An Empirical Study of Financial Inclusion in India

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Abstract
Financial inclusion is strategy of Government of India to provide wide range of financial services in rural area. On the occasion of Independence Day speech of 2012, the Hon’ble Prime Minister has announced that it will be our endeavor to ensure that all households benefit from bank accounts in the next 2 years. The main reason is that financial inclusion will develop a culture of savings among rural population and plays its own role in the process of economic development. Financial inclusion refers to access of financial services to poor or low-income clients. It is process to provide adequate and timely financial products or services to all weaker sections in the society at reasonable rate of interest inclusively very fair and transparent manner. France has first position in promotion of financial inclusion in his realm. A France Banking Act 1984 made that access bank account is a legal right to their inhabitant. Therefore, Financial Inclusion may be defined as universal access to a wide range of financial services at a reasonable cost. Apart from banking it also include other financial services such as insurance and equity products.

Keywords: - Financial Inclusion, Finance & Growth, Affordable Finance.

1 Introduction
Financial inclusion is strategy of Government of India to provide wide range of financial services in rural area since independence and especially RBI have been making concerted efforts since last five decades such as building up of robust branch network of regional rural banks, lead bank scheme, nationalization of banks, formation of self-help groups, network of scheduled commercial banks, permitting BCs/BFs to be appointed by banks to provide door step delivery of banking services, zero balance BSBD accounts, etc. The fundamental goals of all these initiatives are to reach the large sections of the hitherto financially excluded Indian rural population.

France has the leading position in promotion of financial inclusion in his realm. France Banking Act 1984 made that access bank account a legal right to their inhabitant. Therefore, According to Banking Act any person of French nationality has the right to open an account with any bank in France. The table 1 indicates on percentage of un-banked population in some developing nations.
On the occasion of Independence Day speech of 2012, the Hon’ble Prime Minister has announced that it will be our endeavour to ensure that all households benefit from bank accounts in the next 2 years". So, India is on the path to make hard attempt to extend banking facilities to the citizen under Swabhimaan. The campaign launched that every household has at least one bank account. It was expected to that this target will be achieve by August, 2014.

In this regard, the Department of Financial Services, Ministry of Finance stated in a detailed note, among other things, as under:-

Growth and development has been a priority of the Government of India. The policymaking and regulating institutions (Government of India, RBI, IRDA, PFRDA (for micro pensions) have developed regulations and guidelines for strengthening financial inclusion but these are yet to have an ample impact on outreach to the excluded population. Availability of bank finance to small borrowers in urban areas is comparatively better than the rural borrowers. Yet banks offer traditional products but borrowers demanded for customized products based on their income stream. Banks are not in position to meet loan demand due to predominance of service activities in urban areas and such demand fulfils by complementary role of micro financial institutions. The timely and adequate loans availability, especially during emergency is big lacking in the formal banking system. Hence borrowers requirement top-up by MFIs. So, unmet loan demand of formal banking covered by micro financial institutions.

Therefore, financial inclusion will develop a culture of savings among rural population and plays its own role in the process of economic development. Further, by bringing low income groups within the perimeter of formal banking, financial inclusion protects wealth and other resources in exigent circumstances. Financial inclusion also mitigates the exploitation of vulnerable sections by facilitating easy access to formal credit.

### 2 Review of literature

The Ministry of Finance (Department of Financial Services) vide its order dated 10th March, 2011 constituted a Committee to recommend the draft of a new Micro Finance Institutions (Development and Regulation) Bill. This Committee had members from the Department of Financial Services, Reserve Bank of India (RBI), Indian Banks Association (IBA), National Bank for Agriculture and Rural Development (NABARD), Small Industries Development Bank of India (SIDBI), the State Governments (Bihar and Tamil Nadu) and State Level Bankers ‘Committee, Andhra Pradesh. UN Advisors Group on Inclusive Financial Sectors Report (June 2008): Inclusive finance recognizes that
poor and low-income households and micro and small-scale entrepreneurs seek a broad range of financial opportunities; these include better ways to borrow, save, insure, and transfer money. Dr. R. Ramakumar, Expert - MFIs can play only a marginal role in deepening financial inclusion. The most important role has to be played by opening new rural branches of scheduled commercial banks, co-operative societies and grameen banks. This was the position taken by the Reserve Bank of India representative, as a member of the Rangarajan Committee on financial inclusion.

3 Objectives of the Project
The main objective of the study is to make an empirical investigation of financial inclusion in India. Financial Inclusion refers to access of financial services to poor or low-income clients. It facilitates timely and adequate credit where needed by vulnerable groups at an affordable cost. Therefore, Financial Inclusion may be defined as universal access to a wide range of financial services at a reasonable cost. Apart from banking it also include other financial services such as insurance and equity products. Household access to financial services is depicted below:

4 Methodology of the Study
Mainly the secondary data has been collected through RBI Bulletins/ Annual Reports/Working Papers on finance, Reports on Trend & Progress of Banking, Financial Access Survey, Report of the various Committees on Financial Sector Reforms, Basic Statistical Returns and MSME Annual Reports and important data collected from internet. Various tools of analysis have been used in the study as per the requirement such as table/figure/chart presentation for interpretation and analysis.

4.1 Methods Used
A sincere attempt is made by author to go through various reports which have been published by RBI and other financial departments of the Govt. of India for deep knowledge of the subject and use his influence for interpretation about the matter to make good suggestion for better reforms in the field of financial inclusion in India.
The essence of financial inclusion is to ensure delivery of financial services which include - bank accounts for savings and transactional purposes, low cost credit to productive for personal and other purposes, financial advisory services like insurance facilities (life and non-life) etc.

4.3 Extent of Financial Exclusion - In this section, the extent of financial exclusion from different perspectives / angularities is presented based on five different data sources viz.:

(a) Government of India Population Census 2011.
(b) CRISIL-Inclusix.
(c) World Bank ‘Financial Access Survey’ Results.
(e) NSSO 59th Round Survey Results.

5 Government of India Population Census 2011
As per census 2011, only 58.7% of households are availing banking services in the country. In compression with previous census 2001, availing of banking services increased significantly on account of increase in banking services in rural areas (Chart 2).

![Chart 2: Availing of Banking Services](source: Department of Financial Services, Ministry of Finance)

6 CRISIL Financial Inclusion Index (Inclusix)
- CRISIL first time published a comprehensive financial inclusion index (Inclusix) in June 2013. While constructing the index, CRISIL identified three critical parameters of basic banking services.
  (a) Branch penetration.
  (b) Deposit penetration.
  (c) Credit penetration.
- The CRISIL Inclusix indicates the overall improvement in the financial inclusion in India (Chart 3).
- CRISIL -Inclusix (on a scale of 100) increased from 35.4 in March 2009 to 37.6 in March 2010 and to 40.1 in March 2011.
The big positive to have come out that the level of financial inclusion has consistently been on the rise since 2009. The driving reason for this growth has been mainly due to an improvement in deposit penetration. Now it is time to focus on other parameters i.e. branch and credit penetration to ensure all-round improvement in CRISIL Inclusix score. It clearly spells out the need for opening of branches in un-banking or rural areas.

7 World Bank ‘Financial Access Survey’ Results

It would be observed from the data that in our country, financial exclusion measured in terms of bank branch density, ATM density and bank credit to GDP and bank deposits to GDP is quite low in comparison with most of developing countries.

Table 1: Select Indicators of Financial Inclusion, 2011

<table>
<thead>
<tr>
<th>S.No</th>
<th>Country</th>
<th>Number of Bank Branches Per 1000 KM</th>
<th>Number of ATMs Per 0.1 Million</th>
<th>Number of Bank Branches as % to GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>India</td>
<td>30.43</td>
<td>25.43</td>
<td>10.64</td>
</tr>
<tr>
<td>2.</td>
<td>China</td>
<td>1428.98</td>
<td>2975.05</td>
<td>23.81</td>
</tr>
<tr>
<td>3.</td>
<td>Brazil</td>
<td>7.93</td>
<td>20.55</td>
<td>46.15</td>
</tr>
<tr>
<td>4.</td>
<td>Indonesia</td>
<td>8.23</td>
<td>15.91</td>
<td>8.52</td>
</tr>
<tr>
<td>5.</td>
<td>Korea</td>
<td>79.07</td>
<td>...</td>
<td>18.8</td>
</tr>
<tr>
<td>6.</td>
<td>Mauritius</td>
<td>104.93</td>
<td>210.84</td>
<td>21.29</td>
</tr>
<tr>
<td>7.</td>
<td>Mexico</td>
<td>6.15</td>
<td>18.94</td>
<td>14.86</td>
</tr>
<tr>
<td>8.</td>
<td>Philippines</td>
<td>16.29</td>
<td>35.75</td>
<td>8.07</td>
</tr>
<tr>
<td>9.</td>
<td>South Africa</td>
<td>3.08</td>
<td>17.26</td>
<td>10.71</td>
</tr>
<tr>
<td>10.</td>
<td>Sri Lanka</td>
<td>41.81</td>
<td>35.72</td>
<td>16.73</td>
</tr>
<tr>
<td>11.</td>
<td>Thailand</td>
<td>12.14</td>
<td>83.8</td>
<td>11.29</td>
</tr>
<tr>
<td>12.</td>
<td>Malaysia</td>
<td>6.32</td>
<td>33.98</td>
<td>10.49</td>
</tr>
<tr>
<td>13.</td>
<td>UK</td>
<td>52.87</td>
<td>260.97</td>
<td>24.87</td>
</tr>
<tr>
<td>14.</td>
<td>USA</td>
<td>9.58</td>
<td>...</td>
<td>35.43</td>
</tr>
<tr>
<td>15.</td>
<td>Switzerland</td>
<td>84.53</td>
<td>166.48</td>
<td>50.97</td>
</tr>
<tr>
<td>16.</td>
<td>France</td>
<td>40.22</td>
<td>106.22</td>
<td>41.58</td>
</tr>
</tbody>
</table>

Source: Financial Access Survey, IMF, Figures in respect of UK as on 2010
Sadhan Kumar (2011) worked out an Index on financial inclusion (IFI) based on three variables namely penetration (number of adults having bank account), availability of banking services (number of bank branches per 1000 population) and usage (measured as outstanding credit and deposit). The results indicate that Kerala, Maharashtra and Karnataka has achieved high financial inclusion (IFI >0.5), while Tamil Nadu, Punjab, A.P, H.P, Sikkim, and Haryana identified as a group of medium financial inclusion (0.3 <IFI<0.5) and the remaining states have very low financial inclusion. The RBI has put out a discussion paper in August 2013 on Banking Structure for public comments or suggestions. One of the main issues relates to “Differentiated Banking Licenses”. The subject of licensing ‘small banks and financial inclusion’ has been discussed therein. A view will be taken by RBI after factoring in the comments/suggestions received from the general public.

NSSO 59th Round Survey Results

- In India about 51.4% of farmer households are financially excluded from both formal/informal sources.
- Of the total farmer households, only 27% access formal sources of credit and one third of this group also borrowed from non-formal sources. Therefore, 73% of farmer households have no access to formal sources of credit.
- Financial exclusion is more acute in Central, Eastern and North-Eastern regions. All three regions together accounted for 64% of all financially excluded farmer households in the country. Overall indebtedness to formal sources of finance of these three regions accounted for only 19.66%.

However, over the period of five decades, there has been overall improvement in access to formal sources of credit by the rural households (Chart 4).
Recent Measures

10.1 Licensing of New Banks: Licensing new banks has associated the thought of big push to financial inclusion efforts in our country. Innovative business models aimed at financial inclusion efforts would be looked into closely in processing applications for banking license. Thus, financial inclusion plan in India helps to procure a new bank licenses. (Dr. D Subbarao).

10.2 Progress in Financial Inclusion in India

RBI has advised that the Financial Inclusion Plans (FIPs) must have assurance at the highest levels, through preparation of Board approved Plans. The first phase of FIPs was implemented during 2010-2013. RBI has followed a planned approach to ensure financial inclusion by strategies to achieve sustainable and scalable Financial Inclusion.

RBI has adopted a bank-led model based on technological influence. To acquire effective financial inclusion in better way is possible through mainstream banking as they have the ability to offer the suite of products. Progress of financial inclusion plans clearly indicates that banks are progressing in areas like opening of banking outlets, deploying BCs, opening of BSBD accounts, grant of credit through KCCs and GCCs.

10.3 Number of Branches Opened (including RRBs)

- Since 2005, due to RBI’s efforts the number of branches of Scheduled Commercial Banks increased manifold from 68,681 in March 2006 to 1,02,343 in March 2013, spread across length and breadth of the country.
- In rural areas, the number of branches enhanced from 30,572 to 37,953 during March 2006 to March 2013. As compared with rural areas, number of branches in semi-urban areas increased more rapidly (Chart 5).

![Chart 5: Branches of Scheduled Commercial Banks](chart)

Source: Basic Statistical Returns, RBI and DFS, Govt. of India.
10.4 Villages Covered

Chart 6 indicates clearly that number of banking outlets in villages with population more than 2000 as well as less than 2000 increased rapidly since March 2010.

<table>
<thead>
<tr>
<th>Years</th>
<th>Villages with Population &gt; 2000</th>
<th>Villages with Population &lt; 2000</th>
</tr>
</thead>
<tbody>
<tr>
<td>March 2010</td>
<td>26905</td>
<td>27353</td>
</tr>
<tr>
<td>March 2011</td>
<td>45937</td>
<td>54246</td>
</tr>
<tr>
<td>March 2012</td>
<td>65234</td>
<td>82300</td>
</tr>
</tbody>
</table>


Though, RBI is of the belief that sustainable financial inclusion is achievable through mainstream financial institutions i.e. banks. However, as banks are yet to fully penetrate to a large number of villages in the country. The most important role has to be played by opening new rural branches of scheduled commercial banks, cooperative societies and grameen banks.

- **Total Bank Outlets (including RRBs)** - Total number of banking outlets in villages increased from 67,694 in March 2010 to 2,68,454 in March 2013 (increased around 4 times during the period of three years). Of total branches, banking outlets through BCs increased from 34,174 to 2,21,341 during the same period (increased around 6.5 times).

- **Kisan Credit Cards (KCC) Issued** - Banks have been advised to issue KCCs to small farmers for meeting their credit requirements. Up to March 2013, the total number of KCCs issued to farmers remained at 33.79 million with a total outstanding credit of Rs.2622.98 billion.

- **General Credit Cards (GCC) Issued** - Banks have been advised to introduce General Credit Card facility up to Rs. 25,000/- at their rural and semi-urban branches. Up to March 2013, banks had provided credit aggregating to Rs.76.34 billion in 3.63 million GCC accounts.

- **BSBD Accounts Opened** - The number of BSBD accounts opened increased from 73.45 million in March 2010 to 182.06 million in March 2013. RBI advised banks to provide small overdrafts in BSBD accounts. Accordingly up to March 2013, 3.95 million BSBD accounts availed OD facility of Rs. 1.55 billion (These figures respectively, were 0.18 million and 0.10 billion in March 2010).

10.6 ICT Based Accounts - through BCs
In order to provide efficient and cost-effective banking services in the un-banked and remote corners of the country, RBI directed commercial banks to provide ICT based banking services – through BCs. These ICT enabled banking services have CBS connectivity to provide all banking services including deposit and withdrawal of money in the financially excluded regions.

- The number of ICT-based transactions through BCs increased from 26.52 million in March 2010 to 250.46 million in March 2013, while transactions amount increased steadily from Rs.6.92 billion to Rs.233.88 billion during the same period.

10.7 Expansion of ATM Network - The total number of ATMs in rural India witnessed a CAGR of 30.6% during March 2010 to March 2013. The number of rural ATMs increased from 5,196 in March 2010 to 11,564 in March 2013 (Chart 7).

10.8 Insurance Penetration in the Country - The total insurance (life and non-life) penetration in terms of the ratio of insurance premium as a percentage of GDP increased from 2.32 in 2000-01 to 5.10 in 2010-11. The life insurance penetration as a percentage of GDP stood at 4.40 in 2010-11 while the non-life insurance penetration remained at 0.71 during the same period. In other words, there is huge untapped potential as regards insurance penetration.

10.9 Bank Credit to MSME

- MSME sector which has large employment potential of 59.7 million persons over 26.1 million enterprises, is considered as an engine for economic growth and promoting financial inclusion in rural areas. MSMEs mainly depend on bank credit for their operations.

- Of total credit to MSME, public sector banks contributed the major share of 76%, while private sector banks accounted for 20.2% and foreign banks accounted for only 3.8% as on March 31, 2012.
11 Approach to Micro Finance

The Ministry of Finance (Department of Financial Services) in a detailed note stated on the rate of interest of loans by MFIs as under:

MFIs typically charge a higher rate of interest to their clients than traditional commercial banks. The sanction cost of servicing smaller loans is very higher in terms of percentage. Additionally, MFIs provide doorstep services to their customers, a strategy that has a high cost associated with it, in rural areas where population densities tend to be low.

Maglebom Committee (2011) defined the needs of Micro Finance in the following terms that it is so important tools of economic development. The objective is to assist the poor to work with their way out of poverty. It covers a range of services which include, in addition to the provision of credit, many other services such as savings, insurance, money transfers, counseling, etc.

Micro Finance sector can be classified as falling into three main Groups:

(a) The SHG-Bank linkage Model accounting for about 58% of the outstanding loan portfolio.
(b) NBFCs accounting for about 34% of the outstanding loan portfolio.
(c) Others including trusts, societies, etc, accounting for the balance 8% of the outstanding loan portfolio.

Around 95,663 Primary Agricultural Co-operative Societies (PACS) covering every village in India. Combined membership of over 13 crores and loans outstanding of over Rs. 64,044 Crores as on 31.03.2009 have a much longer history and are under a different regulatory framework. Clause 33 deals with redressal of Grievances against MFIs. Reserve Bank shall formulate a scheme for redressal and issue directions to MFIs.

**Chart 8: Bank Credit to MSME**

<table>
<thead>
<tr>
<th>Year</th>
<th>Bank Credit to MSME (in Billion)</th>
</tr>
</thead>
<tbody>
<tr>
<td>March 2007</td>
<td>1013</td>
</tr>
<tr>
<td>March 2008</td>
<td>1273</td>
</tr>
<tr>
<td>March 2009</td>
<td>2135</td>
</tr>
<tr>
<td>March 2010</td>
<td>2561</td>
</tr>
<tr>
<td>March 2011</td>
<td>3640</td>
</tr>
<tr>
<td>March 2012</td>
<td>4859</td>
</tr>
<tr>
<td>March 2013</td>
<td>5209</td>
</tr>
</tbody>
</table>

At present there is only a Grievance Redressal Mechanism is set up by RBI but no criminal proceedings can be initiated. If you are abetting people to commit suicide by your own exploitative practices then we need some kind of punitive measure to be included.

12 Financial Inclusion – RBI Policy Initiatives

Basic Saving Bank Deposit (BSBD) accounts with minimum common facilities such as zero balance, facility of providing ATM card to every customer, deposit and withdrawal of cash at bank branch and ATMs, receipt/credit of money through electronic payment channels. KYC norms must be easy for small accounts with balances not exceeding Rs. 50,000 and aggregate credits in the accounts not exceeding Rs. one lakh a year. Therefore, KYC norms may be relaxed and simplified in case of rural small income group client.

Vital needs of opening new branches in Un-banked Villages, banks are directed to allocate at least 25% of the total number of branches to be opened during the year in un-banked (Tier 5 and Tier 6) rural centers. In the rural area banks are also advised not to insist their rural customers on introduction for opening a new bank account.

Rural branch could be in the form of a low cost structure consisting of minimum infrastructure. Core banking solution terminal linked to a pass book printer and a safe for cash retention for operating larger customer transactions.

Financial Literacy and easy banking access curriculum, accordingly total 718 Financial Literacy Centre have been set up in rural area in the end of March 2013. Approx 2.2 million people have been educated through safe banking lectures, awareness camps and seminars during April 2012 to March 2013.

13 Important Suggestions

- The role of the State Governments is equally important in achieving financial inclusion and in implementing and monitoring.
- It is imperative that financial services to the poor borrowers should be statutorily provided at an affordable cost.
- The Government should have considered involving the Panchayati Raj Institutions (PRIs) in the functioning of MFIs.
- Government should open more branches in rural and remote village’s area to move towards financial inclusion. Therefore, the Government should persist with pursuing the bank-led model for achieving financial inclusion.
- The need for the greater involvement of banks in provision of services to the low income groups.
- Micro credit facility to the “rural and urban poor” and “other disadvantaged sections of the people”. It provides ample scope for MFIs to lend to other sections of Society instead of focusing on the poor / weaker sections. Therefore, flow of equity funds to MFIs need to be examined.
14 Conclusion

Banks have now drawn up fresh 3 year Financial Inclusion Plans for the period 2013-16. The focus under the new plan is to ensure that the large banking network created which will help make the business more viable for banks and will ensure that large number of accounts opened see large volume of transactions and benefits of getting linked to the formal financial institutions. The ceiling on interest rate is currently under review. Also processing charges are not included in the margin cap or the interest cap. It must be noted that the rate of interest may look high but the rate that borrowers will have to pay the money-lender would have been far higher. Interest rates have been deregulated by the Bank. However, given the clientele of the NBFCs-MFI, interest rate ceilings have been placed. It would not be appropriate to levy differential rates of interest under a scenario when the Bank is in favour of leaving interest rates to market forces.

India is standing at such juncture that an assessment of Financial Inclusion efforts under going in our country and the conferences which have been conducted for the past few years. It is one’s earnest hope and desire that the issues raised herein would trigger an informed debate and discussion may like to go into such aspects of Financial Inclusion. These aspects definitely would provide valuable leads to the regulators and all the stakeholders concerned in achieving meaningful and holistic Financial Inclusion at the earliest in our country.

15 References