FINANCIAL INCLUSION: INITIATIVES IN INDIA, CONCEPT & INTERNATIONAL EXPERIENCE

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Abstract

Financial Inclusion in the Indian context implies the provision of affordable financial services, viz., access to payments and remittance facilities, savings, loans and insurance services by the formal financial system to those who lend to be excluded. Besides, access, emphasis is also placed on affordability (low cost) of financial services such as savings, loan, and remittance to the underprivileged segments of the population. With this backdrop an attempt is made to bring out the initiatives which were taken by the Indian Government and the Concept of Financial Inclusion.

Index terms: Financial Inclusion, Financial Exclusion, SHGs

INTRODUCTION

Although, the term 'financial inclusion' was not a vogue in India them, since the late 1960's both the Government and the RBI have been concerned about the non-availability of banking facilities to the under-privileged and weaker sections of the society. Accordingly, several initiatives have been taken over time such as creation of SBI in 1955 , nationalisation of commercial banks, in 1969 and 1980, prescription of priority sector targets, lending to weaker section at concessional rates and initiation of the lead bank scheme in 1970, establishment of RRBs in 1975, introduction of Self-Help Groups Bank-Linkage Programme in 1992 and formulation of the Kissan Credit Card Scheme in 2001. These initiatives were undertaken at different points in time to expand the outreach of banking facilities and increase the flow of credit to the rural areas. However, the broad approach towards financial inclusion followed in India in are 1970s and the 1980s was more oriented towards credit requirements of specific sectors/segments and there were relatively low emphasis on individual/house-hold level inclusion.

With the onset of economic reforms in the beginning of the 1990s, a strong and resilient financial sector was considered necessary for accelerating the growth momentum in the country and also for expanding the coverage of financial services in a sustainable manner. Accordingly the financial sector reform process placed more emphasis on creating a strong, vibrant and competitive banking system. An important step to bring financially excluded people within the fold of formal financial sector was the promotion of micro-finance in India. The SHG bank linkage programe was launched by NABARD in 1992, with policy support from the Reserve Bank, to facilitate collective decision making by the poor and provide 'doorstep' banking. Banks, as wholesalers of credit, were to provide the resources, while the NGOs were to act agencies to organise the poor, build their capacities and facilitate the process of empowering them.

To further promote the SHG-Linkage Programme in the country, banks were advised in1998 that SHGs that were engaged in promoting the savings habits among their members would be eligible to open savings bank accounts and that such SHGs need not necessarily have availed of credit facilities from banks before opening savings bank accounts. Subsequent to the Monetary and Credit Policy announcement for the year 1999-2000, banks were advised that interest rates applicable to loans given by them to micro credit organisations or by the Micro Credit Organisations to SHGs/members beneficiaries would be left to their discretion. Subsequently, banks were advised that they should provide adequate incentives to their branches for financing the SHGs and that the group dynamics of working of the SHGs may be left to themselves.

SIGNIFICANCE

The genesis of the current official disclosures on financial inclusion can be traced to the Budget Speech of Minister of Finance Shri. P. Chidambaram:

"*The findings of the NSS 59th Round (2003) reveal that out of the total number of cultivator households only 27 per cent receive credit from formal sources and 22 per cent from informal sources. The remaining households, namely small and marginal farmers, have virtually no access to credit with a view to bringing more cultivator households within the banking fold I propose to appoint a committee on financial inclusion. The Committee will be asked to identify the reasons for exclusion, and suggest a plan for designing and delivering credit to every household that seeks credit from lending institutions*".

In his opening address at the NDC in 2005, the Prime Minister was unequivocal in his view that for growth to be real it must be informed by equity. It must be growth for all because we cannot reconcile to a growth process, which bypasses those sections of society, which are disadvantaged and vulnerable. More importantly, it has been recognised that if long term sustainability of economic prosperity and social development is to be achieved, bringing in the benefits of economic growth to rural India is critical. It is only by delivering financial services to people in rural areas that they can be brought within the ambit of mainstream economic activity and the full potential of the country's physical and human resources can be realised. That is why issues relating to financial exclusion – particularly in the rural sector become a key policy concern, and devising strategies for inclusive growth have become the guiding principle of public policy.

In the Budget speech 2005-06 Shri P. Chidambaram, the Hon'ble Union Minister of Finance quoted that, "*The Financial Inclusion provides business opportunity for the financial institutions at the bottom of the pyramid to expand the volume of business. Profitability could be increased only by finding newer avenues for deployment of funds and this underscored the necessity for the financial inclusion of those sections who stand excluded*".

The subject came into further limelight on June 23, 2006 when the Prime Minister at the centenary celebration of Canara Bank said, " *I suggest the Finance Minister constitute a group with representatives from the RBI, NABARD, major commercial banks to formulate policies that promote Financial Inclusion by stimulating financial services for the poor, emphasizing micro-finance, micro-insurance and new delivery channels………… I would advise the banks to give the highest priority to customer service, to lower transaction costs and eliminate procedural inconveniences. Like all others the poor need a range of financial services that are convenient, flexible and affordable. The micro-finance can emerge as a powerful tool to fight poverty. It has to be a part of country's financial system it has to be effective*".

The Prime Minister expressed a concern that "*Despite rapid growth, modernisation and expansion of financial services in the country, large section of people particularly marginal farmers and those belonging to unorganised sectors have remained segregated from accessing credits*".

Elaborating on the subject of the Financial Exclusion Shri Leeladhar[1], Deputy Governor RBI said, "There could be multiple levels of Financial Inclusion and Financial Exclusion. At one extreme, it is possible to identify the super-included i.e., those customers who are actively and persistently courted by the financial service industry, and who have at their disposal a wide range of financial services and products. At the other extreme, we may have the financially excluded who are denied access to even the most basic of financial products. In between are those who use the banking services only for depositors and withdrawals of money. But these persons may have only restricted access to the financial system, and may not enjoy the flexibility of access offered to more affluent customers".

Thus, the Indian banking and finance scenario is a mix of Financial Inclusion and Financial Exclusion. The consequences of Financial Exclusion are for wider and are not confined to only excluded ones. It has deep socio-economic, cultural and political repercussions for the society as a whole. Shri Leeladhar's caution in this regard is quite note worthy. His words are, "consequences of Financial Exclusion will vary depending on the nature and extent of services denied. It may lead to increase travel requirements, higher incidents of crime, general decline in investments, difficulty in gaining access to credit or getting credit from informal services at exorbitant rates, and increase unemployment, etc. The small business may suffer due to loss of access to middle class and higher income customers, higher cash handling costs and delays in remittance of money. According to certain researchers Financial Exclusion can lead to social exclusion". It is believed that the spate of suicides by debt – infested farmers in some states over last few years are just a few symptoms of consequences of either inadequate Financial Inclusion or a total Exclusion or a mix of both.

Further to this direction, Dr. Y. V. Reddy, the then Governor, RBI, mooted the idea of reaching the unreached and called upon in his special address to Bankers in Pondicherry on 21-11-2005 to take up a National Pilot Project on Financial Inclusion in the UT of Pondicherry for a period of one year commencing from 01-01-2006. He also called upon the State Level Banker – "Indian Bank" to put in place the project guidelines for operation and allocation of specific villagers/wards to each Bank branch. Thereafter, RBI has taken various measures to facilitate the process.

Addressing the BANCON 2006 Bankers Conference, Dr. Y. V. Reddy, the former Governor, RBI, rightly observed that "Financial Inclusion is not a matter of philosophy but an approach that can lead to a win-win situation for the banks and the customers Treat Financial Inclusion as an investment for business. It is the mass move". In other words, financial inclusion can prove to be a boon to the customer banker and the economy alike.[2]

Hassle free occurs to affordable financial services – especially credit and insurance enlarges livelihood opportunities and empowers the poor to take charge of their lives. Such empowerment aids social and potential stability. It also imparts formal identity, provides access to the payments system and to savings safety not like deposit insurance.[3]

CONCEPT AND DEFINITION

Defining financial inclusion is considered crucial from the view point of developing a conceptual framework and identifying the underlying factors that lead to low level of access to the financial system. A review of literature suggests that there is no universally accepted definition of financial inclusion. As measuring inclusion is perceived to be difficult, financial inclusion is generally defined in terms of exclusion from the financial system. Financial exclusion can be through of in two ways. One is exclusion from the payment system i.e. not having access to a bank account. The second type of exclusion is from formal credit markets, forcing the excluded to move towards the costly option of informal and exploitative markets.

The financially excluded sections largely comprises marginal farmers, landless labour, oral lessees, self employed and unorganized sector enterprises, urban slum dwellers, migrants, ethnic minorities and socially excluded groups, senior citizens and women. There are a variety of reasons for financial exclusion. In remote, hilly and sparsely populated areas with poor infrastructure, physical access itself acts as a deterrent. From the demand side, lack of awareness, low incomes/assets, social exclusion, illiteracy act as barriers. From the supply side, distance from branch, branch timings, cumbersome documentation and procedures, unsuitable products, language, staff attitudes are common reasons for exclusion. All these result in higher transaction cost apart from procedural hassles. On the other hand, the ease of availability of informal credit sources makes these popular, even if costlier. The requirement of independent documentary proof of identity and address can be a very important barrier in having a bank account, especially for migrants and slum dwellers.

DEFINITION:

Financial Inclusion, in the present day context means provision of banking services at an affordable cost to the vast sections of disadvantaged and low-income groups. These include access to savings, credit, insurance, payments and remittance facilities by the formal financial system to those who tend to be excluded. Banking services are viewed as services in public good. Hence, the term financial inclusion means availability of baking services to the entire population without any discrimination.

Over the years, several definitions of financial inclusion/exclusion have evolved (Table: 1)

Table 1 Definitional Aspects of Financial Inclusion/Exclusion

Institutional / Author	Definition
Asian Development Bank (2000)	Provision of a broad range of financial services such as deposits, loans, payment services, money transfers and insurance to poor and low-income households and their micro-enterprises.
Stephen P. Sinclair (2001)	Financial exclusion means the inability to access necessary financial services in an appropriate from. Exclusion can come about as a result of problems with access, conditions, prices, marketing or self-exclusion in response to negative experiences or perceptions.
Chant Link and Associations, Australia (2004)	Financial exclusion is lack of access by certain consumers to appropriate low cost, fair and safe financial products and services from mainstream providers. Financial exclusion becomes a concern in the community when it applies to lower income consumers and/or those in financial hardship.
Treasury Committee, House of Commons, UK (2004)	Ability of individuals to access appropriate financial products and services.
Scottish Government (2005)	Access for individuals to appropriate financial products and services. This includes having the capacity, skills, knowledge and understanding to make the best use of those products and services. Financial exclusion by contrast, is the converse of this.
United Nations (2006 b)	A financial sector that provides ‘access’ to credit for all ‘bankable’ people and firms, to insurance for all insurable people and firms and to savings and payments services for everyone. Inclusive finance does not require that everyone who is eligible use each of the services, but they should be able to choose to use them if desired.
Report of the Committee on Financial Inclusion in India (Chairman: C. Rangarajan) (2008)	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.
World Bank (2008)	Broad access to financial services implies an absence of price and non-price barriers in the use of financial services: it is difficult to define and measure because access has many dimensions.

FINANCIAL INCLUSION AND INTERNATIONAL EXPERIENCE

In view of its paramount significance in economic and banking growth, financial inclusion is being practiced in different developed countries of the world with greater thrust on empowerment of the common person and low income groups. The governments and financial regulators in the UK, USA, Canada, France, Australia, Belgium, Sweden, Germany etc., had undertaken policy initiatives much earlier to eliminate banking and financial exclusion.

In UK one out of 12 households do not have basic current account with any bank. a Task Force on financial inclusion was set up to increase access to banking, to affordable credit and to free money advice. The Financial Inclusion Task Force in the UK has identified three priority areas for the purpose of financial inclusion, viz., access to banking, access to affordable credit and access to free fact-to-face money advice. The UK has established a Financial Inclusion Fund to promote financial inclusion and assigned responsibility to banks and credit unions in removing financial exclusion. An enhanced legislative environment for credit unions has been established, accompanied by tighter regulations to ensure greater protection for investors. The steps taken included introduction of no-frills bank accounts, legislative support for credit unions and tighter regulations to ensure greater protection for depositors/investors. For those who cannot have access to bank accounts, Post Office Card Account (POCA) has been introduced. Besides, the concept of a Savings Gateway and the Community Finance Learning Initiatives (CFLIs) were also introduced to encourage availing of financial services by the disadvantaged groups.

In USA – varying from State to State, 10 to 20 per cent of US households lack a bank account. Among the low-income families, 22% do not have either a current or savings account. The Government has taken various measures to deal with the problem of financial exclusion. In the USA, a civil rights law, viz., Community Reinvestment Act (CRA) prohibits discrimination by banks against low and moderate income neighborhoods. The CRA imposes an affirmative and continuing obligation on banks to serve the needs for credit and banking services of all the communities in which they are chartered. Further, the state of New York Banking Department, with the objective of making available the low cost banking institution, offers basic banking account and in case of credit unions the basic share draft account, which is the nature of low cost account with minimum facilities. Some key features of the basic banking account are:

(i) The initial deposit amount required to open the account shall not exceed US $ 25.
(ii) The minimum balance required to maintain such account shall not exceed US $ 0.10.
(iii) The charge for periodic cycle for the maintenance of such accounts to be declared up front.
(iv) A withdrawal shall be deemed to be made when recorded on the books of the account holder's banking institution.
(v) The banking institution has to furnish, prior to opening the account, a written disclosure to the account holder describing the main features of the scheme, i.e., the initial deposit amount required to open and account, minimum balance to be maintained, charge per periodic cycle for use of such account, maximum number of withdrawal transactions without any additional charge and other charges imposed on transactions for availing electronic facility not operated by the account holder's banking institutions, etc.

In France - As per Article 58 of the Banking Act, any person refused a bank account can approach the bank of France, which will identify and nominate an institution to provide the bank account. In 1992, French banks signed a charter undertaking to open bank accounts at an affordable cost with related payment facilities to all.

In Germany, a volunteer code was introduced by the German Bankers Association n 1996, providing for an 'everyman' current account, offering basic banking transaction, without an overdraft facility.

In Belgium, a banking bill was enacted which was implemented since October, 2003. In addition to setting out the minimum standards for basic bank account, it also specifies the ceiling on charges and a minimum number of free face-to-face transactions.

In Canada – A legislation entitled "Access to Basic Banking Services Regulations" was introduced in 2003 whereby all banks/financial institutions are required to open personal bank accounts and encash most Government cheques at no charge for any citizen who meets the basic requirements. The Federal Government also introduced legislation requiring banks to offer a standard low cost bank account with a basket of services. Memoranda of Understanding were signed between the Federal Government and eight financial institutions to ensure that all Canadians have access to affordable banking services.

In Sweden, banks cannot refuse to open a saving or deposit account under Section 2 of the Banking Business Act, 1987.

SOME OF THE INITIATIONS TAKEN BY NABARD AND RBI TOWARDS DEVELOPING FINANCIAL INCLUSION (BASING ON VARIOUS COMMITTEE REPORTS):

A) Strategy for Building an Inclusive Financial Sector: Overall strategy for building an inclusive financial sector may be based on:

- Effecting improvements within the existing formal credit delivery mechanism;
- Suggesting measures for improving credit absorption capacity especially amongst marginal and sub marginal farmers and poor non-cultivator households;
- Evolving new models for effective outreach, and
- Leveraging on technology based solutions.

B) Financial Inclusion Funds: Two funds may be constituted – a Financial Inclusion Promotion & Development Fund, with NABARD, for meeting the cost of developmental and promotional interventions and a Financial Inclusion Technology Fund, with NABARD to meet the costs of technology adoption. Each Fund will have an initial corpus of Rs. 500 crore, with a start up funding of Rs. 250 crore each, to be contributed equally by GoI / RBI / NABARD and annual accretions thereto. Banks will be eligible for support from the Funds on a matching contribution of 50% from the Fund in regard to districts other than tribal districts and 75% in case of branches located in tribal districts identified under the Tribal Sub Plan.

C) NABARD to open 'Project Offices' in identified Priority States: NABARD is managing the Micro Finance Development and Equity Fund (MFDEF) with a corpus of Rs. 200 crore. One major focus of the Fund should be promoting the SHG-Bank Linkage Programme in States where it has been comparatively slow moving. NABARD has already identified 13 States with large population of the poor, but exhibiting low performance in implementation of the programme. The ongoing efforts of NABARD to upscale the programme in the identified States need to be given a fresh impetus.

D) Greater role for NABARD: While greater emphasis is needed for growth and spread of SHGs across the country, the quality in terms of outreach of financial services, capacity building, sustainability etc., needs to be reemphasized. NABARD shall play a pro-active role and identify new initiatives that will contribute to effectively improving outreach to the poor thru' SHGs, MFIs, etc.

E) Amendment to NABARD Act: At present, NABARD is permitted, as per its Act and Mandate, to support micro finance activities in rural and semi-urban areas only. An enabling provision is made in the NABARD Act, 1981 permitting NABARD to provide micro finance services to the urban poor.

F) Pilot Scheme to allow drawals from Semi-Closed Mobile Wallets (RBI): Semi-closed mobile wallets, which were once hailed as weapons of financial inclusion as they do not require the user to have a bank account, have one noticeable drawback: a user can add cash but can't draw it out. The Reserve Bank has long-held the view that letting telecom operators to offer cash-out facilities for their mobile wallet users would allow the companies to bypass the banking system. According to people with direct knowledge of the matter, a number of pre-paid payment issuers (PPIs) have been petitioning the central bank to allow cash withdrawal facilities. The central bank has, therefore, decided to start a pilot that would allow pre-paid payment instruments such as mobile wallets to proliferate and in order to see whether it would throw up any security problems. When contacted, a RBI spokesperson confirmed that the pilot had started and that a few entities had started carrying out transactions.

Institutional structure to coordinate financial inclusion

Country	Coordination body
Kenya	In Kenya, financial inclusion monitoring is supervised by the Central Bank (CBK). In 2005, CBK partnered with the Financial Sector Deepening FSD) Kenya and other financial sector players and stakeholders under a private-public partnership arrangement, the Financial Access Partnership (FAP), to monitor and measure levels of access to financial services with reliable data collected in a regular basis.
Korea	The Financial Supervisory Commission (FSC) is Korea’s lead agency for financial inclusion policy. FSC works closely with other agencies such as the Small and Medium Business Administration. In addition, the Money Lending Policy Council is responsible for monitoring money lending regulations.
Brazil	In 2009, the Financial Inclusion Project at the Central Bank was created with the objective of integrating various stakeholders to develop effective policies for financial inclusion. A major part of the project was the collection, organization, and analysis of data and research on various issues related to financial inclusion (such as the expansion of correspondent banking across regions in Brazil). In November 2011, the National Partnership for Financial Inclusion was launched.
Indonesia	The Vice President’s (VP) Office in Indonesia is responsible for coordinating all efforts toward financial inclusion. The VP Office coordinates national policy initiatives in close consultation with the central bank or Bank Indonesia (BI). Since the VP Office took responsibility, several steps to advance financial inclusion in the country have been taken (an online case study will be posted on the Indonesia Financial Inclusion Strategy process).
United Kingdom	In the United Kingdom, the Financial Inclusion Taskforce was an independent body that advised HM Treasury and monitored and evaluated progress on financial inclusion. The taskforce was launched on February 2005 and was composed of members drawn from the private, public, and non-profit sectors, who served in a personal capacity, and on a voluntary basis. The taskforce concluded its work in March 2011, making final recommendations for government and the private sector.
United States	To support financial literacy in the United States, the Financial literacy and Education Commission was established with the Financial Literacy and Education Improvement Act of December 4, 2003. the act named the secretary of the treasury as chairperson of the commission and mandated the commission’s composition to include the heads of 20 federal agencies, such as the labor, education, and agriculture departments, the Federal Deposit Insurance Corporation, the Board of Governors of the Federal Reserve System, and the White House Office of Public Engagement (FEC 2011).
Philippines	The Bangko Sentral ng Pilipinas created a Microfinance Unit in 2002, which was transformed into the Inclusive Finance Advocacy Staff in 2007, in recognition of the importance of a broader objective of financial inclusion.
Mexico	To provide an institutional mechanism to facilitate coordination among these agencies, the National Council on Financial Inclusion was created in 2011 (see Box 4). The objective of this council is to organize the different entities working on financial inclusion in the country, from regulatory agencies to social development and consumer protection agencies. For countries like Mexico, with a variety of social programs that can be leveraged to promote

	financial inclusion, this council represents an important achievement. The Council will coordinate proposals for financial inclusion policies and their implementation, formulate guidelines of a National Policy on Financial Inclusion, define medium- and long-term goals for financial inclusion, propose the necessary changes in the financial sector, and obtain information from the private sector on programs and actions related to financial inclusion.

Source: Financial Inclusion Strategies Reference Framework, June 2012, The World Bank.

Conclusion

The financial system in India has grown rapidly in the last three decades and more. The functional and geographical coverage of the system is truly impressive. Nevertheless, data do show that there is exclusion and that poorer sections of the society have not been able to access adequately financial services from the organized financial system. There is an imperative need to modify the credit and financial services delivery system to achieve greater inclusion. However, creating an appropriate credit delivery system is only a necessary condition. This needs to be supplemented by efforts to improve the productivity of small and marginal farmers and other entrepreneurs so that the credit made available can be productively employed. While banks and other financial institutions can also take some efforts on their own to improve the absorptive capacity of the clients, it is equally important for Government at various levels to initiate actions to enhance the earnings capacity of the poorer sections of the society. The two together can bring about the desired change of greater inclusion quickly.

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