

# INTERNATIONAL JOURNAL OF RESEARCH IN COMMERCE, ECONOMICS & MANAGEMENT

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# CONTENTS

Sr. No.	TITLE & NAME OF THE AUTHOR (S)	Page No.
1.	PERCEPTUAL MAPPING OF STUDENTS FOR ENGAGEMENT IN CLASS: AN EMPIRICAL STUDY OF STUDENT APATHY TOWARDS HIGHER EDUCATION <i>DR. D. S. CHAUBEY &amp; K. R SUBRAMANIAN.</i>	1
2.	EFFECTIVE FOOD PACKAGE DESIGN AND CONSUMER ATTRACTION <i>DR. R.RAJESWARI &amp; T.RAMYA</i>	9
3.	DO ASIAN STOCK MARKETS INTERACT? <i>PRASHANT JOSHI</i>	14
4.	A STUDY ON CUSTOMER MOBILE APPLICATIONS USAGE PATTERN AND THEIR SATISFACTION <i>ABDULKHADAR J. MAKANDAR, SANJAY HANJI, BRIJMOHAN VYAS &amp; DR. M. M. MUNSHI</i>	19
5.	EVALUATION OF RAJIV AAROGYASRI SCHEME IN ANDHRA PRADESH AND SURVEY OF PATIENTS OPINION <i>DR. D. SHREEDEVI</i>	25
6.	STUDY ON THE TIME DURATION OF INTERNSHIP IN HOTEL MANAGEMENT COURSE CURRICULUM <i>DR. ANIL CHANDHOK &amp; DR. BHAVET</i>	30
7.	HUMAN RESOURCE MANAGEMENT MODEL FOR NEW GLOBAL ECONOMY: OVERVIEW <i>DR. GEETANJALI V. PATIL, DR. V. S. PURANIK &amp; RAMESH S. NAIK</i>	40
8.	CUSTOMER EXPECTATIONS AND PERCEPTIONS ON SERVICE QUALITY IN BANKING SECTOR: WITH SPECIAL REFERENCE TO PUBLIC SECTOR BANKS IN RAJASTHAN REGION <i>DR. POONAM MADAN &amp; PREETI SHARMA</i>	45
9.	DETERMINANTS OF FOREIGN DIRECT INVESTMENT INFLOWS IN THE TRANSITION ECONOMIES OF EUROPEAN UNION <i>YILMAZ BAYAR &amp; HASAN ALP OZEL</i>	49
10.	INCIDENCE OF POVERTY AMONG THE RURAL LABOUR HOUSEHOLDS: A STUDY IN CHITTOOR DISTRICT OF ANDHRA PRADESH <i>DR. TRIPURANENI JAGGAIAH &amp; DR. TRIPURANENI BALAJI</i>	54
11.	FINANCIAL BEHAVIOUR Vs. PERSONALITY TYPES: A MECHANISM TO IMPROVE CUSTOMER RELATIONSHIP MANAGEMENT <i>NATARAJ B &amp; MADHUMITHA T</i>	58
12.	FINANCIAL INCLUSION: AN INSTRUMENT THAT PULLS MILLIONS OF RURAL INDIANS OUT OF THE CLUTCHES OF POVERTY - A REVIEW <i>ANSHA JASMIN S.N</i>	65
13.	POVERTY ERADICATION THROUGH INTEREST FREE FINANCE: A CASE STUDY <i>AHSANATH.MK</i>	69
14.	EMPLOYEE RETENTION STRATEGIES: AN OVERVIEW <i>RUHANI SOHAL</i>	72
15.	A STUDY ON EMPLOYEES' INVOLVEMENT TOWARDS EFFECTIVENESS OF TEAM WORK IN GLOBAL SCENARIO <i>K. KALAIVANI &amp; P. SASIKALA</i>	75
16.	COMPARATIVE STUDY OF UNORGANISED AND ORGANISED RETAIL: THE CASE OF INDIAN GROCERY MARKET AT NCR <i>SHASHANK MEHRA &amp; MOONIS SHAKEEL</i>	78
17.	HAPPINESS MAKES GOOD BUSINESS SENSE <i>PRAKRITI CHAWLA &amp; SHILPI ARORA</i>	85
18.	RISK MANAGEMENT PRACTICES IN YES BANK <i>DR. N. FATHIMA THABASSUM</i>	89
19.	THE EFFECT OF THE CHANGE IN SHORT-RUN FOREIGN DEBT STOCK IN TURKEY ON THE OUTPUT VOLATILITY <i>DR. OZGE UYSAL SAHIN &amp; DR. SEVDA AKAR</i>	93
20.	A CASE STUDY ON SELF-HELP GROUPS: MARKETING PERSPECTIVES & LEARNING <i>SOUVIK ROY &amp; CHAITALI DATTA</i>	98
	<b>REQUEST FOR FEEDBACK &amp; DISCLAIMER</b>	101

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## FINANCIAL INCLUSION: AN INSTRUMENT THAT PULLS MILLIONS OF RURAL INDIANS OUT OF THE CLUTCHES OF POVERTY - A REVIEW

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### ABSTRACT

*This article provides a review of Financial Inclusion Programme - an initiative to provide financial services to the rural Indians. How Financial Inclusion pulls millions of rural Indians out of the clutches of poverty is also explained in detail. RBI has taken several initiatives such as providing No-Frills Account, started Financial Literacy Centre's, simplified KYC norms and branch authorization policy, deployed Business Correspondents, issued Kisan Credit Cards and General Credit Cards etc. How far India reached in achieving the financial Inclusion path is analysed through CRISIL Inclusix, RBI Working Paper Study And World Bank Access Survey. Most of the South Indian states achieved high Financial Inclusion but still its proper and speedy implementation is required in other states in India.*

### KEYWORDS

Financial Inclusion, CRISIL Inclusix, No-Frills Account, RBI, Kisan Credit Cards and General Credit Cards.

### INTRODUCTION

*If the misery of the poor be caused not by the laws of nature, but by our institutions, great is our sin"*

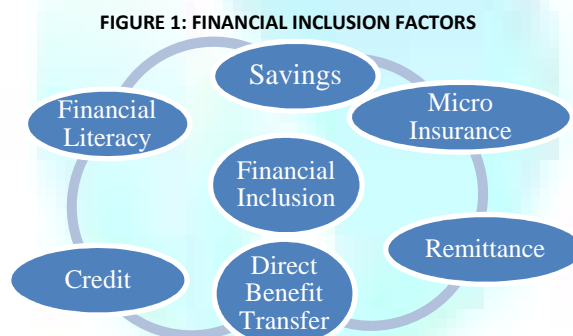
*– Charles Darwin*

Banking system is an important constituent of overall economic development as it improves capital formation through mobilization of the savings of the country. As India is predominantly a rural economy efforts have to be made for inclusive growth i.e. growth with equity. For inclusive growth Financial Inclusion has to be given upper most priority. Government of India and RBI have been putting continuous efforts to promote financial inclusion as the important national objective of the country.

Financial inclusion will positively impact the lives of rural Indians and pulls millions of them out of the clutches of poverty. It will provides them with a formal identity, access to banking products and services, opportunities to build savings, avail credit, make investments and equips them to meet emergencies.

The Committee on Financial Inclusion (Chairman: Dr. C.Rangarajan, 2008) has defined Financial Inclusion as '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 impact financial products and services provided by banks on the lives of rural Indians are explained below:



**Savings:** The savings habit of the vulnerable groups can be improved through financial inclusion as RBI has advised all banks to open Basic Savings Bank Deposit (BSDA) Accounts with very minimum balance or nil balance, with fewer charges and with facility of receipt or deposit of money through, electronic payment channels, ATM. For their deposits in savings account interest will be allowed and small overdraft facility is also provided to that account. Know your customer norms were relaxed for small accounts from August 2005 and banks were also permitted to take any evidence as to the identity and address of the customers to their satisfaction, so that customers can open account easily. A pure savings account, which facilities recurring or variable recurring deposit, improves the savings habit of the low income people as there is no limit on the number of deposits that can be made in a month.

**Credit:** Availability of adequate, low cost and transparent credit from the regulated or formal banking system protects the vulnerable sections from the inhuman money lenders charging high interest rate and helps them in starting business themselves and getting self-employed. Under priority sector lending, banks are required to lend 40 percent of their loans to agriculture and economically weaker sections of the society. NSSO 59<sup>th</sup> Round Survey Results says that 73 percent of farmer households in India are financially excluded from formal sources of credit. RBI advised Banks to issue Kisan Credit Cards (KCC) and General Credit Cards (GCC) to small farmers for meeting their credit requirements. General Credit Card facility enables them to raise credit up to Rs.25000. RBI has also deregulated interest rates on small value loans to encourage greater lending to the poor.

**Direct Benefit Transfer:** The objective of Direct Benefit Transfer is to ensure that the subsidies as well as the money under various developmental schemes of both central and state government reaches directly to the beneficiaries bank account without any bureaucratic delay. Aadhaar enabled bank account is used for direct transfer of social security benefits such as pensions, scholarship, NREGA wages, healthcare, subsidy for LPG, kerosene, fertilizers etc

**Micro-Insurance:** Micro insurance is a form of insurance suitable for the low income and poor people with flexibility of payment through cash, starting from as little as Rs. 100/- every month and insurance of Rs. 50,000 per person. Life insurance and non-life insurance provided to the vulnerable sections help them in facing the financial crises or manage risk arising particularly in times of natural calamities and financial burden due to health problems. Life insurance products not only provide social security to the insured but also enable them to use the same as a savings cum wealth creation tool. Non- life insurance provided on crops, livestock, buildings, vehicles machineries etc. helps them in covering the loss related to that particular asset. Micro insurance is provided to meet the future unforeseen and unexpected financial needs of the poor.

**Remittance:** Money remittance or transfer is required for migrant labourers working in another city or country to improve their life due to poverty. These populations are being exploited by the money changers (Hawala) as they charge high to provide remittance facility. On 14<sup>th</sup> June 2014 RBI Deputy Governor H.R.Khan reported "We are also coming up shortly with what could be payment bank because there is huge potential for financial inclusion with focus on remittances by involving payment system product." Fixed cost of sending remittance through formal financial institutions make lump sum amount transfer, which in turn might increase the demand for savings deposit accounts. At the same time banks might extend loans based on information on the income flow of recipient household. Remittance transfer pushes people to financial services available to them.

**Financial Literacy:** Financial inclusion and financial literacy go hand in hand. Financial education promotes awareness among the people regarding the need and benefits of financial services provided by banks and other financial institutions. There are nearly 800 Financial Literacy Centers set up by banks to educate the financially excluded population about the general banking concepts to enable them to make informed financial decision.

**RBI INITIATIVES**

Over the years several steps, such as Co-operative movement, setting up of State Bank of India, Nationalization of Banks, Establishment of Regional Rural Banks, Lead Bank Schemes, Self Help Group-Bank linkage programme etc., have been taken by RBI to increase access to financial services by priority sector of the economy. A committee called Financial Inclusion Advisory Committee, headed by deputy governor RBI, has been formed on October, 2005 to ensure accessible financial services and to increase speed of financial inclusion in India. RBI initiatives to implement Financial Inclusion programme are:

**No Frills Account (NFA's):** Basic banking no frills account is with nil or minimum balance as well as charges that make such accounts accessible to vast sections of the population. Banks have advised to provide small overdraft in such accounts.

**Relaxation on Know your Customer norms:** Know Your Customer norms were relaxed for small accounts (account balance not exceeding Rs. 50, 000 and credit not expected to exceed Rs. 100000 in a year) from August 2005 and banks were also permitted to take any evidence as to the identity and address of the customers to their satisfaction, therefore customers can open account easily.

**Usage of Regional language:** The banks are required to provide all the material related to opening accounts, disclosures etc. in the regional languages.

**Engaging Business Correspondents:** RBI has permitted banks to engage Business Facilitators (BFs) or Correspondents (BCs) as intermediaries for providing banking and financial services to far flung areas of the country. BC model allows banks to provide door step delivery of services especially to do cash-in and cash-out transactions, thus addressing the last mile problem. The BC model facilitates receipt and delivery of small value remittances, disbursement of small value credit, collection of interest and principal, collection of small value deposits, sale of other financial investment products like mutual funds and insurance.

**Opening of branches in rural areas:** On May 2013 banks have been mandated to open at least 25 percent of the branches in unbanked rural areas. In order to facilitate this mandate banks have been advised to open small intermediary brick and mortar structures between the base branch and the unbanked villages. This idea is to ensure efficient delivery of services, channelize benefits provided by government (DBT/EBT), redressal of customer grievances and closer supervision of Business Correspondents (BC's) operations.

**Simplified Branch Authorisation:** RBI has simplified and relaxed branch licensing norms considerably. Now banks are free to open branches in areas with population less than 1 lakh under general permission, subject to reporting.

**Established Bharatiya Mahila Bank:** In order to address gender related aspects of empowerment and financial inclusion RBI issued license to India's first Women's bank called Bharatiya Mahila Bank Ltd. on September 2013.

**Credit cards:** RBI has advised all Scheduled Commercial Banks including Regional Rural Banks to provide General Purpose Credit Cards as well as Kisan Credit Cards facility at their rural and semi urban branches. Kisan credit card scheme is to provide adequate and timely credit from the banks to the farmers for cultivation and other needs.

**Restructured SGSY:** To promote financial inclusion Ministry of Rural Development, Government of India has restructured Swarnajayanti Gram Swarozgar Yojana (SGSY) as the National rural livelihood mission with effect from April 2013. It will ensure that at least one member from each identified rural poor household, preferably a women, is bought under the Self Help Group network in time bound manner. Under this scheme poor are provided with requisite skills for managing their institutions, linking up to the market, managing their livelihoods and enhancing their credit absorption capacity and credit worthiness.

**Payment system:** RBI Governor Raghuram Rajan announced approval of the payment system that shall enable people maintaining no bank accounts and receiving remittances to withdraw funds from Automated Teller Machine or ATM.

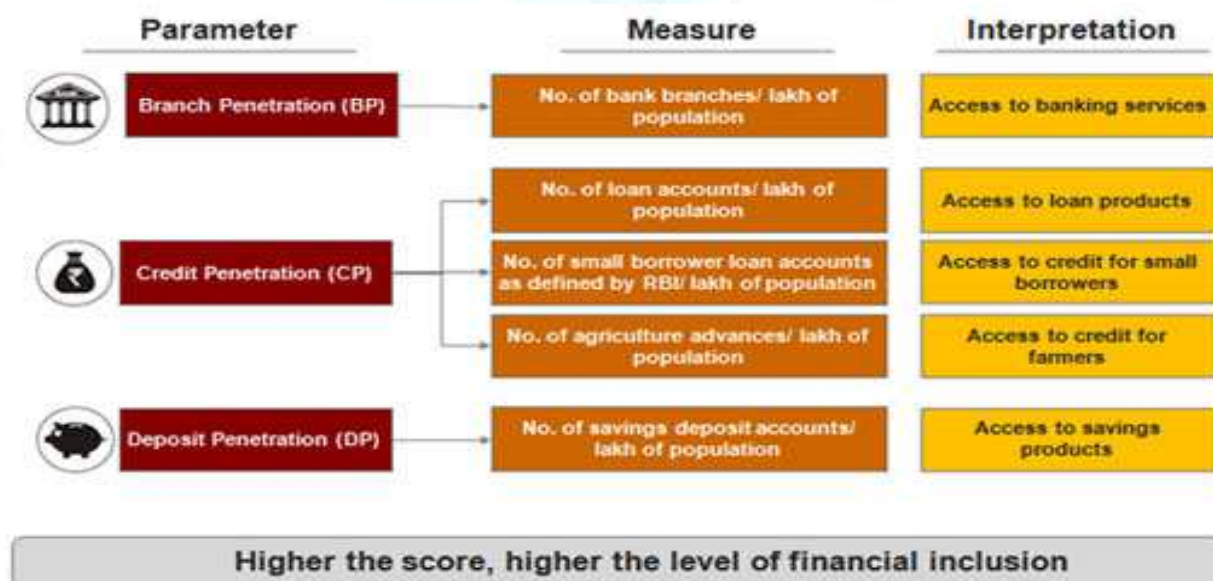
**Leveraging on technology:** As banking services provided through traditional brick and mortar model is expensive for banks, RBI suggested banks to adopt and leverage technology to attain greater reach and penetration, while keeping the cost of providing financial services to minimum. Technological advances in banking services include ATM, mobile banking, internet banking, Electronic fund transfer etc.

**Swabhimaan Campaign:** Swabhimaan is an initiative taken by Union Government and the Indian banks to bridge the gap between the rural and urban Indians. It aims at providing branchless banking services through the use of modern technology or by using the service of business correspondents. This initiative enables government subsidies and social security benefits to now be directly credited to the accounts of the beneficiaries so that they could draw the money from the business correspondents in their village itself.

**PRESENT POSITION**

On 25<sup>th</sup> June 2013, CRISIL, India's leading credit rating and Research Company launched an index, Inclusix, to measure the status of financial inclusion in India at national/regional/ state/ and district levels. CRISIL inclusix, whose methodology is similar to other global indices, measures financial inclusion on three critical parameters of basic banking services- branch penetration, deposit penetration and credit penetration – together into one single metric. The index uses parameters that focus only on the number of people whose lives have been touched by various financial services, rather than on the amount deposited or loaned. It is a relative index measured on a scale of 0-100. CRISIL Inclusix parameters to measure status of financial inclusion is shown below:

**FIGURE 2: CRISIL FINANCIAL INCLUSION PARAMETERS**



Source: www.CRISIL.com: CRISIL comprehensive financial inclusion index. Inclusix parameters



- CRISIL Inclusix at all India level stood at a relatively low –level of 40.1 for 2011 and 37.6 for 2010.
- Southern region leads in terms of financial inclusion in the country with a score of 62.2 for 2011. Western region (38.2) is a distant second, and is followed by Northern (37.1), Eastern (28.6) and North-Eastern Region (28.5) respectively.
- Smaller states (population < 3 crore) and union territories such as Puducherry (rank 1), Chandigarh (2) and Goa (4) perform better than the larger states due to higher urbanization.
- Amongst larger states (population > 3 crore) Kerala has the highest score with 76.1 followed by Andhra Pradesh and Tamil Nadu with 61.3 and 60.5 respectively. Top five are Puducherry, Chandigarh, Kerala, Goa, and Delhi.
- Most of the districts in southern region (103/107) have score higher than all India average. Kerala has the highest proportion of districts (11 out of 14) in the list of top 50 scoring districts. The top five districts are Pathanamthitta (96.2), Karaikal, Thiruvananthapuram, Ernakulam, and Kottayam.

**RBI Working paper study:** Sadhan Kumar worked out an index on financial inclusion 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). It indicates that Kerala, Maharashtra and Karnataka have achieved high financial inclusion (IFI > 0.5).

FIGURE 3: FINANCIAL INCLUSION INDEX WORKED OUT BY SADHAN KUMAR



Source: RBI working paper on financial inclusion in India: A case study of West Bengal by Sadhan Kumar Chattopadhyaya

**World Bank Access Survey Result:** On the basis of world bank access survey result it would be observed that in India, financial inclusion measured in terms of bank branch density, ATM density, bank deposit to GDP and bank credit to GDP are quite low as compared to other countries in the world.

Table 1: Select Indicators of Financial Inclusion, 2011

S.No	Country	Number of Bank Branches	Number of ATMs	Number of Bank Branches	Number of ATMs	Bank Deposits	Bank Credit
		Per 1000 KM		Per 0.1 Million		as % to GDP	
1	India	30.43	25.43	10.64	8.9	68.43	51.75
2	China	1428.98	2975.05	23.81	49.56	433.96	287.89
3	Brazil	7.93	20.55	46.15	119.63	53.26	40.28
4	Indonesia	8.23	15.91	8.52	16.47	43.36	34.25
5	Korea	79.07	...	18.8	...	80.82	90.65
6	Mauritius	104.93	210.84	21.29	42.78	170.7	77.82
7	Mexico	6.15	18.94	14.86	45.77	22.65	18.81
8	Philippines	16.29	35.75	8.07	17.7	41.93	21.39
9	South Africa	3.08	17.26	10.71	60.01	45.86	74.45
10	Sri Lanka	41.81	35.72	16.73	14.29	45.72	42.64
11	Thailand	12.14	83.8	11.29	77.95	78.79	95.37
12	Malaysia	6.32	33.98	10.49	56.43	130.82	104.23
13	UK	52.87	260.97	24.87	122.77	406.54	445.86
14	USA	9.58	...	35.43	...	57.78	46.83
15	Switzerland	84.53	166.48	50.97	100.39	151.82	173.26
16	France	40.22	106.22	41.58	109.8	34.77	42.85

Source: Financial Access Survey, IMF; Figures in respect of UK are as on 2010

**CONCLUSION**

Reserve Bank of India has planned NPR/ Aadhaar- linked bank account for all adults of India by January 2016 to meet its commitment on financial inclusion. It will greatly transform India by preventing the poor people falling into debt- traps of unlawful money lenders, cashless transactions, elimination of poverty and corruption. If financial inclusion programme is implemented properly it will benefit millions of small and marginal farmers and rural artisans in far flung areas of our country by providing them easy access to credit at lower rates and save. The success of banks cannot be measured simply in terms of profit their banking operations generate but it is equally about addressing the financial needs of various stakeholders. To attain inclusive growth banks have to protect the customers through improved awareness and better grievance redressal mechanism. In a fast growing country like India the poor are the middle class of tomorrow and banks can find a remarkable opportunity for their development. Therefore it can be concluded that Financial Inclusion is an opportunity rather than an obligation which will eradicate the poverty that hit the vulnerable section of India.

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