Financial Inclusion – A Socio Economic impact on poverty reduction in India.

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Abstract: India has witnessed many economic and development plans changes over the last few decades. Several reforms and initiatives aimed at poverty reduction and enhancing financial inclusion had been attempted by the Indian government and its development partners in the recent time. The purpose of the study is to investigate the effects of financial inclusion on poverty reduction: the moderating effects of microfinance. Data collection techniques employed was self-administered questionnaire. The findings of the study revealed that there is a significant relationship between the financial inclusion and poverty reduction. The results further revealed that microfinance positively moderate the relationship between the variables under studies. The paper recommends the financial inclusion to be more robust in the rural areas and to make microfinance a more effective means of poverty reduction other services such as, education loan, technological support loan, skills training, and housing appliance loan should be included in microfinance services.

Keywords: financial inclusion, microfinance, PLS, SEM

Introduction

Financial inclusion is a key element of social inclusion (the antithesis of social exclusion), roughly meaning the opportunity for people to benefit from, and to contribute to the processes of economic and social advancement According to the RBI (2006) financial inclusion is the "provision of affordable financial services" to those who are under-attended by formal agencies of the financial system. These financial services include savings, remittance facilities loan, payments, and insurance services" (RBI, 2006) [58]. Given the definition of financial inclusion, any means for financial inclusion, to begin with, has to be not just easily accessible but also affordable to the borrowers, who do not have access to the formal financial system. it should also ensure that the borrowers are able to reduce their dependence over time on informal sources of finance, which can work towards permanent or effective inclusion of these borrowers into the formal banking network. Previous research has shown that financial services are not made readily available to everyone that needs them for some reasons which could be lack of awareness (financial illiteracy), unfavorable regulatory environment, rigid product structure, etc. (Dashi, Lahaye, & Rizvanolli, 2013) [26].

Previous data has shown that about 50% of the global adult population aged 15, and above are financially excluded. Of this number, about 2.7 billion adults in the world (equivalent to 70% of the world adult population) lack access to formal financial services which makes financial inclusion a complex matter across different nations (Dashi et al., 2013) [26]. Over 2 billion adults in emerging economies such as Nigeria still lack access to basic financial services.

Financial inclusion or inclusive financing is the delivery of financial services at affordable cost to socially deprived and low-income segments of society. Financial inclus ion is a critical step that requires political will, bureaucratic support and determined persuasion by RBI. It is expected to unleash the hugely untapped potential of that section of Indian economy, which is at the bottom of pyramid. Financial inclusion will be the next revolution for growth and prosperity in Indian economy.

The objective of Financial Inclusion is to extend financial services to unlock growth potential of economy. In addition, it strives towards a more inclusive growth by making financing available to the poor in particular. Financial Inclusion and Financial Literacy both are twin pillars where Financial Inclusion acts on the supply side i.e. for creating access and financial literacy acts from the demand side i.e. creating a demand for the financial products and services.

Financial Inclusion: The attention of researchers, policy-makers, and development oriented agencies on financial inclusion has continued to increase especially been it a tool for economic development, particularly in the area of improving welfare and general standard of living, wealth creation, employment generation, and poverty reduction. The World Bank argues that access to and use of basic financial services like savings, payments, loans, and insurance, helps t1he poor to move out of poverty by economically and socially empowering them. Financial inclusion of the unbanked poor is a critical step that requires bureaucratic support and political will by CBN.

Financial inclusion is achieved when financial services are provided at an affordable cost and adults have easy access to many formal inancial services that meet their needs. This is in support of the elements used in the definition provided by CBN (2012) which include:

i) Access to and usage of a wide range of financial products and services such as insurance, credit, savings, pension, and payments products.

ii) Easy access to financial products and services financial products, this financial product, and services must be within reach of all sections of the populace and should not have onerous requirements.

iii) Provision of affordable financial services to low-income groups.

iv) Financial products must be designed according to the need of customers (financial excluded) persons and should consider access to distribution channels and income levels.

Why is Financial Inclusion in India Important?

The policy makers have been focusing on financial inclusion of Indian rural and semi-rural areas primarily for three most important pressing needs:

1. Creating a platform for inculcating the habit to save money – The lower income category has been living under the constant shadow of financial duress mainly because of the absence of savings. The absence of savings makes them a vulnerable lot. Presence of banking services and products aims to provide a critical tool to inculcate the habit to save. Capital formation in the country is also expected to be boosted once financia l inclusion measures materialize, as people move away from traditional modes of parking their savings in land, buildings, bullion, etc.

2. Providing formal credit avenues – So far the unbanked population has been vulnerably dependent of informal channels of credit like family, friends and moneylenders. Availability of adequate and transparent credit from formal banking channels shall allow the entrepreneurial spirit of the masses to increase outputs and prosperity in the countryside. A classic example of what easy and affordable availability of credit can do for the poor is the micro-finance sector.

3. Plug gaps and leaks in public subsidies and welfare programme – A considerable sum of money that is meant for the poorest of poor does not actually reach them. While this money meanders through large system of government bureaucracy much of it is widely believed to leak and is unable to reach the intended parties. Government is therefore, pushing for direct cash transfers to beneficiaries through their bank accounts rather than subsidizing products and making cash payments. This laudable effort is expected to reduce government’s subsidy bill (asit shall save that part of the subsidy that is leaked) and provide relief only to the real beneficiaries. All these efforts require an efficient and affordable banking system that can reach out to all.
Therefore, there has been a push for financial inclusion.

Poverty is general scarcity or dearth or the state of one who lacks a certain amount of material possessions or money. It refers to the deprivation of basic human needs, which commonly include health care, shelter, sanitation, water, food, clothing, and education]. Poverty may also be understood as experienced as social exclusion, inequitable social relationships, a facet of asymmetrical social status, diminished capacity to participate or to develop significant associates with other people in society. Poverty is one of the core problems of every economy all over the world. Approximately, 1.2 billion people about one-fifth of the world population - live below the extreme poverty line of $1 a day in the late 1990s. If we use the $2.5 line, this number rises to 2.8 billion, more than half of the world's population. Studies conducted by Chandran (2011) [17] and Sarma and Pais concluded that financial inclusion is pro-poor. The authors pointed out that financial inclusion help low-income households to access basic financial services like savings, credit, and insurance, which, in turn, fosters their financial autonomy and thus amplifies economic growth. They advocated that enhanced financial services not only raises economic growth but also reduces poverty and income inequalities.

Strategies for achieving the financial inclusion targets

To meet up with stated targets, efforts will be concentrated in the area of agent banking, mobile banking, linkage banking, and client banking.

- **Agent banking**: is the provision of banking services outside traditional bank branches through mobile phones, technology such point of sales (POS) devices and touch points such as petrol station and existing retail stores.
- **Mobile Banking:** Provision of access to financial services through the use of mobile wallets as intermediary virtual money accounts or mobile phones that are directly linked to a bank account.
- **Linkage models:** Business cooperation and enhancement of financial between traditional financial institutions (Deposit Money Banks or Development Finance Institutions), microfinance banks/institutions, and government for providing wholesale funding for and lending transactions.

OBJECTIVE OF THE STUDY:

- To rank the need and examine the current status of financial inclusion in India.
- To study the existing measures of financial inclusion initiated by central and state governments and their implementation.
- To know the awareness level of financial inclusion among public.
- To measure socio – economic impact of financial inclusion on beneficiaries.
- To find out the challenges and prospect of financial inclusion.
- To suggest the action plan to draw the maximum benefit of financial inclusion.

HYPOTHESIS:

H1: Financial inclusion has a positive relationship with poverty reduction.
H2: Microfinance has a positive relationship with poverty reduction.

Access to financial services enables the poor to fight the various dimensions of poverty and make improvement in their lives and provides momentum for growth and development. Financial inclusion through cooperative banks is the key to empowerment of poor, underprivileged and low-skilled rural households. Through financial inclusion, microfinance banks increase the economic opportunities for the poor and low-income people, which lead towards a positive result in social progress, economic development, economic empowerment and social/ political/ legal empowerment. Thus, it is hypothesized that.
H1: Financial inclusion has a positive relationship with poverty reduction.

Microfinance

Over the last three decades, the acceptance of microfinance has progressively increased. Microfinance has unlocked the entrepreneurial ambitions of some of the world's poorest people. It is defined as a provision of credit, thrift, other financial services, and products of very small amounts to the poor in both urban, semi-urban, and rural areas so as to enable them to improve their living standard and raise their income.

Microfinance also refers to a wide range of organizations dedicated to providing micro financial services including nongovernment organizations, credit unions, co-operatives, private commercial banks, non- banking financial institutions and some state-owned banks. The establishment of Microfinance is centered on economic development programms that aims at poverty reduction through financial services to the micro-entrepreneurs, low-income earners and poor that cannot access similar services from the formal financial market.

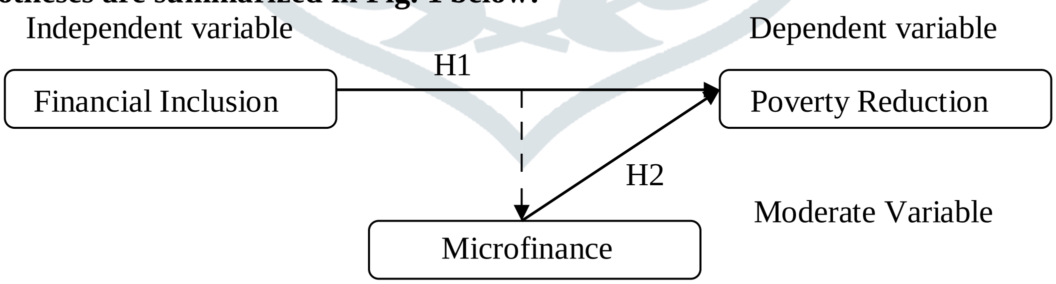
Microfinance also from other perspective involves the provision of financial services such as loans, savings, and insurance to poor people living in rural and urban settings who are financially excluded from the formal financial sector. The services are provided by formal, semi-formal and informal organizations. According to Kumra and Sharma (2018) [49] characterized microfinance the following:

1. Provision of small loans for the working capital to the rural poor.
2. Minimal appraisal of investments and borrowers as compared to commercial banks.
3. Demand no collateral. However, these bodies enforce compulsory savings and group guarantees. That is not based on legal procedures and system but on trust.
4. Microfinance institutions extend larger loans to customers continually, based on their loan repayment history.

Microfinance develops savings habit among people. Poor people with meager income can also save and become bankable. Microfinance programmes help the poor by improving entrepreneurial skills and encourage them to exploit business opportunities. They also help them by providing self employment opportunities. Employment increases income level which in turn reduces poverty.

In this regard, the establishment of microfinance institutions means the procedure of making an available very small proportion of financial services to the poor with the purpose of making them takes up new opportunities which the development process offers. In addition, it is responsible for creating and sustaining new income-generating activities in poor areas traditionally dependent on subsistence farming. Many in the Western countries saw microfinance as an essential innovation in the fight against poverty in the developing world. Thus the paper hypothesized that:

The study hypotheses are summarized in Fig. 1 below:



Methodology:

The study aims at examining the socio economic impact of financial inclusion on poverty reduction alleviation the moderating effects of microfinance banks. Researchers attempting to conduct a survey of any sort should pay ample attention to their sampling, which is derived through careful selection of the sampling design and procedures. The present study adopted stratified and simple random sampling methods to select the sample.

Data Analysis:

Response Rate of the Questionnaires

The research used all 10 Microfinance located in the three senatorial districts of the state from the sampling frame from each microfinance, 38 customers were randomly selected to participate in the study from the 6 microfinance, while 39 customers were randomly selected to participate in the study from the 4 microfinance. Therefore, 384 questionnaires were randomly distributed to the beneficiaries, but 318 responded back. Out of 318 respondents, 25 questionnaires were rejected because of either incomplete responses or the problem of outliers, so the final sample size came to 293 respondents. The effective response rate came out to be 76.30.

Assessment of the measurement model

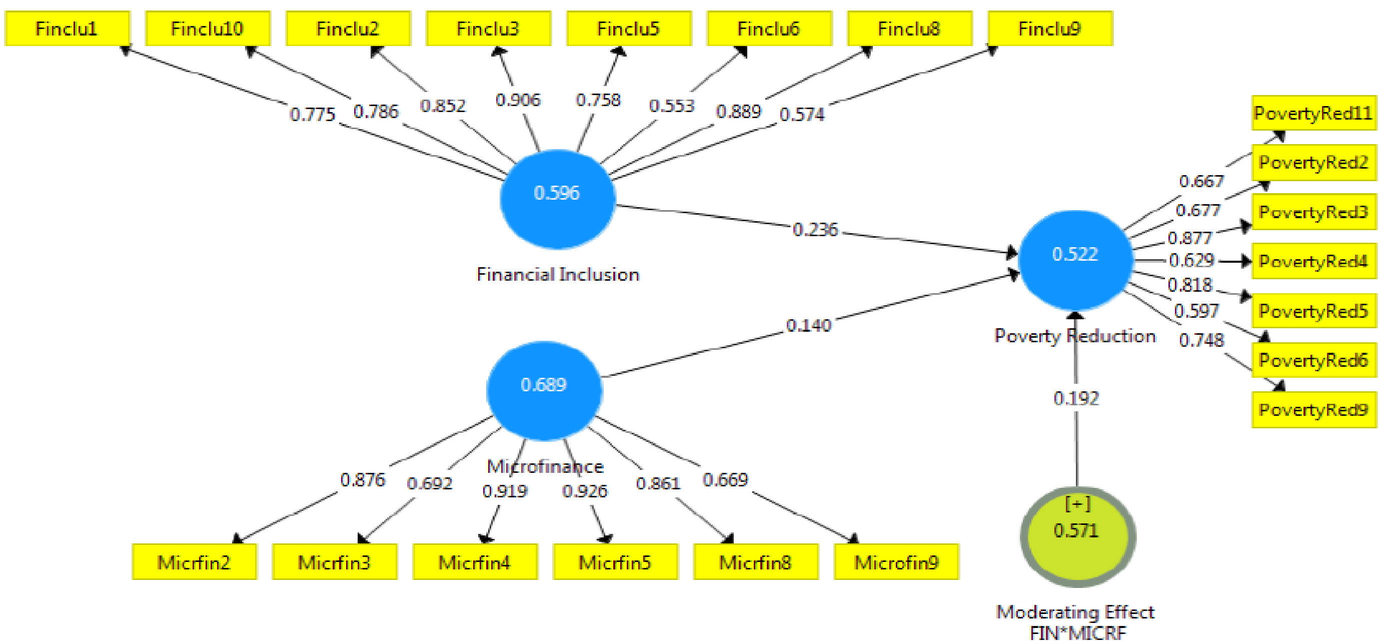


Fig 1 : Assessment Model

Discriminate Validity Test

	Mean	Std. Dev	Financial Inclusion	Microfinance	Poverty Reduction
Financial Inclusion	4.1246	0.4604	0.772	Financial Inclusion	
Microfinance	3.9859	0.4945	0.215	0.830	
Poverty Reduction	3.8120	0.4866	0.313	0.276	0.723

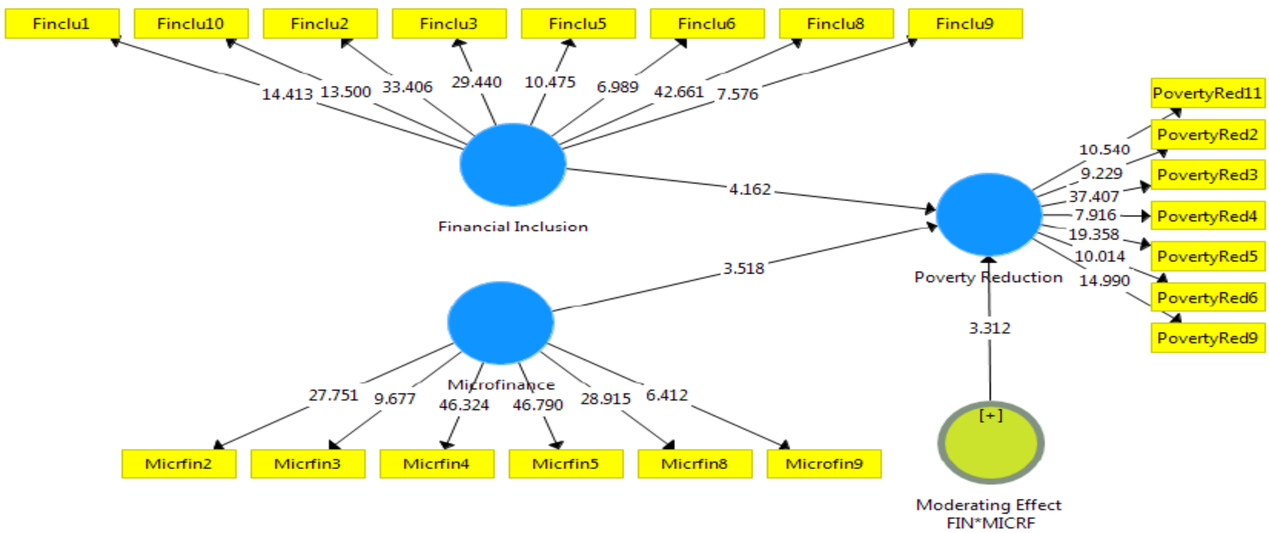


Fig 2: Structural Model

Path Coefficients: -

Hypothesis	β	Std Dev	T-Value	P Values
Financial Inclusion -> Poverty Reduction	0.236	0.057	4.162	0.000
Microfinance -> Poverty Reduction	0.140	0.040	3.518	0.000
Moderating Effect FIN*MICRF -> Poverty Reduction	0.192	0.058	3.312	0.000

In order to assess the structural model (i.e Fig 3), the path coefficients, including an assessment of their significance, the coefficient of determination R2. Results show that financial inclusion is positively related to poverty reduction ($\beta = 0.236$, $p < 0.000$), supporting H1. Microfinance is positively related to poverty reduction ($\beta = 0.140$, $p < 0.000$), supporting H2. Overall satisfaction of the model is revealed in the coefficient of determination R2 of the endogenous latent variables, a common indicator in multiple regression analysis. The result of the model shows an R2 of 0.169 for poverty reduction.

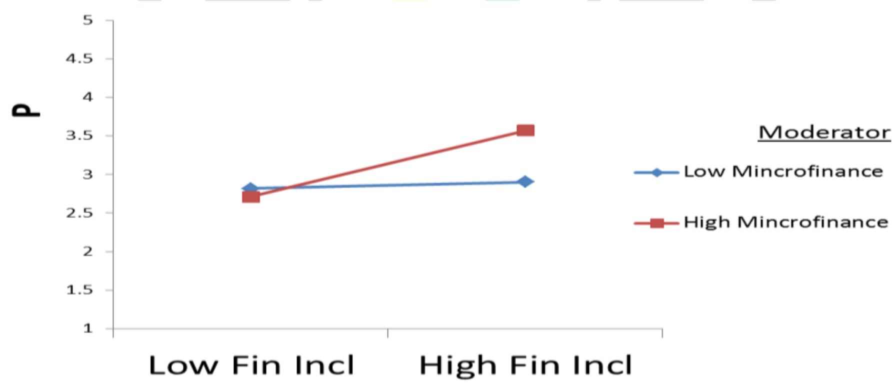


Fig 3: The plot of the interaction between financial inclusion and microfinance in predicting poverty reduction.

Fig. 3 illustrates the ordinal relationship between financial inclusion and microfinance in the prediction of poverty reduction. The graph clearly demonstrates that low levels of financial inclusion have a weaker positive effect on poverty reduction compared to the higher level of financial inclusion characterized by the area with high microfinance.

Conclusion:

The objective of the study was to evaluate the moderating effects of microfinance in the relationship between financial inclusion and poverty reduction. The model was tested to verify the hypotheses with respect to financial inclusion and microfinance. Concerning the academic contribution of this study, we have to highlight that there are studies in the literature about the proposed model with regard to the influence of financial inclusion and microfinance in the poverty reduction. However, this study is pioneering research in the field of empirical analyses regarding the moderating effect of microfinance on the relationship between financial inclusion and poverty reduction.

This research analyzes the moderating role of microfinance as proposed in the model. The study is relevant as it contributes in the microfinance, financial inclusion, and poverty reduction context. In addition, the main theoretical contribution is the study of the moderating effects of microfinance on the relationship between financial inclusion and poverty reduction.

Results show that financial inclusion positively and significantly impacts on poverty reduction. The finding of this research is consistent with previous research suggesting that when there is financial inclusion in the rural areas, poor households are likely to use the opportunity of having financial services available to invest and seek for financial services that will increase their level of standard. Also, the results are also consistent with the finding that financial inclusion of the excluded poor adult population in India could unlock their productive potentials by helping them to be involved in productive activities.

Future research should study other factors that may influence the variables in the proposed model, for instance future researchers should consider government policy, interest rate, and risk management the their study. It would also be useful to analyze other potential moderators, such as risk culture, bank size, and bank age.

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