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FINANCIAL INCLUSION AND ECONOMIC GROWTH

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ABSTRACT

Economic growth with social justice is prime objective of Indian economy. The government initially believed in trickledown theory i.e. benefits of growth will trickledown till bottom and the people will be uplifted above poverty line. But in reality trickledown theory did not work. Instead the gap between rich and poor increased over a period of time.

This paper is a humble attempt to review the role of RBI in implementing Financial Inclusion (FI) policy in India over a period of time. The study also reviewed the progress report of FI in India. The country has come long way in the process of financial inclusion, but still has a long way to go. We were moving from mandates, subsidies and reliance on the public sector banks for inclusion. Now we are creating frameworks that attract and enable financial institutions to target the excluded. The interests of the excluded are protected through education, competition and regulation.

Financial inclusion will be an important element in ensuring access and equity, necessary building blocks for the sustainable growth of our country.

INTRODUCTION

According to ILO declaration of Philadelphia (1944), "Poverty any where is a threat to prosperity everywhere".

The policy makers in India too realised the implications of poverty on financial stability and through various policies trying to ensure that the benefits of economic growth reaches the poor and excluded sections of the society. Our economic policy has always been driven by the objective of sustainable and inclusive growth. Financial inclusion is very important policy objective for sustained and inclusive growth.

Financial Inclusion (FI) is the process of ensuring access to appropriate financial products and services needed by all sections of the society in general and vulnerable

groups such as weaker sections and low income groups in particular at an affordable cost in a fair and transparent manner by mainstream institutional players.

Financial inclusion is about

(a) The broadening of financial services to those people and enterprises that do not have access to financial services sector.
(b) The deepening of financial services sector for those who have minimal financial services.
(c) Greater financial literacy and consumer protection so that those who are offered financial products can make appropriate choices.
RBI is trying to bring about sustained economic growth through the policy of FI.

Objectives of the study:

1) To review the financial inclusion policies of the government over a period of time.
2) To review the progress of financial inclusion in India.

Methodology:

The present study is based on the secondary data collected from different journals, magazines, sites, news papers, Economic survey and published data from various issues of RBI Bulletin and reports. Various studies on this subject have also been referred in this study.

Role of RBI in Financial Inclusion

RBI started its efforts on this line in 1960 by channelising credit to the neglected sectors of the economy and weaker sections of population.

Steps taken at that time were:

1) Nationalisation of commercial banks in two tranches in 1969 and 1980,
2) Priority sector leading requirement for banks,
3) Lead bank scheme,
4) Establishment of Regional Rural Bank (1975-76),
5) Service Area Approach (1989),
6) Self Help Group linkage programme (1989-90),
7) Setting up of Local Area Banks,

All these schemes aimed at making available benefits of banking services to the masses for financial inclusion.

According to former governor of RBI Raghuram Rajan India has 21% of the worlds unbanked population as of 2015. India's banked population stood at around 400 million in 2014. Since then 257 million Jan Dhan banks accounts have been created. Still many people are without bank accounts. There are certain structural challenges which impede the progress of financial inclusion.

On the supply, side absence of technology was a major impediment which restricted expansion of banking services to remote villages. The most important impediment is the economic condition of the excluded because they are hard to service profitably. The excluded may live in remote areas or may belong to communities or segments of society that undertake economic activity informally. They do not maintain record or documentation. They don't have securities for mortgage, do not get easy loans. The third impediment is transaction costs. Time given by the officer while helping a client fill out the forms and to provide necessary documentation for loan of Rs, 10,000 and Rs. 10 lacks is same. Therefore a banker naturally focuses on large borrowers in preference to small ones.

There are positive social benefits to financial inclusion. For example, when farm worker starts a poultry farm through bank loan, he gets a better status in the community. Similarly direct transfer of benefit is easier when majority of beneficiaries have a bank account and they use it to transfer money to other account through mobile phones. Therefore Raghuram G. Rajan former governor of RBI has given three approaches to deal with the problem of Financial Inclusion.

One approach is to push formal institutions into reaching out to the excluded, even if it is unprofitable. Banks are asked to open 25% of their branches in unbanked areas. Loans are available to particular sectors at concessional rate.Banks have been urged to open bank account for all under PMJDY and they are also being exhorted to make loans to small business under Mudra Scheme.

RBI tried to make the mandate more effective by revising list of sectors eligible for priority sector treatment in which real excluded are targeted. The share of small and marginal farmer (including share croppers) in adjusted net bank credit is set at 8% and for micro enterprises set at 7.5%. Banks are required to meet their targets at the end of every quarters rather that at the end of the year. This reduces the scope for window dressing. Thus priority sector mandate is better targeted at the real excluded and will also be delivered more efficiently.

Approach II: Creating the right institution:

Our nationalised banks with a local transaction suffers two infirmities,

1) Sometimes branch manager is not familiar with local people as he is not from same state because he has been recruited through an All India Exam. His higher socio-economic status also creates a distance with the poor segment of the community. Their higher salary makes many branches in remote area economically unviable.
2) The excluded do not have formal documents which make it difficult for manager to provide effective service.

Local financial institutions with local control and local staff could be better solution to provide service to excluded. Similarly micro finance institutions are also successful to provide finance to excluded.

However both types of institutions have some deficiencies. Local areas banks could not expand out of their local area. Micro finance institutions do not have access to low cost deposit financing.

To solve these problems the RBI has the Small Finance Bank (i.e. 75% of loans mandated to be below 25 lakhs). These institutions are supposed to maintain low cost structure. The use of Aadhaar in identifying individuals will also help eliminate duplicate records.

Approach III: Don't start with credit:

RBI was trying for decades to expand credit but focussed less or easing payment and remittances, on expanding remunerative savings vehicles or on providing easy to obtain insurance against crop failures.

Now in the emerging financial inclusion paradigm, the Govt. and the RBI are trying to expand inclusion by encouraging these products. Some of the SHGs try to expand inclusion encouraging other products mentioned above which inculcate not only saving habit among the people but also allow the customer to handle the burden of repayment better. Easy payment and cash out will make formal savings more attractive.

Therefore RBI is strengthening the network of Banking Correspondents, giving them the ability to take and give cash on behalf of any bank through the Aadhaar enabled payment system. They are also adequately trained in providing financial services. By making post offices and telephonic kiosks entry points into financial system, cash in and cash out points are expanding making payments and transfer easy. Through unified payment interface via mobile banking, depositing money or withdrawing money becomes easier.

Thus RBI is trying to expand financial inclusion through these three approaches.

For this RBI needs to focus on 1) KYC requirement, 2) encouraging competition to prevent exploitation 3) ensuring some flexibility and forgiveness in financial arrangement, 4) the need for skilling and support 5) encouraging financial literacy and ensuring consumer protection.

Steps taken by RBI from 2006:

The issue of financial inclusion was addressed by RBI through planned and structured approach to focus on demand as well as supply side.

It is mainly possible due to adoption of technology by banking sector.

Major steps towards enhancing access of banking services are:

1) Institutionalisation of the framework of Banking Correspondents (BCs)

2) RBI advocated a combination of 'Brick and mortar structure with mouse and click technology'.

3) Regulatory side: Banks were mandated to open at least 25% of their new branches in unbanked rural centres.

4) Measure to solve difficulties of meeting KYC requirement

   i) RBI allowed banks to accept self certification for opening of Basic Service Bank Account
   ii) RBI encouraged banks to open Aadhaar Enabled Bank Accounts by linking Aadhaar number of individuals whenever available with the Basic Savings Bank Accounts opened for them, so that their credit histories can also be built up over time.

5) RBI prepared Board approved Financial Inclusion Plans (FIPs). The first two phases of FIPs implemented over 2010-13 and 2013-16 were interspersed with the implementation of Pradhan Mantry Jan Dhan Yojna (PMJDY), on 28th August 2014 by Govt. of India where supply side efforts received extra push. The objective of PMJDY is to provide universal access to banking facilities, providing basic banking accounts with overdraft facility and Ru Pay Debit card to all households, conducting financial literacy programmes, creation of credit guarantee fund, micro-insurance and unorganised sector pension schemes.

6) Approval has be granted by RBI to some entities to setup differentiated banks namely 'Small Finance Banks' (SFBs) and 'Payment Banks' to support financial inclusion in the country.

SFBs and Payment Banks are expected to enhance the supply of credit to small business units, small and marginal farmers micro and small industries and others entities in unorganised sector. Besides promoting habit of saving among people they also provide the facility of remittances with secured technology.

7) Financial Inclusion and Payment System are closely linked: Considering this RBI has taken several steps.

   a) Mobile banking is encouraged
   b) Digital Wallets and Mobile Wallets, Prepaid Instrument Aadhaar Bridge Payment System (ABPS) and Aadhaar Enabled Payment System are operationalised.

8) To have fair balance between the BC and Brick and Mortar Branches, it is mandated to open physical bank branches in all villages above population of 5000 in a phased manner. This will provide timely support to their BC network.

9) Creation of BC Registry Certification: Developing a BC registry not only ensure greater oversight on the functioning of BCs but would also provide more confidence to the end customers.

10) A scheme for graded certification training programme for BCs is also being introduced to enable BCs with good track record and advance training to handle complex tasks that are beyond deposits and remittances.

Third Phase of FI Plans for Banks (2016 – 19)

The focus is on mere granular monitoring of progress made by banks under FIPS at district level.

Demand side aspect of Financial Inclusion:

RBI believes that the goal of financial inclusion is difficult to achieve unless the demand side measures adequately supplement the supply side measures. Banks have opened about 440 million accounts under the push form RBI and the PMJDY. Now the focus should be on

enhancing capabilities so that the individual is in a position to not merely avail the offered services, but is also capable of demanding preferred products and services suitable to his/her need/choice.

been set up by various banks all over the country at the district level with the objective of short term training and long term hand holding with assistance to credit linkage for trainees .

11) RBI continued its efforts towards fulfilling the FI agenda during the year. The committee on Medium Term Path on Financial Inclusion (chairman: Shri Deepak

12) Mohanty) wasFinancial Literacy Centres (FLCs) / Rural Self Employment Training Instructions

For imparting efficacy to financial inclusion initiatives financial literacy is important. With the introduction of PMJDY, the emphasis on keeping new bank accounts operationally active. Therefore banks are advised to focus on financial literacy programmes through

i) Board Level policies for stronger financial literacy architecture;
ii) A tailor made approach to financial literacy and organising camps for different target groups;
iii) Following a concerted approach among various stake holders and the district /panchayat /village level (local officials of NABARD and the Revere Bank, district and local administration, block level official , NGOs, SHGs, BCs, farmers' clubs, panchayats, primary agricultural credit society and village level functionaries).

As at end March 2016 1,384 financial literacy centres were operational in the country, up from 1,181 FLCs at end March 2015. During the year end March 2016, 87,710 FL activities were conducted as against 84,089 activities during the preceding year.

13) Direct Benefit Transfer(DBT):

If entitlements under various state sponsored schemes start directly flowing into the bank accounts of individuals under DBT mode, it can act as a catalyst to encourage saving habit leading to build up of investment and seed capital for availing productive credit.

13)Rural Self Employment Training Institutes (RSETIs) have constituted to work out a medium term (5 years) measurable action plan. The committee submitted its report in December 2015. The committee reorganised that substantial progress had been made in terms of access to financial products and services specially after the launch of the PMJDY.

The committee identified significant gaps in terms of usage, inadequate last mile service delivery, exclusion of women and small and marginal farmers and very low formal link for micro and small enterprises.

Progress of Financial Inclusion:

i) The number of banking outlets in villages went up from 67,694 in March 2010 to 5,86,307 in March 2016 after RBI permitted appointment of BCs and laid out a roadmap for spreading banking services in rural India through a mix of bank branches and BC outlets. In addition, the number of urban locations covered through BCs has also surged from 447 in March 2010 to 1,02,552 in March 2016.
Out of 2259 rural bank branches opened during April 2015 to March 2016, 1670 branches were opened in unbanked rural centres under FIP. Around 71 million basic savings bank deposit accounts were added taking the total to 469 million by March 2016.

ii) The Basic Savings Bank Deposit Accounts(BSBDAs) have gone up from 73 million in March 2010 to 469 million as on March 31 2016. Under the PMJDY alone, until June 1, 2016, 220 million accounts have been opened with an approximate balance of Rs. 384 billion. After demonetisation the number of these accounts increased a lot.

iii) There were 47.31 million small farm sector credit accounts (Kisan Credit Card) and 11.3 million small non farm sector credit accounts (General credit Card) with an outstanding of Rs. 5130.7 billion and Rs. 1493.3 billion outstanding respectively as on March 31,2016. The number of small farm and non farm sector credit account stood at 24.3 million and 1.4 million respectively in March 2010.

iv) The total number of transactions in BC-ICT accounts which were around 26 million during 201-11 have been increased to 826.81 million as on March 31, 2016.

v) With the conclusion of FIP's Phase II (2013-16) on March 31, 2016 all domestic scheduled commercial banks (including RRBs) were advised to set new Board approved FIP targets for the next three years (April 2016 to March 2019)

vi) Banking facility for Unbanked :
At the end march 2016 as reported by the State Level Bankers' Committees (SLBCs), 4,50,686 villages (91.9% of the target) had been covered by 14,901 branches, 4,15,207 villages through BCs and 20,578 villages through other modes such as ATMS and mobile vans. SLBC convenor banks have been advised to open branches

in villages with population above 5000 to promote banking penetration and financial inclusion.

CONCLUSION

The country has come long way in the process of financial inclusion, but still has a long way to go. We were moving from mandates, subsidies and reliance on the public sector banks for inclusion. Now we are creating frameworks that attract and enable financial institutions to target the excluded. The interests of the excluded are protected through education, competition and regulation.

Financial inclusion will be an important element in ensuring access and equity necessary building blocks for the sustainable growth of our country.

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