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FINANCIAL INCLUSION - THE QUESTION UNANSWERED

SMITA RAO
LECTURER
DATTA MEGHE INSTITUTE OF MANAGEMENT STUDIES
NAGPUR - 440 022

VAISHALI RAHATE
ASST. PROFESSOR
DATTA MEGHE INSTITUTE OF MANAGEMENT STUDIES
NAGPUR - 440 022

ABSTRACT

For the total economic development of India it is important to develop rural India. Government and RBI being aware of the fact has always been keen to spread formal financing system through opening number of branches in under banked in unbanked areas. The government is also coming up with number of schemes in every five year plans, but still there are number of villages unbanked. As Reserve Bank of India data shows that as many as 139 districts suffer from massive financial exclusion, with the adult population per branch in these districts being above 20,000 and only 3 percent with borrowings from banks. This paper is to bring forward the various factors related to banks and rural population which at micro and macro level hindering the financial inclusion. This paper also proposed the recommendation to minimize the lacunas to accelerate financial inclusion.

KEYWORDS

Financial Inclusion, financial exclusion, banks, rural.

INTRODUCTION

Financial inclusion is the need of hour and dream of every country. India being country of large and diverse population, where significant segment is rural and financially excluded, requires a high level of penetration of formal financial system for financial inclusion. India has roughly 70% of the population located in almost 6,27,000 villages where even today the influence of moneylenders is high due to which 64% to 97% of the rural population is in the clutches of informal channels. Since independence Government is putting all the efforts to provide formal finance to the rural population by opening branches of co-operative banks, commercial bank, and regional rural banks in under/unbanked rural areas but maximum rural population is deprived of banking facilities which lead to ***financial exclusion***.

FINANCIAL EXCLUSION

According to K.C.Chakrabarty "Financial Exclusion is the lack of access by certain consumers to appropriate, low cost, fair and safe financial products and services from main stream providers."

Financial Exclusion: is lack of access by the poor and rural population to the formal sources of banks finance and other financial entities. Financial exclusion can be of following types:

- Core Exclusion: those who operate their financial affairs completely outside the regulated financial system
- Limited Access: May have a basic bank account but poor financial habits and little advice
- Included but using inappropriate products: Victims of inappropriate products.

Problem area: As Reserve Bank of India data shows that as many as 139 districts suffer from massive financial exclusion, with the adult population per branch in these districts being above 20,000 and only 3 percent with borrowings from banks.

FINANCIAL EXCLUSION REASONS

Financial Exclusion Attributes

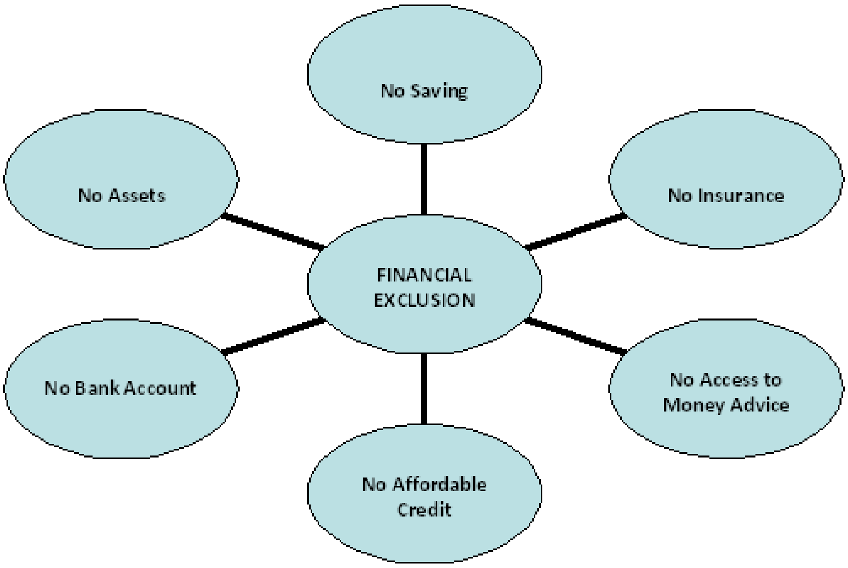
Lack of Financial Services

- No or lack of banks and financial institutions
- Lack proper of information about the financing facilities.
- Poor service history of various banks already present in rural areas.
- High cost of operations in rural areas due to less volume and more number of clients
- Delay in sanctioning of loan by bank due to paper formalities and technical analysis.
- Product does not match with the rural expectations and capacity.

Other Attributes

- Discarded section of the society
- High illiteracy rate among the rural population (especially women)-
- Sections of society excluded from the banking system.
- Rigidity to change the source of financing.

FACTORS OF FINANCIAL EXCLUSION

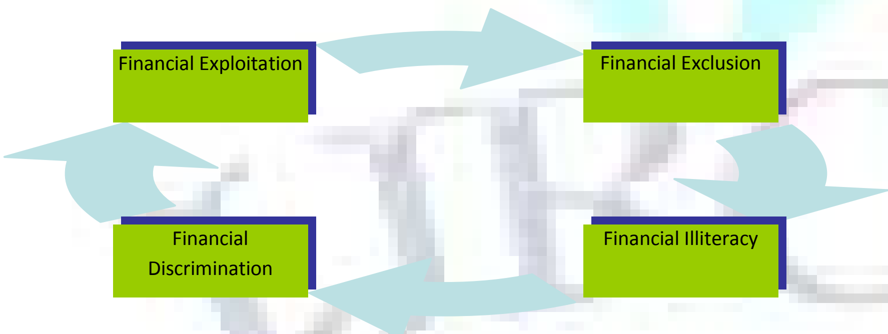


No saving: maximum population in the rural areas is below poverty line and they hardly earn money to satisfy their family hunger, which makes the saving impossible.
No Assets: being BPL the rural population do not have enough assets to keep as mortgage with bank as security to fulfill the terms of bank lending for sanction of loan.
No Bank Account: as per the present study the number of population in rural areas having mobile is more than the bank account holders. This is somewhere due to the less informative approach of banks to the unbanked people.
No Affordable Credit: the banks are somewhere unable to define a clear demarcation between the services provided for urban and rural areas.
No access to Money Advice: due to lack of information about the various loan facilities, deposits options and insurance schemes with the banks the rural people are unable to take the facilities of banking.
No Insurance: now banks are coming up with the facilities of insurance which was not present way back to give the cushion to the farmers and other rural people.

SECTION EXCLUDED FROM BASIC FINANCING

1. Urban-slum dwellers
2. Marginal farmers
3. Landless laborers
4. Oral lessees
5. Self-employed and unorganized sector enterprises
6. Migrants
7. Ethnic minorities, and
8. Socially excluded groups, senior citizens, women and disabled people

VICIOUS CIRCLE OF FINANCIAL EXCLUSION



Indian rural is trapped in the vicious circle of financial exclusion, reason being the high ***illiteracy*** rate which results in narrow and conservative thinking process because of which they always hesitate to accept the formal finance pattern provided by the bank in place of lending from moneylenders. This financial illiteracy leads to financial ***discrimination*** between rural from urban population as former hesitate and fear to accept the formal financing facilities by bank and latter avail the benefits of formal financing. These financially discriminated poor bound to approach their village moneylenders, which leads to ***exploitation***, and increases of ***financial exclusion*** even though the country is coming up with bank branches in under banked and unbanked rural areas for 100% financial inclusion. Due to this *vicious circle* India has 145 million household excluded from banking resulting half of the India un-banked.

FINANCIAL INCLUSION

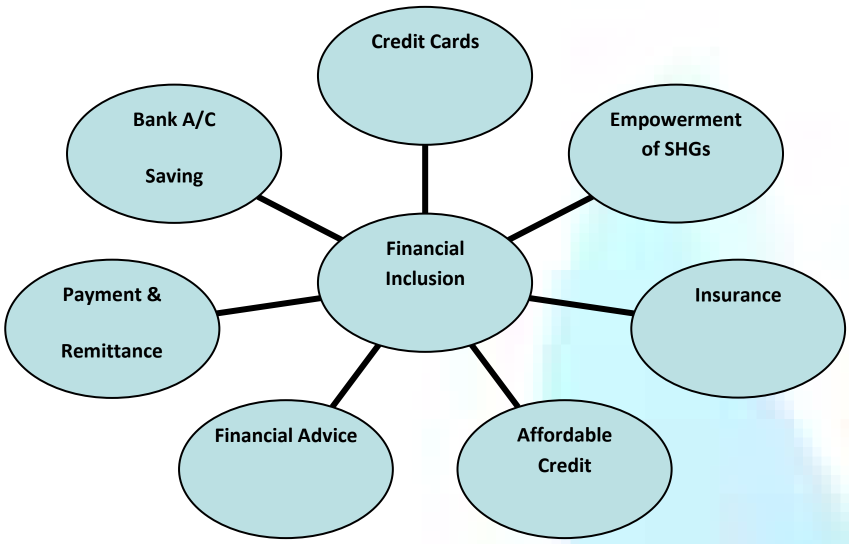
Financial inclusion is very important for the stable and economic growth of any country this can be achieve through active participation of banks. Thus Financial Inclusion is the process of ensuring access to appropriate financial products and services needed by vulnerable groups such as weaker sections and low income groups at an affordable cost in a fair and transparent manner by mainstream institutional players. The Governor of RBI has announced that we need to achieve financial inclusion through the mainstream financial institutions whether by mobile or card.

"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." - NABARD

"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." --- C Rangarajan

On the basis of above definition, financial inclusion is to make people access to the formal financial banking services of saving and borrowing and providing proper financial education to derive the benefits of formal financing. But as per present data only 38 per cent (32,000 branches) of the bank branches of scheduled commercial banks are in the rural areas and only 40 per cent of the country's population has bank accounts.

FACTORS OF FINANCIAL INCLUSION



FINANCIAL INCLUSION – PHASES & STEPS TAKEN BY GOVERNMENT

INSTITUTIONS	EAR	OBJECTIVES
Co-operative banks	1904	Basically to help poor people by opening branches in rural areas
Nationalized banks	1969	To open public sector banks branch in rural areas to provide easily accessible bank facility
Lead Bank Scheme	1970	The lead bank was to act as consortium leader for coordinating the efforts of all credit institutions in each of the allotted districts for expansion of branch banking facilities and for meeting the credit needs of the rural economy.
Regional Rural Banks	1975	It is the combination of the local feel and the familiarity with rural problems which the cooperatives possess and the degree of business organization, ability to mobilize deposits, access to central money markets and modernized outlook which the commercial banks have The institution of Regional Rural Banks was created to meet the excess demand for institutional credit in the rural areas, particularly among the economically and socially marginalized sections
Microfinance	1990	To provide micro-credit to the poor to help them in earning their livelihood by self employed.
Self Help Group	1992	SHG is a group of about 10 to 20 people, usually women, from a similar class and region, who come together to form savings and credit organization. They pooled financial resources to make small interest bearing loans to their members.
Self Help Group-Bank Linkage		Through the SHG-bank linkage program the RBI and NABARD have tried to promote relationship banking, i.e., improving the existing relationship between the poor and bankers
Microfinance Institution		Parties who provide microfinance services, such as loans, micro deposits and micro insurance. They may include microfinance banks, non-governmental organizations
Swarnjayanti gram Swarojgar yojana	1999	SGSY is holistic Scheme covering all aspects of self-employment such as organization of the poor into Self Help Groups, training, credit, technology, infrastructure and marketing. The scheme will be funded by the financial institutions, Panchayat Raj Institutions, District Rural Development Agencies (DRDAs), Non Government Organisation (NGOs),
Committee of financial inclusion	2006	Allowing the use of intermediaries for providing banking and financial services. Through such policies the RBI has tried to improve Financial Inclusion.
Business Correspondent	2009	The RBI approved BC model to approach the interiors where banks cannot be opened. Business correspondents are intermediaries who carry out banking functions in villages or areas where it is not possible to open a branch. These can be NGOs, or individuals of village who will work for spreading awareness of banking facilities and get stipulated remuneration for that.

RBI is keen on achieving 100% financial inclusion for sustaining equitable growth. It has emphasized banks whether public sector, private sector or multinational banks to open or support more and more branches of formal finance in under/un-banked areas, by increasing the reach to remote areas by which not only rural people will be benefited by loan at lower interest rate, interest on saving, other investment opportunities, insurance, e-card, kisan credit card but banks business will also increase by connecting to people.

THE PROGRESS OF RBI IN SPREADING FINANCIAL INCLUSION

Number of No-Frill Accounts	28.23 million (as on Dec. 31, 2008)
Number of rural bank branches	31,727 constituting 39.7% of total bank branches (as on June. 31, 2009)
Number of ATMs	44,857 (as on May 31, 2009)
Number of POS	4,70,237 (as on May 31, 2009)
Number of Cards	167.09 million (as on May 31, 2009)
Number of Kisan Credit cards	76 million (Source: CMIE publication 2007-08)
Number of Mobile phones	403 million (as on Apr.30, 2009)– out of which 187 million (46%) do not have a bank account (Source: Cellular Operators Association of India

A Presentation by Dr. K.C.Chakrabarty, Deputy Governor, Reserve Bank of India

No doubt like other nation in world India is also striving hard for financial deepening to make the country financially inclusive which ultimately leads to economic growth. The R.B.I. has given

- RBI is pushing banks to provide basic banking services in villages with a population of 2,000 and above by 2012 and those with a population of less than 2,000 over the next three to five years.
- RBI issued a circular in 2006 allowing the use of intermediaries for providing banking and financial services. Through such policies the RBI has tried to improve Financial Inclusion.
- RBI has told chiefs of both private and public sector banks that in addition to allowing the underprivileged no-frills accounts without a minimum balance requirement, banks should also provide them loans through an overdraft facility. This direction was given with the objective of achieving financial inclusion.
- All banks are urged to give wide publicity to the facility of such no frills account printed material can be used by banks in local languages.
- RBI has asked for a three-year plan on the extent of financial inclusion they achieve by 2011. This is the first time RBI has asked banks to give a roadmap on financial inclusion. So far, RBI has been asking for roadmap from banks on commercial matters such as capital raising plans.
- The 1990s also saw introduction of self-help groups – bank linkage program and launch of Kisan credit cards in the country. The present phase of pursuing financial inclusion as a declared policy objective started in 2005.
- The Information and Communication Technology (ICT) are now make available to penetrate the formal financial sector in widespread unbanked areas in a cost effective way
- KYC (Know your Customer) norms were relaxed for people intending to open accounts with annual deposits of less than Rs. 50,000.
- Banks providing kisan credit card to every household in a village with a population of over 2,000.
- General Credit Cards (GCC) were issued to the poor and the disadvantaged with a view to help them access easy credit. General purpose Credit Card (GCC) facility up to Rs. 25000 at rural & urban branches. In this facility Withdrawal is allowed up to limit sanctioned based on household cash flows, it does not require any security or collateral.
- RBI on June 2007 has started providing information on banking services through multilingual website in 13 Indian languages to make the e- banking concept more user friendly.
- In April 2006 RBI has announced the policy of identifying one district in each state by State Level Business Correspondent for 100% financial inclusion – 13 district are identified in NER for Financial Inclusion – RBI evaluation of progress through an external agency
- In January 2006, the Reserve Bank permitted commercial banks to make use of the services of non-governmental organizations (NGOs/SHGs), micro-finance institutions and other civil society organizations as intermediaries for providing financial and banking services.

Nearly forty years after nationalization of banks, 60% of the country's population does not have bank accounts and nearly 90% do not get loans, RBI and other financial institution are putting efforts to the financial inclusion but somewhere the financial inclusion activity is not taking pace as it should be, reason being there are various extraneous factors at micro and macro level which are effecting both the rural population and banks. The various factors affecting the two main ends (bank & rural poor) are as follows:

INTERNAL & EXTERNAL FACTORS RELATED TO RURAL POPULATION

EXTERNAL FACTORS
Bank Formalities
Lack of confidence of Bank
Geographical constraints
Section Disparity/ Inequality
Less Amount of Loan
Opinion Leader
Lack of Availability of Formal Finance
Mortgage Formalities
Financial Illiteracy
Employment

INTERNAL FACTORS
Lack of Education
Gender
Habits
Family Structure
Loan Priorities
Awareness
Prejudice of Individual

Rural Population

INTERNAL FACTORS

- **LACK OF EDUCATION:** the **Sarvashiksha Abhiyan, Adult Education system** started by the government with the view to literate every individual in India but the rural population is still hesitate to go school because of which the illiteracy rate is high in India basically the percentage is high in northern India. This lack of education keeps the individual away from the bank financing.
- **GENDER:** India has currently the second-highest number of financially excluded households in the world. In villages there is a widespread gender difference which deprives women from earning and makes their position in society and home.
- **HABITS:** in rural population men are very much into smoking, drinking and speculation this lead to misutilization of their earnings and they unable to save money for their future security in bank and if they get loan from formal sector they misuse the loan.
- **FAMILY STRUCTURE:** in rural family the number of depending members are more then the number of bread earners, this lead to spending of maximum or full earnings in basic need of the family and left with no amount for saving in banks.
- **LOAN PRIORITIES:** due to illiteracy poor people unable to decide priorities for which they should take loan due to which they somewhere unable to repay the loan and declare as defaulter.
- **AWARENESS:** poor people are in such a vicious circle of poverty that they have no awareness about the various facilities given by the government for their upliftment.
- **PREJUDICE OF INDIVIDUAL:** Distance from bank branch, branch timings, cumbersome documentation/procedures, unsuitable products, language, staff attitude are common reasons due to which poor prejudice that the banking facility is not for them.

EXTERNAL FACTORS

- **EMPLOYMENT:** in rural areas the main source of earning of an individual is agriculture and maximum of them do not have their own land so they work on "Adhiya" and due to slow infrastructure development other employment are not available because of which people do not have sufficient money to meet their basic needs as well as no amount left for making any assets or saving in banks.
- **FINANCIAL ILLITERACY:** the reach and frequency of the financial literacy provided by the banks and government is not reaching to the under-banked and unbanked villages because of which they prejudice that banking facilities are for urban or rich people in the villages.
- **BANK FORMALITIES:** the banks have number of formalities like identity card, guarantor, KYC (know your customer), sanction limit etc. prior to sanctioning of loan because of which the rural people hesitate and panic to avail the facility of financing from banks.
- **LACK IN AVAILABILITY OF FORMAL FINANCE:** at present only 38% number of villages has been covered by co-operative, commercial and regional rural banks and today also there are number of villages where there is no bank to avail the formal financing facilities.
- **OPINION LEADERS:** when an individual took monetary decision he/she always take advice from friends and relatives, in case of the rural the possibility of financially literate and convinced opinion leader is less.
- **LOAN AMOUNT:** poor people unable to satisfy their need with the help of loan amount sanctioned by the bank reason being prices are directly proportional to inflation but the revision of the loan amount to be sanction to the farmers or other allied workers do not get revised all the time with change in inflation.
- **INEQUALITY PROBLEM:** in rural areas people still follow caste & society due to which person from lower society deprived from education and formal loan due to the pressure of high society people in villages.
- **LACK OF CONFIDENCE OF BANKS:** the banks are prejudice that people in rural areas misuse loan and unable to repay loan which lead to increase in NPA of their balance sheet, that's why they sanction lower share for the rural financing.
- **GEOGRAPHIC CONSTRAINTS:** some villages are Remote, hilly & sparsely populated areas with poor infrastructure and difficult physical access due to which the banks find it difficult to open branches in these geographic constraints.

INTERNAL & EXTERNAL FACTORS RELATED TO BANKS OR FINANCIAL INSTITUTIONS

EXTERNAL FACTORS
RBI Rules and Regulations
Competition
Business Correspondents
Dormant No Frill Account
Lack of Confidence of Rural People
Infrastructure Constraints
Inflation

INTERNAL FACTORS
Priority Clients
Existing NPA
Employee Resistance
Cost-Benefit Ratio
Transaction Cost
Anticipated Profit

Bank

INTERNAL FACTORS

- **TRANSACTION COST:** banks have to incur high transaction cost for financing rural people with small amount of loans.
- **COST – BENEFIT RATIO:** the banks need to earn profit to survive in the competitive world, the bank sanction the amount of loan extended to the rural branches on the basis of cost benefit analysis.
- **EMPLOYEE RESISTANCE:** the trained bank officers hesitate to move to rural area branches due to lack of infrastructural facilities, due to which the rural branches somewhere lack in experience staff.
- **EXISTING NPA:** rural poor are dependent on natural climate for the cultivation so when the climate is not as per the crop they suffer loss and fail to pay loan installment or repay loan amount which increase the NPA of banks balance sheet.
- **PRIORITY CLIENTS:** banks give more weight to the regular customers, high net worth customers or the customers having good past record with bank because those customers regular in use of bank services (which generate the revenue) and also make timely repayment of loan.
- **ANTICIPATED PROFIT:** every year banks made their anticipated expenses and revenue statement to determine the profit to be earn in concerned year, so to earn the anticipated profit bank provide the bank financing firstly to those who really contribute to the profit of the banks than the rural areas where the security of earning profit is less.

EXTERNAL FACTORS

- **RBI RULES AND REGULATIONS:** to control inflation RBI increase the CRR (cash reserve ratio) and SLR(statutory liquidity ratio) due to which the banks left with less amount to be allocated for urban and rural financing.
- **COMPETITION:** banks to sustain in competitive scenario give more substance to the urban population to capture major population which is financially literate and aware about the banking services, this somewhere neglect the rural poor.
- **INFRASTRUCTURE CONSTRAINTS:** number of villages in India does not have good roads, electricity supply, telephone and other infrastructure which lead to non opening of branches at remote rural areas and the population of those villages deprived of the formal finance system.
- **RURAL MISCONCEPTIONS:** rural population have a myth that banks are only for city people or people already have money and assets can avail the facility of banks. They also feel cumbersome due to paper formalities of the banks that's why they hesitate to approach banks.
- **DORMANT NO – FRILL ACCOUNT:** government has ordered banks to open no-frill account with minimum balance or no balance in the rural branches so that poor people start saving and availing various services, but in actual number of accounts has been opened but the rural people have not accessed then even a single time.
- **BUSINESS CORRESPONDENT:** the banks can not open branches in every village due to cost constraint to overcome this problem without depriving the rural poor from formal financing the banks appoint BC in those areas, but the coverage or acceptance of banking facility in that area become the responsibility of BC, who some time due to less commission does not take much effort.

From the above mentioned factors which pose as hindrance for Financial Inclusion, the following recommendations are proposed which will help to minimize the lacunas.

RECOMMENDATIONS

- The banks prior to open any branch in unbanked area can spread awareness among villagers through panchayat people as these are very strong opinion leaders for villagers.
- The government can bring awareness of banks schemes to rural by extending projects to rural management colleges for internship program. The students can bring awareness through role play, street play, and consultancy desk.
- The RBI can also lay down annual targets to banks for accomplishing financial inclusion.
- The bank can provide financial literacy to the village people by taking sessions during panchayat. This help in making maximum villagers aware of the banks facilities.
- The banks can keep some portion of loan for rural women so that they also take loan for self employment as well as bank's percentage of NPA will also be decrease as women are more sincere in repaying loans.
- There should be proper assistance to villagers at the time of filling of form for loan and enclosing of various proofs for this they can keep management trainees.
- The National Channel Doordarshan can be used by government to broadcast of the types of loans available for the farmers and the name of banks giving those loans.
- At the time of waiver-off, the full information of the person applying for waiver should be available so that only those who are unable to repay the loan could get the facility.
- The banks can touch no-frill account holder and explain them the benefits of interest earning even on the minimum amount of saving, the facility of taking loan against the saving account and general credit card.

CONCLUSION

No doubt financial inclusion is very important to uplift rural for the overall economic development of India, through this paper an attempt has been made to highlight various determinants from the perspective of rural population (like less amount of loan, financial illiteracy, geographical constraints etc.) and banks (like transaction costs, NPA, RBI regulations, etc) which are working as obstacles in implementing policies and schemes lay by RBI and government.
This paper tried to bring forth the various problems of rural population due to which they kept aloof from getting formal finance from banks. This paper tried to contributes various recommendations through which banks and R.B.I. in large can accelerate the pace of financial inclusion in under banked and unbanked rural areas.

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