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# FINANCIAL INCLUSION: OLD WINE IN NEW BOTTLE

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**ABSTRACT**

*Government and finance ministry is working hard for financial inclusion in the country. Basically financial inclusion is related with the delivery of financial services at an affordable cost to vast sections of low income groups which includes savings, credit, insurance, and remittance facilities. This article critically examines the efforts and role of government in financial inclusion as it is not a new project. Providing a financial service to low income group and channelizing them to main stream of country's financial system remains an important agenda of government. Earlier also government launched various schemes like Prime Minister Employment Scheme, priority sector advance, etc. for the up- liftment of these people but due to poor implementation at the ground level could not achieve desired success. Now the government is trying to revive the same under the new banner called Financial Inclusion. This article is an effort to elaborate the Motive, Problems & Suggestions.*

**KEYWORDS**
Financial Inclusion, Financial Services, Financial System, Microfinance.

## INTRODUCTION

"Financial inclusion may be defined 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." It is the buzz word today. Every second day we find a headline in newspaper related to financial inclusion. RBI and Finance Ministry are very keen towards financial inclusion. Even finance ministry has announced to launch financial inclusion index this year.

Basically financial inclusion means providing access to financial services such as payments, savings, insurance etc. at an affordable cost, to low income group and weaker section of society, who are not using banking and financial services through organized channel.

Banks act as mobilizers of public saving. They channelize the funds in organized way. The people, who have surplus with them, put their money with banks and banks lend these surpluses to those who need it. Banks also facilitate people to route their business and financial transactions through banks, which helps in efficient management and flow of funds throughout the country.

As per available data, 66% of Indian people are not using financial services through organized sector. They borrow from local vendors at unfavorable conditions in times of need and also disburse their surplus in unorganized way (like there are some local agents who run some schemes often called kametis or chit funds in which a group of 12-20 people pay some fixed amount every month depending upon the number of members). If the members are businessman they bid for the kitty every month and the highest bidder takes the money. Sometimes it is merely a lottery system in which the names are chosen through lottery and the member chosen through lottery gets discounted amount of the kitty. These systems have their own merits and demerits. The major drawbacks of these systems are: These are quite risky and the returns are unsystematic and inadequate.

The key purpose of financial inclusion is to bring these unorganized people into the mainstream of country's financial system, so as to get these funds into the system and provide due benefits to the investors. Banks being regulated by the government regulations and controlled by the Central Bank of the country have to keep caution and their uttermost priority is the security of the deposits placed by the depositors whereas money with local agents is always at the risk of not only loosing the interest but even the capital. Further the interest rates on credits provided by the banks are comparatively low and planned (EMIs).

Banks market customized products according to the needs of the customers like loan for small & rural businesses, housing loans, personal loans, child future plans, pension plans etc. Banks also provide extra benefits with accounts like insurance plans and risk covers. The return on the deposits are fixed which helps the customers in future planning and if required the depositor can take loan against their deposits by paying a marginal higher rate of interest in case of need, without breaking the deposit. This loan can be repaid as and when the depositor gets the money or can be adjusted at the time of final maturity. In case of emergency the deposits can be broken and taken away with a nominal loss in interest.

But in spite of all these rural and uneducated people hesitate to go to the banks because of certain difficulties remarkably, the complex procedures and formalities for opening of accounts, and the non-cooperation of bank officials. The biggest difficulty faced by the borrowers is the requirement of collaterals for availing loan facility.

## REVIEW OF LITERATURE

So far researchers have carried out a little work on the prospectus and problems of Financial Inclusion in India, but the suggestions based on the Theories/Material Published/Development so far are mentioned hereunder:

- Fed Governor, Frederick Mishkin in his JMCB-FDIC Lecture presented at the FDIC, Washington, D.C. on September 22, 2005 said "The importance of finance to economic growth has also frequently been ignored by economists.
- The leading textbook on economic growth, Weill (2005) does not discuss the link between finance and growth at all.
- In initial finance theories like Modgillani Miller theorems and Efficient Market Hypothesis (developed by Eugene Fama and Kenneth French) were based on the assumption that markets are perfect and there are no frictions. But if these theories were correct then there was very little reason for financial markets to exist. However, later development showed that there were imperfections in the financial market and how various financial entities led to reduction of these imperfections.
- Rangarajan Committee, 2008, "Report of the Committee on Financial Inclusion", Committee Report.
- Sinclair S. P., 2001. "Financial exclusion: An introductory survey", Report of Centre for Research in Socially Inclusive Services, Heriot-Watt University, Edinburgh. Etc.

## WHY IS FINANCIAL INCLUSION IMPORTANT?

Financial inclusion is important to divert the funds from unorganized financial sector to productive organized sector. The surplus money if infused in the system can give risk free returns and to channelize these funds to those who can put it to productive use and encash the available opportunities as such helping the economy to grow. On the other hand, low income groups and weaker section of society can be provided the credit facility to uplift their living conditions. There are many government schemes providing subsidies for the benefit of the rural and unorganized poor strata of the society. But it is very difficult to implement these schemes in absence of proper distribution channels. Another important sector, of which the benefits have still not reached to this section of society, is the insurance sector.

## PREVIOUS EFFORTS MADE BY GOVERNMENT

The phenomenon of Financial Inclusion is not new in India. Government had initiated several schemes to streamline the financial markets i.e. converting them from unorganized to organize. Various schemes were initiated like priority sector advances, providing easy loans in rural areas to buy cattle, for agriculture purposes, poultry, handicrafts, Scheme for unemployed educated youth to establish their own business etc. Government also encouraged cooperative societies, established specific financial institutions for sectoral developments i.e NABARD, SIDBI, Bhoomi Vikas Banks etc., All these efforts did not give the desired results due to poor implementation. The plans were really good and their purpose to benefit the lower sections was also very pious, but all these went in vain due to poor implementations.

## THE MAJOR REASONS BEHIND THE FAILURE OF THESE SCHEMES WERE

Firstly, the employees at the implementation level were not motivated enough to implement these schemes. Government developed these schemes to increase their vote bank and through RBI, tried to implement the schemes that in turn imposed them on banks by giving them specific targets and linking the same with new branch licences. The banks, in order to achieve their targets, forced the staff at these places to implement these schemes. The employees who were posted in rural areas who already considered their posting as a punishment did not take much interest in disbursing and monitoring these schemes. These Employees had no motivation factor working in rural areas, so they just wanted to kill their time and wait to complete their rural posting so that they could get a transfer to an urban city.

Secondly, the employees worked under pressure. They had to achieve the targets, so they just disbursed the loan by misguiding the people that they will get subsidy from the government and there was no need to repay these loans. They did not bother to educate people about the benefits of the scheme i.e. to plan the financials, efficient use of loans, plan the repayments and encouragement for small savings. They did not blend the social values in their working.

Thirdly, the corruption was another reason. Rural and low income people are illiterate. In lack of knowledge and awareness, the government agencies in connivance with bank officials took the advantage. They took loan by using their name and use for personal purposes; the schemes were implemented only in papers.

Additionally, the repayment was very poor. People were unable to pay their debts due to bad management of loans. For example, agriculture loans were used for personal purposes like marriages etc. then the farmers were unable to pay and it lead to suicides. Banks did not show any interest to provide them adequate knowledge about the financial management. Also the products and services were not suitable to the needs of people.

Lastly, people did not have collateral security to provide against these loans. No alternative was evolved to cover the risk of banks money. Banks stick to their policy of providing loans based on collaterals. So in absence of collaterals people could not be benefited from these government schemes.

## REASONS BEHIND GOVERNMENT INTEREST TOWARDS FINANCIAL INCLUSION

RBI and Finance ministry are very keen regarding financial inclusion. Finance Ministry assigns targets to various banks to open the bank accounts of people. Banks are opening "no-frill accounts" with minimum or zero balance. Now question is that what makes government think about the financial inclusion at high pace. The major motivation behind this is success stories of microfinance institutions. The microfinance institutions play a vital role to provide small loans to rural and low income groups. In spite of the fact that they charge a very high interest rate, they have shown remarkable profits and growth in client base in very short time span. More and more people and financial institutions are getting attracted towards the financial inclusion or microfinance. The success stories of the microfinance institutions like SKS Microfinance have opened the eyes of RBI and finance ministry. The area which had always been considered as an expenditure and burden for government has been proved milk giving cow for microfinance institutions. Many microfinance institutions which had started their operations as NGOs, converted to NBFC's have a large client base and earning handsome profits with complete safety of their money.

For example SKS Microfinance, India's first biggest Microfinance Institution started by Vikram Akula, an IIT'ian in the year 1997 as NGO, converted it into NBFC in the year 2005, is coming with its IPO worth INR 1658 crore this year, working in 16 states, having branches in 340 districts, has 1627 centers, 5.3 million clients, total loan disbursement INR 32,319 million, total portfolio outstanding INR 32,080 millions, has shown INR 556 million profits, has total assets INR 36,435 million till September 2009.(Data source www.sksmicrofinance.com)

What SKS Microfinance did differently to convert the expenditure & burden to milk giving cow? The credit goes to better implementation strategies, understanding the needs of the people and implementing the schemes in well planned and systematic way. They adopt a village, train people to efficiently use the loans, help them to start small businesses. They have efficient weekly collection system, along with better risk hedging strategies like joint liability groups. Therefore they have excellent repayment record and hence able to get good returns.

Success of these microfinance institutions gave insight to government that if these MFIs earning profits out of rags then why not banks.

## GOVERNMENT IS MAKING A MISTAKE AGAIN

However government is motivated enough for financial inclusion, finance ministry as well as RBI are planning for the implementation of financial inclusion. However they have not learnt lesson from the previous failures. If finance ministry wants 100% financial inclusion it has to look upon the working of microfinance institutions. It has to apply various strategies for successful implementation of its plans. It has to make policies for ground level activities and need strong controlling and monitoring strategies so that the project does not loose its motive. Finance ministry is thinking to include local kirana stores as their agents, but again it needs an effective controlling and monitoring system so that the owners of these kirana store holders can effectively transfer the benefits to the people and also insure that they do not cheat the people due to their illiteracy and unawareness.

## SUGGESTIONS

The following prerequisites are certain to give a big boost to Financial Inclusion in India such as:

- The main emphasis is here to impart the financial awareness among people so that they can themselves take decisions and the agents, local vendors, bank officials can not take advantage of them and help in delivering the benefits to them which they deserve and made especially for them.
- As finance ministry going to take the help of local kirana stores, in addition to that government can take the help of Postal Department because it has a strong network throughout the rural areas of India as well as it is already have some financial products like savings and insurance products, through which it is serving low income groups and rural societies. As Bancassurance is a collective effort of insurance department and banks through which banks are distributing insurance products, similarly there should be collaboration between post offices and banks so that post offices can distribute banks products.
- Additionally government can emphasized financial inclusion through its existing systems. Government can restructure cooperative societies and self help groups and impart more efficient controlling and monitoring system so that they can come out with desired results.
- Also, banks should have enough motivational incentives for the employees who are working in rural areas. Banks also recognize those employees, who have high need of achievement and reorganization derive in them and send them to rural areas with targets and should reward appropriately, so that employees take it as challenge rather than punishment to work in rural areas.

## CONCLUSION

Since there has been numerous research analyzing how financial systems help in developing economies. This research has not just looked at how finance inclusion helps economic activity but also social aspects like Employment, poverty, hunger etc. Like any research on a particular topic, the findings have been diverse and the consensus is that finance helps but the magnitude of impact differs. Also research provide the way to give a big boost to Financial Inclusion in India.

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