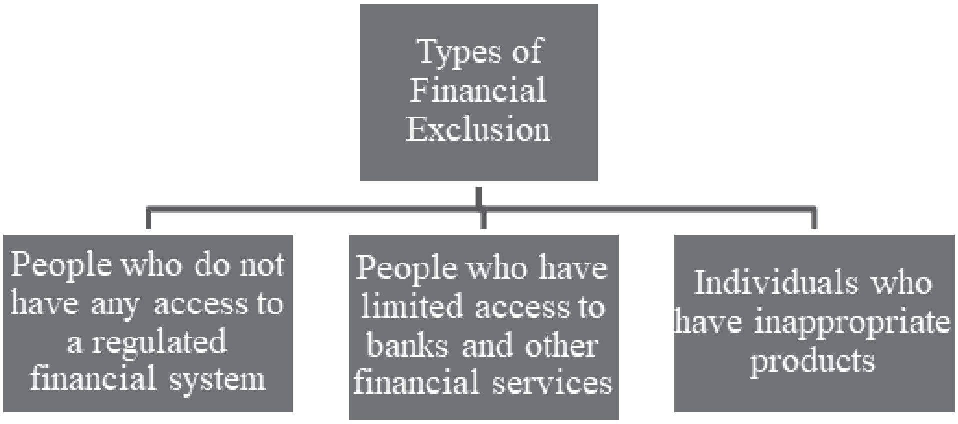

Figure: Types of Financial Inclusion

It is observed in various studies that mostly BPL families and low income groups, disabled, unemployed and illiterate people are excluded from the formal financial services. Lack of banking knowledge, high transaction cost, lack of Banking habits, and insufficient knowledge on banking products and services are the major obstacles for the unbanked people from knocking the door steps of banks. Thus, Financial Exclusion means "No Savings, No Insurance, No access to money advice, No affordable credit, No Bank account and No assets". There are people who desire the use of financial services, but are denied access to the same. Consequently, there are three types of Financial Exclusions, namely:

- People who do not have any access to a regulated financial system;
- People who have limited access to banks and other financial services; and
- Individuals who have inappropriate products.

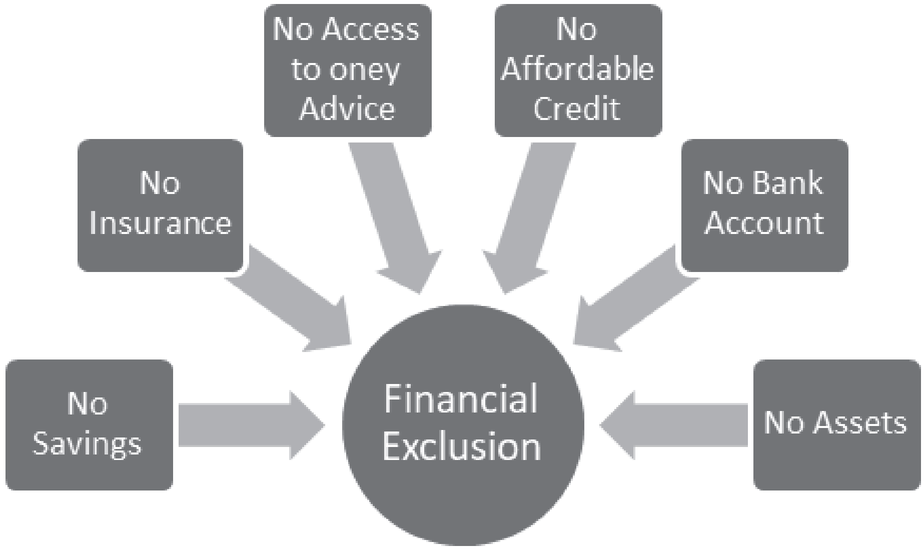

Figure: Meaning of Financial Exclusion

STATE OF FINANCIAL INCLUSION IN INDIA

Finance is very effective tool in spreading economic opportunity and fighting poverty. India has a relatively comprehensive financial system and a wide network of banks. Access to savings products, credit and transaction services enables people and businesses to accumulate financial assets, invest, spread risks and make payments cheaply and efficiently. There are well-established links between the size and scope of the financial system and the rate of economic growth.

Since the concept of Financial Inclusion is not new, it has become a global phenomenon and catches the global attention in the recent years. Lack of accessible, affordable and appropriate financial services has always been a global problem. Around 2.9 billion people in the world do not have access to formal sources of financial and banking services.

Most of the Indian population resides in rural areas, a convincing statement, nearby 72% of the population lives in villages. However, a large number of villages do not have a single bank to provide financial services to the households, which result the rural population in financial exclusion. RBI has reported that the financial exclusion in India leads to the loss of GDP to the extent of one per cent (RBI, Working Paper Series (DEPR): 8/2011). Disadvantaged people (also called financially excluded households) depend on informal system like money lendersfor their day to day expenditure, andthey borrow at the high excessive rates to get caught in a debt trap. In addition, people in far-off villages are completely unaware of financial products like insurance, which could protect them in adverse situation. Therefore, financial inclusion has a critical role in the development of India as a large population of the world resides in India. Although, for social cohesion and poverty reduction, access to financial services by the poor and vulnerable groups is a prerequisite.

A recent RBI report quotes a World Bank study undertaken in April 2012, which stated that only 9 % of Indian population had taken fresh bank loan in the past year with only 35% having formal accounts versus an average of 41 % in developing economies.

RBI defines Financial Inclusion as "a process of ensuring access to appropriate financial products and services needed by all sections of the society in general and vulnerable groups such as weaker sections and low income groups in particular, at an affordable cost in a fair and transparent manner by regulated mainstream institutional players". Therefore, the primary motive of Financial Inclusion is to provide financial products and services to the large amount of untouched population of India and to improve growth potential of financial sector in India. Further, it helps to achieve sustainable development and inclusive growth by making financial services available to the poor and disadvantaged people. Thus, keeping in view of the interests of the poor people, the Government of India (GoI) has taken a number of measures so that the underprivileged sections of the society can reap the benefits of the financial services.

In simple terms, Financial Inclusion could be defined as the delivery of financial and banking services to all the population in a transparent,equitable and fair manner at an affordable cost. Financial inclusion has been officially defined in India as the "provision of affordable financial services" to those who have been left unattended or under attended by the formal agencies of the financial system [RBI 2006]. These financial services include insurance and loan services, savings, payments and remittance facilities.

V. Leeladhar, 2006, Financial Inclusion is the delivery of banking services at an affordable cost to the vast sections of disadvantaged and low income groups. According to Chakravathy (2010), financial inclusion refers to delivery of financial system of an economy to its members.

ABC OF FINANCIAL INCLUSION

Financial Inclusion dependsupon three pillars which are (i) access to financial services, (ii) affordability of such services and (iii) actual utilization of such services. Financial Inclusion can be achieved with the affirmative results of all these three pillars.

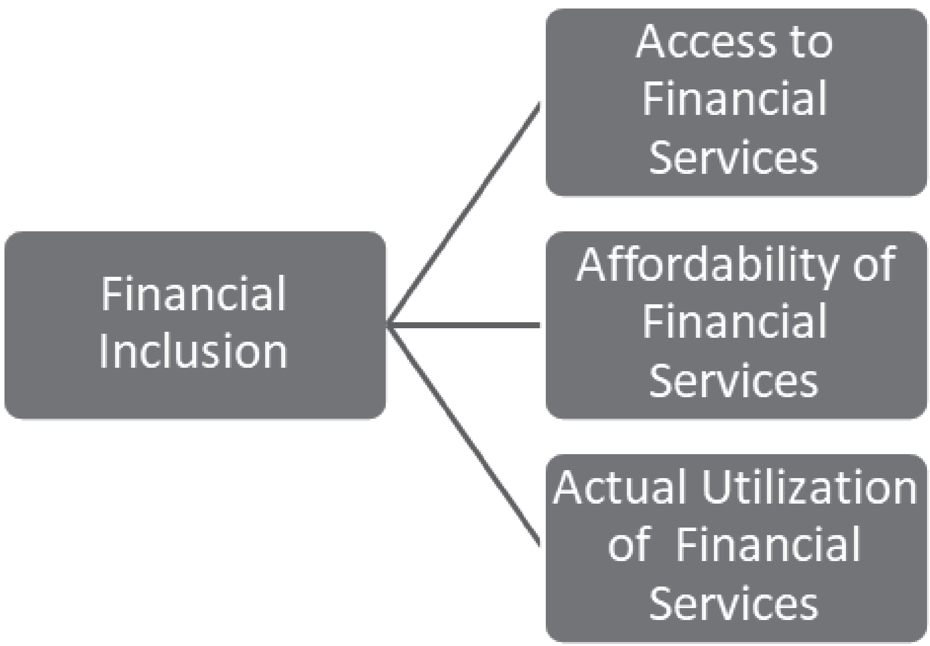

Figure: Pillars of Financial Inclusion

Figure: ABC of Financial Inclusion

Thus, promotion of financial inclusion would require a holistic and coherent approach on the part of the banking industry as also the regulator (RBI) and the Government.

NEED AND IMPORTANCE OF FINANCIAL INCLUSION IN INDIAN ECONOMY

The importance of Financial arises in developing countries because it is a milestone in the Economic Development of an economy. This will result in reducing poverty and providing for equitable growth to all sectors in the economy. Since traditional banking system has high cost, the bottom of pyramid section in India remains as the unbanked potential. If unbanked potential is bring within the ambit of Financial Inclusion, over the period of time it will lead to Economic growth.

However banking and financial institutions and Government of India perform a lot of efforts to obtain financial inclusion in India, but at the same time there are some expectations from the financial system that there should be:

- minimum paper work and relaxation in KYC norms,
- ease of access the financial services,
- provide security and safety of deposits,
- low transaction costs,
- convenient operating time ,
- avail easy and quick access to credit and other,
- ability to transact easily effect.

By providing, suitable and cost effective financial products and services to the BPL and low income families,the structure of informal unbanked sector will transform into the formal financial (banking) sector. Due to lack of Financial Literacy and practically no access to financial services, the substantial weaker section of society is unaware of Financial services and has to be depended upon informal sectors like borrowing from friends, family or usurious moneylenders to meet their needs like illness, property damage or death of the primary breadwinner .The existing Financial system requires to be redesigned so as to suit the requirements by taking into account their seasonal inflow of income from agricultural operations, migration from one place to another ,seasonal and irregular work availability and income.

To provide such financial system which is more responsive to needs of vulnerable group of the society, out of 20crorepeople in India, only 6.82 crorepeople have good access to banking and financial services. As far as rural population is concerned, out of 14croreindividual households, only 4.16 crore rural households are having access to basic financial services. In respect to urban areas, 49.52% of the urban population has access to financial services (basically banking services). In India, more than 41% of people falling in the category of major as per their age do not have their bank account. There are many factors having impact on the access to financial services by the financially weaker population of the society in India. Majorly, lack of awareness, social exclusion, illiteracy, low income and assetsare the barriers from demand side (population side). If we talk about the supply side, factor responsible for financial exclusion, these are the distance of household from bank branch, timings of bank branch, cumbersome banking procedure, unsuitable banking products, and requirements of KYC documents for opening a bank account, high transaction costs,language and attitude of bank officials. Hence, theneed for financial inclusion is immerged to obtain uniform economic development.

Since banking services are positively favorable for the public, the availability of banking and financial services to the poor and disadvantaged people becomes essential for the development of an economy. These services must be provided to the people at the same price so that discrimination of these services cannot take place. It becomes the primary objective of the economic growth.

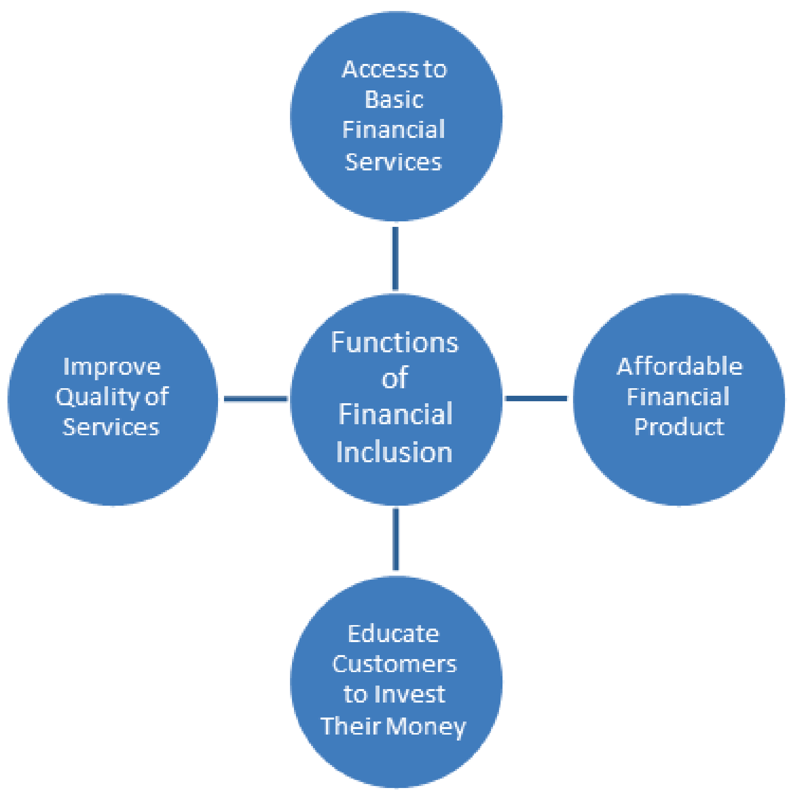

Figure: Functions of Financial Inclusion

FACTORS AFFECTING FINANCIAL INCLUSION

Factors having an impact on financial inclusion include the demand side factors as well as supply side factors. In Indian economy, the supply side factors are the various tools and parameters used by the RBI and GoI, and these factors are already discussed earlier. On the other part, the demand side factors include many regions, segment of the population and sub sectors of the economy. These sectors have low demand for the financial and banking services. So these sections of the community must be properly focused. In order to improve the level of inclusion, demand side efforts need to be undertaken including improving human and physical resource endowments, enhancing productivity, mitigating risk and strengthening market linkages.

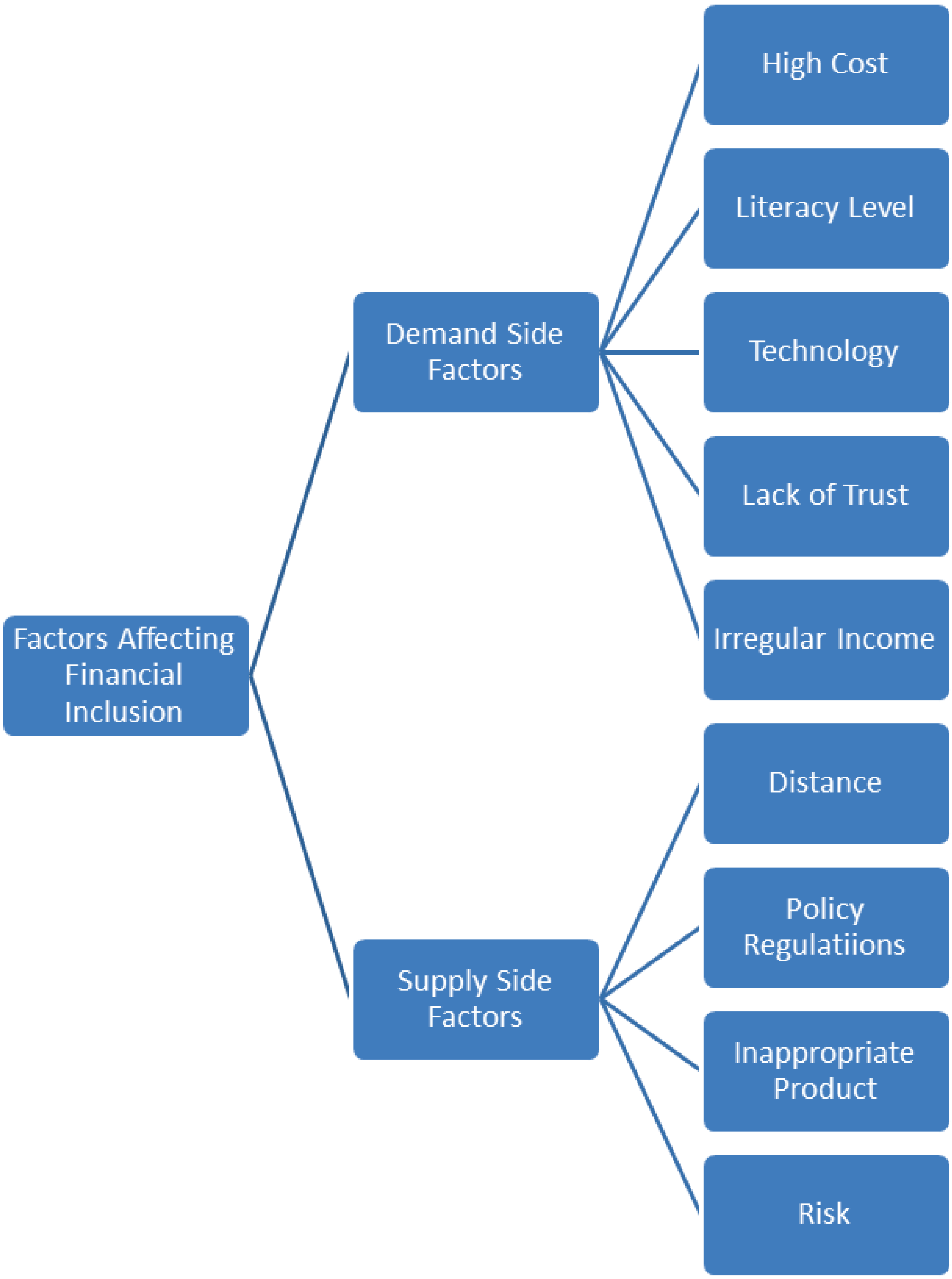

Figure: Factors Affecting financial Inclusion

Both factors are equally important for the growth of financial inclusion in the Indian economy. Government of India and the Reserve Bank of India have focused more on the supply side factors and delivery system for the financial inclusion which will lead to create a demand for these financial services and boosting the inclusion of vulnerable groups into the ambit of financial services.

FINANCIAL TRIPOD

Financial Tripod means the three essential factors responsible for the effective growth of an economy. These factors are as follows:

1.) Financial Education
2.) Financial Inclusion
3.) Financial Stability

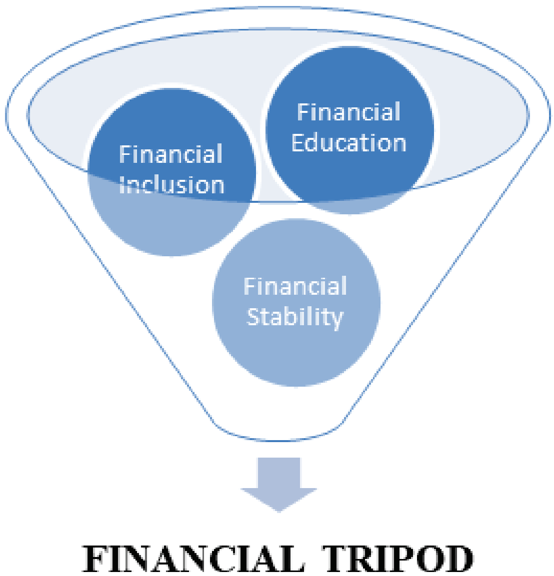

Figure: Financial Tripod

CONCLUSION

Data show that there is exclusion and that the poorer section is not covered under the area of financial inclusion. They were unable to access the financial services adequately. The farmers and sub marginal farmers, low income groups and other vulnerable groups need to be focused and must be provided with the easy credit and financial services delivery system. The delivery system of credit and other financial services should develop rapidly in order to bring the disadvantaged people within the area of finance. However, creating an appropriate credit delivery system is the only necessary condition. Banks are working for the inclusion while the Government is working for the employment generation and both are working together to achieve the goal of financial inclusion. These both can bring about the desired change of greater inclusion quickly.

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