# INTERNATIONAL JOURNAL OF RESEARCH IN COMMERCE, ECONOMICS & MANAGEMENT

IJRCM

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   RESEARCH METHODOLOGY

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# A REVIEW OF ECONOMIC AND FINANCIAL INCLUSION IN NORTH EASTERN STATES OF INDIA

*DR. SANJAY TUPE*
*HEAD*
*DEPARTMENT OF BANKING & FINANCE*
*B. Y. K. COLLEGE OF COMMERCE*
*NASHIK*

**ABSTRACT**

*This paper begins with an introduction to inclusive development and financial inclusion. Further, it reviews the macro economic status of NES and compared it with all India macroeconomic parameters. To understand the economic position of these states, various broad macroeconomic parameters are used in this paper. To know the process of financial inclusion and it status; we focus on the flow of deposit and credit state wise and compared it with all India C-D ratio and takes stock of branch banking area and population wise. This paper tries to communicate to policy makers for devising suitable policy for increasing the depth of financial inclusion. To make dent over the backwardness of NES in all respect, an integrated policy of development should put in place for infrastructure development and to harness the local potential so that food processing, wood products and traditional textile industries can be developed on a large scale. To increase the access of NES to other parts of India there is need to build strong air and road network which can increase the potential for marketing locally manufactured product. At last, initiative needs to be taken for stepping up agricultural productivity along with diversification into horticulture, floriculture, and animal-husbandry. All these efforts may push further the inclusive growth and financial inclusion in NES.*

## KEYWORDS
Banking Network, Credit Deposit Ratio, Financial Inclusion, Inclusive Growth, Macroeconomic -Parameters, North Eastern States.

## I. INTRODUCTION

North Eastern States (NES) are neglected from the mainstream of planning despite these states being endowed with natural resources. The degree of backwardness is high in these states (Planning Commission, 1981). However, Government of India is helping them through sizeable resources transfer and giving boost to industrialization and tourism in NES. The performance of NES is poor in respect of inclusive growth and financial inclusion. The concept of Inclusive growth or inclusive development is used interchangeably. Inclusive development encompasses increase in personal living standard, reduction in poverty and economic inequality along with infrastructure development in the region or country. It gives strength to an individual for making him economically independent. A socio-economic speed of development of economy as a whole or a region in particular is depending on the availability of all kinds of infrastructure. Infrastructure reduces transaction cost and risk involved in business and facilitate toward achieving minimum standard of living to an individual. Infrastructure is a composite term which covers presence of physical assets and various kinds of services together. Among various kinds of infrastructure, active presence of financial infrastructure is necessary for rapid economic progression of a country or region.

Economic inclusion is a wider term which comprises of various aspects of enriching human well- being. Economic inclusion facilitates to human beings to live comfortably by various ways and it makes them economically and socially independent. Inclusive growth is an essential ingredient of planning in developing countries. However, in broad perspective of macro planning, needy section of the society is always neglected from the outcome of development planning. It is also observed that underprivileged section of the society do not get the benefits of planned schemes of welfare. Hence, a concept of inclusive growth comes into limelight, and it has been in the debate since introduction of new economic reforms in the many developing countries and in India too. The necessity of inclusive development is felt on urgent basis even though India implemented new economic policies for two decades.

Presently, three kinds of models of financial inclusion are being practiced in India: 1) People movement group based model: some NGO's fall in this category. They do not remain dependent on the government or banks for financial support. It is a community based movement, if there is need of intervention from the outside agency; people take such decision collectively and consciously. 2) Self Help Group Model: Initially, people's movement is already present and intervention from the government side is expected in this model. Later, it turns into the form of self help group. This kind of model is a supply driven which addresses the institutional and physical infrastructural needs of the members of self help group and offers them standard supply side solution. 3) Market based Model- In which business is seen as an opportunity. Accordingly, credit is delivered through an efficient delivery model. This approach is of more than a decade old. The institutions engaged in this mode are known as microfinance business institutions that often charges high interest rate.

Despite the comprehensive banking network and financial system in India, services and product delivered by banking institution are not yet reached to underprivileged sections of the society, marginalized groups, and slum dwellers in urban and rural masses. Regardless of all the efforts directed for banking spread in India, only 35.5% of the total households in the country were availing banking services, while this proportion can be further divided as 49.5% in urban areas and 30.1% in rural areas (RBI, 2010). It is imperative to tap saving of rural and urban households by banks and lend loans to needy people for augmenting their livelihood and make them better-off.

As a part of inclusive growth and development drive in India, opening of savings account in any bank has now been made free and even without cash and with minimum documents. To increase the reach of banking facility to people of all kinds, recently banks have been told to open no balance saving account or no frills account with no or minimum balance in the account. In August 2005, the RBI has announced more simplified KYC norms particularly for poorer section of the society in India to motivate them for opening savings accounts at least with one bank.

This paper begins with meaning of inclusive development and financial inclusion. Section II covers the objectives, data and methodology. Section III reviews the related literatures. Section IV analyses the relative strength of NES region. In the section V, banking network in India and NES region are compared. Section VI concludes the paper with suggestions.

## II. OBJECTIVES, DATA AND METHODOLOGY

This paper reviews the macro economic status of the states fall in the group of NES and compares them with all India macroeconomic parameters. To understand the economic position of these states, various broad macroeconomic parameters are used in this paper. To know the process of financial inclusion and it status; we focus on the deposits collected and credit disbursed in the states area wise and it takes the stock of branch banking area-wise. This paper tries to communicate to the policy makers for devising a suitable policy for increasing the depth of financial inclusion in these states. We use data appeared in the various issues of RBI Monthly bulletin, Hand Book of Statistics on Indian Economy, March 2009-10 and Basic Statistical Returns of Scheduled Commercial Banks in India, Vol. 39, March 2010. This paper uses the review methodology however we have not used advanced statistical or econometric tools due to data constraints pertaining to the theme of this paper.

## III. LITERATURE REVIEW

Survey on access of finance to rural poor people conducted by National Council of Applied Economic Research and World Bank in Uttar Pradesh revealed that bank takes 33 weeks on an average to process loan application and 1/3 rd applicants had paid 10% bribe of the sanction amount loans. Bribe paid to government officials for availing government schemes was observed as near about 40% of the sanction amount (Basu, 2006).

Recently published discussion paper entitled as "Entry of new banks in India", by T. T. Ram Mohan (2010) showed that the entry of industrial houses in banking business is being restricted by various ways. If banks have to focus on financial inclusion, capital requirement for new bank is made Rs. 500 crore and with a condition that sponsored group has to increase capital base to Rs. 1000 crore in next five years. However, the apprehension of this policy is that the task of financial inclusion may look after effectively by retail banks but not big banks whose capital base is over and above Rs. 1000 Crore. The indirect meaning is those new private sector banks will not work for unorganized and underprivileged class of the society in India.

Bhatia and Chattergee (2010) concluded that 1/3 respondents residing in slums tried to open saving account with banks but failed to do so due to rigidities in banking system and paper work. 1/5 th people were saving their surplus money privatively with money lenders. Despite Mumbai being financial capital of India, penetration of banking facilities is very poor in the slum areas of Mumbai.

Sriram (2010) concluded that MF's institutions have serious governance issues that are not being investigated. Many micro finance (MFS) institutions have entered into market in search of profit and now they are competing with their rivals for lending to the poor. However, in the process of lending, they have forgotten the needs of poor and their ability of repayment. Now, these institutions are chasing for targets and numbers. Rakshit (2010) observed that infrastructural bottlenecks and skill shortage in the rural and semi urban areas have limit down the optimal scale of credit disbursement in unorganized sector.

As (Chandrasekhar, 2011) observed that private sector banks' lending to villagers is relatively small, though they are covered under inclusive development scheme. This shows that private sector banks are reluctant to lend these people. Study made by (Subramanian, 2011) on the status of consumption expenditure and poverty in rural India pointed that per capita consumption expenditure of rural people in India was Rs. 68.69 in 1977-78, which rose to Rs.90.35 in 2004-05 by compounded growth rate 1.01%. However, the quintile consumption of the poorest 20% population was Rs.20.14 and Rs.44.90 during the same period. This shows that 20% rural population was living in extremely poor condition and neglected from the ambit of development.

## IV. MACRO ECONOMIC STATUS OF NORTH EASTERN STATES OF INDIA

Macroeconomic indicators are generally used to reveal the economic strength and status of a state. Generally, it includes growth rate of state domestic product, per capita income, size of deficit in the state budget and also the burden of public debt on the state. NES have been understood as backward states in India since independence. Real per capita income is being used as the base of consumption expenditure which reveals the economic status of an individual in the each state.

**TABLE 1: TRENDS IN REAL PER CAPITA INCOME AND NET STATE DOMESTIC PRODUCT** (At 1999-2000 Prices)

| States | Real PCI in 2007-08 | Average growth rate NSDP |
|---|---|---|
| Assam | 15,526 | 4.5 |
| Arunachal Pradesh | 21,582 | 7.3 |
| Manipur | 15,667 | 4.3 |
| Meghalaya | 21,597 | 5.6 |
| Mizoram | 20,688 | 6.8 |
| Tripura | 17,129* | 7.2 |
| Nagaland | 22,493 | 8.2 |
| NES | 20,655 | 6.3 |
| All India | 22,581 | 7.1 |

Source: RBI Monthly bulletin April 2011. * Figure pertains to the year 2006-07.

It can be concluded from the Table 1 that among the all NES, real PCI of Assam, Manipur, and Tripura are found below the NES average real per capita income and lesser by Rs. 5000/- of the all India average real PCI in 2007-08. However, states such as Arunachal Pradesh, Meghalaya, Nagaland's real PCI remains above the NES average. Average growth rate of net state domestic product (NSDP) for the period 2000-01 to 2007-08 is recoded much below in the states of Assam; Manipur was at around 4.3%, which is even lower than NES and all India average growth rate of NSDP. It concludes that among all NES, Assam and Manipur remained on back foot due to the poor performance of agricultural and industrial sectors. In order to bring NES at equal level of all India growth rate plunk, special efforts through sectoral policy of development for these states should be implemented on urgent basis.

Table 2 reveals trends in fiscal indicators such as revenue deficit and outstanding debt. They are viewed as indicators of fiscal discipline. Gross fiscal deficit of NES reveals that in the year 2000-01, it was 6% of GSDP, which subsequently declined to 0.2% in the year 2008-09 and suddenly shot up to 10.5% due to increase in liability on account of implementation of Sixth pay commission and impact of slow down realized in India. The revenue deficit has been started declining from the year 2001-02 due to measures undertaken for fiscal consolidation that resulted into surplus in revenue from 2003-04 to 2008-09.

**TABLE 2: TRENDS IN FISCAL INDICATORS OF NES** (As per cent of GSDP)

| Year | Gross fiscal deficit | Revenue deficit | Primary deficit | Outstanding debt |
|---|---|---|---|---|
| 2001-02 | 6.0 | 2.0 | 2.5 | 37.3 |
| 2002-03 | 4.2 | 0.8 | 0.6 | 37.9 |
| 2003-04 | 3.6 | -0.4 | -0.1 | 42.2 |
| 2004-05 | 4.8 | -0.5 | 1.4 | 43.1 |
| 2005-06 | 1.3 | -3.4 | -1.9 | 43.4 |
| 2006-07 | -0.1 | -5.2 | -3.1 | 40.1 |
| 2007-08 | 0.1 | -5.6 | -2.6 | 38.8 |
| 2008-09 | 0.2 | -6.5 | -2.4 | 41.1 |
| 2009-10 | 10.5 | 0.7 | 7.5 | 40.3 |
| 2010-11 | 7.5 | 0.3 | 4.6 | 37.8 |

Source: Budget Documents of State Government and RBI Monthly Bulletin April 2011. Note: Minus (-) sign indicates surplus.

Although it is a good sign of fiscal discipline but other side of conclusion is that these states might not be spending more on social and economic schemes or may not be inventing in capital assets. Surge in revenue account occurred mainly because of resources transfer from central government to NES and not because of state tax collection efforts. The portion of debt on NES is observed below the 43% of GSDP which is quite good but it also depicts that NESs are not taking risk in investing in infrastructural facilities and state enterprises.

## V. BANKING NETWORK IN INDIA AND NORTH EASTERN STATES

Financial network is the main conduit of transferring resources from savers to users of the funds. It inculcates habit of thrift and act as source of income for depositors. Through this network Social safety payment and all other government payments can be given to beneficiaries. The active presence of financial network is necessary for promoting financial inclusion in underdeveloped countries (Ranjan and Zingales, 1999, Levine, 2005). According to (RBI, 2009) study, near about 49% of the total Indian population is unbanked or virtually has no access of banking facility. Insufficient institutional access to finance increases dependency on non-institutional sources of rural as well as urban population.

*The Expert Group on Indebtedness* (2007) have pointed that out of 90 million households in 2003, 43.4 million (48.6%) were indebted. In addition, the share of non-institutional sources rose from 32% to 39% during the period 1991-2002. This shows that despite implementing financial reforms since 1991 the dependency on money lenders and other sources have increased. The spread of banking facility is measured by looking at number of accounts of depositors and creditors.

It can be seen from the Table 3 that only 30.5% accounts of deposits were operated by rural population and remaining 70% accounts operated by urban based population. Major portion of total deposits i.e. 90.2% were coming from urban and semi-urban including metropolitan based banks. Thus, rural population does not have either access of bank or their personal income was insufficient to save. Hence, banking spread is remained confine to urban centers. Credit accounts statistics pertaining to different population groups are more or less same as the deposit account figures except the metropolitan centers which has 33.3 % credit account. To the maximum extent, credit disbursement activities were centralized at metropolitan based banks. However, rural population has an exposure of credit to the extent of only 7.5%. This shows that either banking institutions were reluctant to give credit to rural population (supply flow of credit) or there might be bottleneck in availing loans from banks in rural areas (demand flow for credit).

In the Table 4, network of bank offices in NES are shown. In the group of NES, out of total 2068 branches of different banks, 53% were located in rural areas and remaining 47% in the urban areas. However, in the states Manipur and Nagaland, number of rural braches was less than 37 in both the states but in Assam 791 were the rural branches.

**TABLE 3: DEPOSITS AND CREDIT OF SCHEDULED COMMERCIAL BANKS POPULATION GROUP WISE IN INDIA UP TO MARCH 2010** (Amount in Rs. Lakh)

| | | **Deposit** | | **Credit** | |
|---|---|---|---|---|---|
| Population group | No. of Offices | No. of Accounts | Amount | No. of Accounts | Amount Outstanding |
| | 1 | 2 | 3 | 4 | 5 |
| Rural | 32,320 | 2241,54,850 | 420337,72 | 361,92,714 | 249276,96 |
| | (37.2) | (30.5) | (9.2) | (30.5) | (7.5) |
| Semi-Urban | 20,601 | 1894,57,206 | 614047,18 | 268,75,601 | 319972,87 |
| | (23.7) | (25.8) | (13.5) | (22.7) | (9.6) |
| Urban | 17,964 | 1523,22,831 | 944992,24 | 160,19,694 | 558531,01 |
| | (20.7) | (20.7) | (20.7) | (13.5) | (16.7) |
| Metropolitan | 16,075 | 1689,34,254 | 2581651,91 | 395,59,873 | 2217388,48 |
| | (18.5) | (23.0) | (56.6) | (33.3) | (66.3) |
| All India | 86,960 | 7348,69,141 | 4561029,05 | 1186,47,882 | 3345169,32 |
| | (100.0) | (100.0) | (100.0) | (100.0) | (100.0) |

Source: 1) RBI Monthly bulletin, 2010 and Basic Statistical Returns of Scheduled Commercial Banks in India, Vol. 39, March 2010.Note: Figure in the parenthesis are percent of All India figures.

The distribution of banks in the various states of NES shows that each 19000 population has one bank against every 14000 people has one bank at all India level. This shows that strength of bank branches in NES region were insufficient to cater to the needs of local people. Among the group of NES states, Assam, Manipur and Nagaland have few bank branches per thousand populations of these states. Average number of banks according to area wise was found in the range of 3 to 4% in NES against the all India banks distribution strength. The inferences appeared from the distribution of banks area-wise can be concluded as NES region has few branches of banks that act as constraint in the process of inclusive development and financial inclusion in the region.

Indian financial system is a bank oriented and dominated by banking institutions. Therefore it is prime supplier of funds to industry, business and agricultural sectors in India. The spread of banking institutions in NES is relatively low compared to other regions of India.

**TABLE 4: BANKING NETWORK IN NES**

| States | Banks | | | | |
|---|---|---|---|---|---|
| | Rural | Urban | Semi-Urban | Population per bank | Total |
| Assam | 791 | 364 | 322 | 21000 | 1477 |
| Arunachal Pradesh | 51 | ---- | 29 | 16000 | 80 |
| Manipur | 35 | 26 | 20 | 33000 | 81 |
| Meghalaya | 126 | 54 | 33 | 12000 | 213 |
| Mizoram | 54 | 30 | 14 | 10000 | 98 |
| Tripura | 114 | 56 | 59 | 16000 | 229 |
| Nagaland | 37 | ----- | 53 | 25000 | 90 |
| NES* | 1208(3.73%) | 530(2.57%) | 530(2.95%) | 19000 | 2268(2.60%) |
| All India | 32320 | 20601 | 17964 | 14000 | 86960 |

Source: Dept of statistics and information of Management, RBI (Latest version). 2) Basic Statistical Returns of Scheduled Commercial Banks in India, RBI, Vol. 39, March 2010..Note: * percent of All India bank offices.

We conclude from the Table 5 that banking penetration is measured by credit deposit ratio which is 27.8 % in NES when all India banking penetration ratio was 59.2% in 2001. After a span of further nine years, the C-D ratio in NES increased to 35.5% and all India C-D ratios reached to 73.3 %. No doubt, C-D ratios increased across the two periods by 7.3% in NES but all India C-D increased more rapidly than NES. Across the states of NES; Nagaland, Tripura have shown lowest C-D ratio and Mizoram has highest ratio 53.2%. Trends in C-D ratio show that the deposit and credit flows are weak in NES due to backwardness of the region caused by negligible industrialization and poor performance of agricultural sector.

**TABLE 5: BANKING PENETRATION IN NES**

| State | C-D Ratio in per cent* | |
|---|---|---|
| | 31st March 2001 | 31st March 2010 |
| Arunachal Pradesh | 12.7 | 27.5 |
| Assam | 32.8 | 37.8 |
| Manipur | 38.9 | 42.1 |
| Meghalaya | 23.5 | 25.6 |
| Mizoram | 16.5 | 53.2 |
| Nagaland | 13.8 | 30.3 |
| Tripura | 20.0 | 30.7 |
| NES | 27.8 | 35.5 |
| All India | 59.2 | 73.3 |

Source: Data is collected from Basic Statistical Returns of Scheduled Commercial Banks in India, RBI, Vol. 39, March 2010, However *C-D ratio is calculated by author.

## VI. CONCLUSIONS AND POLICY SUGGESTIONS

The economic status of NES in context of all India financial and fiscal indicators was found extremely weak during the study period. However, it is not because of lack of natural resources and manpower but it seems to be the non-implementation of regional plan and special strategy for fostering industrial development in these states. There is ample scope for developing tourism sector in NES. The interplay between agricultural and industrial development can promote inclusive growth in these states. The spillover effect of industrialization and tourism development would act as catalyst for achieving the goal of economic inclusion in general and financial inclusion in particular in NES.

The credit deposit ratio in NES was 27.8 percent when all India penetration of banking was 59.2% in 2001. After a span of nine years, the C-D ratio in NES has improved marginally and reached to 35.5% when all India banking development denoted by C-D was 73.3 %. The rural and urban divide in respect of banking development is very extreme in NES. That has arrested the process of financial inclusion in these states. Taking into account the total branches of commercial banks in India, hardly 2.60% bank offices are located in NES to deliver services to people. This observation suggests for opening of more branches of banks along with use the network of the post offices as bank and setup more credit societies in NES for giving access of banking to people of the these states. In the group of NES, number of branches of commercial banks should be increased in the states Meghalaya and Manipur since the density of bank per thousand people was found poor in these states.

To make dent over the backwardness of NES in all respect, an integrated policy of development should put in place for infrastructure development to harness the local potential so that food processing, wood products and traditional textile industries can be developed on large scale. To increase the access of NES to other parts of India, there is need to build strong air and road network which may increase the potential of marketing for locally manufactured product. At last, broad initiative is needed for stepping up agricultural productivity along with further development of horticulture, floriculture, animal husbandry is possible. All these efforts may push further the inclusive growth and financial inclusion in NES of India.

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