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20-Year Financial Inclusion Plan - Milestones, Field Feedback and Monitoring

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Abstract

Financial inclusion is a process that enables improved and better sustainable economic and social development of the country. It focuses on raising the standard of living of the underprivileged people in the society with the objective of making them self-sufficient and well informed to take better financial decisions. Also, it acknowledges the participation of the low income groups based on the extent of their access to financial services in economic growth. India has been working on enhancing financial inclusion since 1955 when State Bank of India was nationalized, followed by more nationalization of banks in 1969 and 1980. A number of focused initiatives have been undertaken since 2005.The paper is forward looking and explores the scenarios in the next 20 years, identifies challenges and makes a few recommendations.

Key words: Financial inclusion, social security, MUDRA bank, Jan Dhan Yojana

Introduction

Financial inclusion is a process that enables improved and better sustainable economic and social development of the country. It focuses on raising the standard of living of the underprivileged people in the society with the objective of making them self-sufficient and well informed to take better financial decisions. Also, it acknowledges the participation of the low income groups based on the extent of their access to financial services in economic growth.

The Committee on Financial Inclusion (Government of India, 2008) defines financial inclusion as the process of ensuring access to financial services and timely and adequate credit where needed by vulnerable groups at an affordable cost. The aim of financial inclusion is delivery of financial services to low income groups with the provision of equal opportunities. The Report of the Committee suggested that financial inclusion must be taken up in a mission mode to achieve universal financial inclusion within a specific time frame and constitution of two dedicated funds focused on development and technology for better credit absorption by poor.

On the other hand, CRISIL (2013) measured the extent of financial inclusion in India in the form of an index and revealed that one in two Indians has a savings account and only one in seven Indians has access to banking credit. In short, CRISIL gave ground-level information regarding the progress of financial inclusion in the country.

A small sample, pilot survey, conducted in Bombay in early 2007, revealed that unbanked people were willing to have a bank account as it was considered economical and safe. Also, the loan could be availed at reasonable price during emergency and the monthly interest receipts on deposits was considered to be an additional source of income. In contrast, some people observed that there was no need for a bank account as they lacked capacity to save. Interestingly, people without bank account also feared that they would be asked to pay 'hafta' for opening and maintaining an account in a bank to the uniformed guard at the standing at the entrance of a bank. Also, the poor assume that banks are for rich and therefore they had very low desire in opening an account. Also, many unbanked poor felt that, minimum deposit while opening an account was too high for them, fixed timings of banking operations were too restrictive and non-cooperative behavior of the bank employees was discouraging.

The paper is arranged in five more sections after the above introduction. Section II gives an overview of the changes and progress of financial inclusion till March 31, 2014. Section III provides details of Pradhan

Mantri Jan Dhan Yojana. Section IV discusses the MUDRA bank and social security schemes announced recently. Section V presents various challenges in achieving success of financial inclusion. Section VI discuss about 20 - year plan for financial inclusion and necessary policy recommendations.

Section II: Financial Inclusion – Historical Developments

The progress in the development of financial inclusion in India can be examined by understanding the phases involved in extending it. The concept of examining financial access became important immediately after the results of the All-India Rural Credit Survey, completed in the 1950s, revealed that farmers relied heavily on money-lenders.

The efforts to usher financial inclusion have been recorded since nationalization of State Bank of India in 1955 followed by nationalization of other banks in 1969 and later in 1980. Other important measures included instituting priority sector lending, and issuing Kisan/General Credit Card. In the earlier years, urban areas had significantly large number of bank branches compared to rural areas. As the urban areas were concentrated with numerous bank branches, this resulted in higher absorption of bank credit in the urban areas. Such a condition continued in the country until the RBI rigorously started pursuing financial inclusion model in the mid-2000s.

Since 2005, GOI and Reserve Bank of India (RBI) have been initiating a number of concerted measures in order to promote and enhance financial inclusion. These include Business Correspondents (BCs) or branchless banking through different banking agents which ushered a paradigm shift. The GOI also initiated "Swabhimaan" campaign in 2011 to provide access to banking services to the excluded sections of the society (GOI, 2014c).

Despite these various measures taken by authorities, financial inclusion remained a distant dream with a majority of Indians still struggling with lack of access to banking services. Census 2011 reveals that, in India, out of 24.67 crore households only 14.48 crore (58.7 percent) households had access to banking services. In the rural areas, out of 16.78 crore households only 9.14 crore (54.46 percent) were availing banking services.[1] During the post liberalization period, there was a substantial progress in the economy but still majority of the sections of the society were not benefitting from such a progress. The percentage

[1] GOI (2014c).

of indebted agricultural households, a proxy for credit penetration, in different states of India in 2013 was not encouraging (Table 1).

Table 1: Proportion of Indebted Agricultural Households in 2013

States	Percentage of Indebted Agricultural Households	States	Percentage of Indebted Agricultural Households
Andhra Pradesh	92.9	Madhya Pradesh	45.7
Assam	17.5	Maharashtra	57.3
Bihar	42.5	Odisha	57.5
Chhattisgarh	37.2	Punjab	53.2
Gujarat	42.6	Rajasthan	61.8
Haryana	42.3	Tamil Nadu	82.5
Jharkhand	28.9	Telangana	89.1
Karnataka	77.3	Uttar Pradesh	43.8
Kerala	77.7	West Bengal	51.5
All India			**51.9**

Source: Government of India (2014b).

In order to overcome this grim situation, government rigorously pursued financial inclusion and there was substantial increase in banking network, opening of accounts and growth in deposits and credit (Tables 2, 3 and 4).

Table 2: Financial Inclusion Progress: Banks and RRBS

Particulars	Year Ended 2010	Year Ended 2011	Year Ended 2012	Year Ended 2013	Year Ended 2014
Banking Outlets in Villages					
a) Branches	33,378	34,811	37,471	40,837	46, 126
b) Branchless Mode	34,316	81,397	144282	2,27,617	3,37,678
c) Total	**67,694**	**1,16,208**	**1,81,753**	**2, 68. 454**	**3, 83, 804**
Urban Locations through BCs	447	3,771	5,891	27,143	60,730
Basic Saving Bank Deposit A/c- branches					
a) No. in million	60.19	73.13	81.20	100.80	126.00
b) Amt. in Rs. billion	44.33	57.89	109.87	164.69	273.30
Basic Saving Bank Deposit A/c- BCs					
a) No. in million	13.27	31.63	57.30	81.27	116.90
b) Amt. in Rs. billion	10.69	18.23	10.54	18.22	39.00
Overdraft facility availed in BSBDA's account					
a) No. in million	0.18	0.61	2.71	3.92	5.90
b) Amt. in Rs. billion	0.10	0.26	1.08	1.55	16.00
KCC					
a) No. in million	24.31	27.11	30.24	33.79	39.90
b) Amt. in Rs. billion	1240.10	1600.05	2068.39	2623.00	3684.50
GCC					
a) No. in million	1.40	1.70	2.11	3.60	7.40
b) Amt. in Rs. billion	35.10	35.07	41.84	76.30	1096.90

Source: GOI (2014c), RBI (2014) and RBI (2013).

Table 3: Deposits and Credit of Scheduled Commercial Banks (Number of Accounts)*

Year	Deposit		Credit	
	Rural	Urban	Rural	Urban
2001	24812283 (58.0)	17990636 (42.0)	3650098 (69.7)	1586341 (30.3)
2011	462296734 (57.1)	347832619 (42.9)	67802446 (56.2)	52921649 (43.9)
2014	747146277 (60.9)	479563894 (39.1)	86186161 (62.1)	52564721 (37.9)

*Rural includes semi urban; Urban includes metropolitan.
Note: Figures in parenthesis are percentage to total.
Source: RBI.[2]

[2] Basic Statistical Returns of Scheduled Commercial Banks in India, RBI.

Table 4: Deposits and Credit of Scheduled Commercial Banks*

(Amount in Rs. Crore)

Year	Deposit		Credit	
	Rural	Urban	Rural	Urban
2001	32561 (34.3)	62381 (65.7)	11616 (21.6)	42226 (78.4)
2011	121009 (22.5)	417945 (77.5)	67738 (16.7)	339825 (83.4)
2014	192822 (24.2)	602749 (75.7)	118870 (19.0)	509337 (81.1)

*Rural includes semi urban; Urban includes metropolitan.
Note: Figures in parenthesis are percentage to total.
Source: RBI.[3]

In addition, there were nearly 28 crore accounts in post offices with savings account numbering more than 13 crore and recurring deposits of more than 11 crore.[4] Although, various initiatives had been undertaken in order to financially include all sections of society, the success of such measures had remained partial.

Section III: Pradhan Mantri Jan Dhan Yojana

In August 2014, the GOI initiated Pradhan Mantri Jan Dhan Yojana (PMJDY) which aimed at ensuring universal access to financial services viz. banking and deposit accounts, remittances, credit, insurance and pension in an affordable manner. Among various measures initiated by GOI, PMJDY has been successful in opening nearly 9 crore accounts in the rural areas (Table 5).

Table 5: Progress of PMJDY as on May 13, 2015

(All figures in Crore)

No.	Banks	No. of Accounts			No. of Rupay Debit Cards	Balance In Accounts (Rs.)	% of Zero Balance Accounts
		Rural	Urban	Total			
1	Public Sector Banks	6.63	5.56	12.19	11.39	13087	54.55
2	Private Banks	0.38	0.26	0.64	0.58	920	50.00
3	Regional Rural Banks	2.35	0.41	2.76	1.99	2912	55.43
	Total	9.36	6.23	15.59	13.96	16919	54.52

Source: GOI (2015a).

[3] Basic Statistical Returns of Scheduled Commercial Banks in India, RBI.
[4] Other accounts in post offices include time and fixed deposits.

PMJDY is also included in the the JAM number trinity, i.e. Jan Dhan Yojana-Adhaar-Mobile Number, which focuses on providing support to the poor households in a targeted way. The main objective of the JAM trinity is linking the Adhaar number to an active bank account in order to implement income transfers. Also, with the introduction of PMJDY, the total number of bank accounts is expected to increase and thereby targeting transfer of financial resources to the poor households.

Section IV: Mudra Bank and Social Security Schemes

Mudra Bank

In April 2015, the GOI introduced Micro Units Development Refinance Agency (MUDRA) bank to focus on providing credit to small entrepreneurs. As PMJDY aimed at providing banking services to the unbanked, MUDRA bank (MB) would fund the unfunded in the country. Earlier, the Finance Minister in the Union Budget speech had announced a firm belief that development has to generate inclusive growth which cannot be completely addressed by large corporate and business entities. There were nearly 6 crore enterprises, mostly individual enterprises, running small manufacturing, trading or service business and only 4 percent of such units received institutional finance.

MB with a corpus of Rs.20,000 crore and credit guarantee corpus of Rs.3,000 crore is to be used to refinance and assist those financial institutions who finance micro enterprises in India. Thus, MB will act as a regulator and a refinance institution for micro-finance institutions (MFIs) which lend to very small units to help them develop.

The businesses covered under MB would include small manufacturing units like shopkeepers, fruits and vegetable sellers, hair cutting saloons, beauty parlours, transporters, truck operators, hawkers, repair shops and artisans with financing requirements of up to Rs.10 lakh.

MB is also offering development support across the entire spectrum of beneficiary segments. The key areas include supporting financial literacy, promoting and supporting grass root institutions and creation of framework for small business finance entities. The roles envisaged for MB would include laying down policy guidelines for micro enterprise financing business and responsible financing practices to ward-off over indebtedness, ensure proper client protection principles, and methods of recovery.

MB would help in preparing policy guidelines, as well as enforcing client protection principles so that small scale enterprises are not cheated to pay more than what is the standard rate prevailing in the country. Also, through the MB, a data base of MFIs, in India will be built so that micro enterprises will have the option to choose between different lenders. MB will also partner regional and local level institutions so that even the weaker sections of the society are able to access funds at reasonable rates of interest.

The setting up of MB can raise an issue whether there was a need for another regulator and refinance agency. The country already has RBI, National Bank for Agriculture and Rural Development (NABARD) and Small Industries Development Bank of India (SIDBI) who are playing a prominent role in the domestic market by extending financial services to the unbanked. However, in view of the success of PMJDY, a new gap clearly emerged and that was the financing of the micro sector. The RBI, set up in 1934 regulates and supervises the banking system. From the RBI, to focus on rural and agriculture sector, NABARD was set up in 1982. Similarly, SIDBI, was set up in 1990 to help finance and develop small, micro and medium enterprises. Now, in 2015 MB has been set up to take over some activities from NABARD, SIDBI and RBI, with focus exclusively concentrated on the micro sector.

In addition, though financial inclusion has been pursued by commercial banks for many decades, the focus on the micro sector was missing. Small and micro entrepreneurs were generally cut-off from the banking system because of limited branch presence. Now, MB will partner with local coordinators and provide finance to small and micro business enterprises.

Also, a single regulator for all entities engaged in micro finance activities could lead to standardizing the formats and documents for the sector as well as regular monitoring and evaluation. It could also establish golden rules for the industry to be uniformly practiced for delivery of services to the poor.

MB is expected to provide increased access to low cost funding in the micro finance sector. Partnership with different agencies and cooperation with state level banker's committee could lead to a focused approach in extending financial services to areas which were not adequately covered by formal institutions so far.

Social Security Schemes

On May 9, 2015, having successfully achieved the distinction of ensuring that more than 95 percent of Indian households have bank accounts through the PMJDY, in a logical and well sequenced step, the Central government extended social security to the masses, soon after launching the MB to ensure adequate flow of credit to micro units. The extension of these products will ensure business volumes to the banking industry which will carry new instruments to the masses and help in making financial inclusion commercially viable. The structure of the schemes entails contribution, though nominal, by the individual subscribers to minimize the risk of exploitation and moral hazard.

The flagship scheme, Atal Pension Yojana (APY) will provide old age income security to the working poor in the unorganized sector while addressing the longevity risks amongst the workers constituting nearly 88 per cent of the total labour force of 47 crore. The APY would provide fixed monthly pension of Rs.1, 000, 2,000, 3,000, 4,000 and Rs.5,000 respectively from the age of 60 years depending on the contribution. The amount of monthly contribution would have to be paid through a bank account.

The Prime Minister has also announced the Jeevan Jyothi insurance scheme providing a one year cover, renewable annually, offering life insurance for death. The scheme again envisages a savings bank account and will be administered through life insurance companies in arrangement with banks. The third scheme is the Suraksha insurance scheme, renewable annually, providing insurance to cover death or disability on account of an accident. The scheme will be operated through general insurance in arrangement with banks. All savings bank account holders are eligible to join and the premium of Rs.12 per annum will be shared between insurance company, agent and bank.

These three schemes will ensure financial inclusion, enhanced business opportunity for banks and higher insurance penetration, thus providing economic security to people in the unorganized sector.

Section V: Challenges of Financial Inclusion

The key challenges are –

1. **Accounts are not operative -** Most of the bank accounts are not operative due to lack of funds with account holders. The cost effectiveness aspect, given low balances in accounts, in implementing technological advancements is a matter of concern.
2. **Lack of financial literacy -** The rural households do not have adequate financial literacy resulting in lack of awareness of many financial services provided by financial institutions.
3. **Too large volumes of Accounts** – There is a need for technical and institutional infrastructure for e-payment systems to service large number of new and existing accounts.
4. **Need for Manpower planning** – There is a requirement of sufficient technical skill development and training for banks and institutional staff.
5. **Secure Environment -** The security of electronic transactions is a matter of concern especially with large number of new accounts.
6. **Malpractices** – Illustratively, in some locations, people were persuaded to pay an amount ranging between Rs. 1000 – 3000 while opening a bank account under PMJDY.
7. **Ease of transaction-** Lack of ease in transaction related activities in banks is clearly demonstrated by repetitive behavior of rural households' persistence in taking loans from the money lenders.

Further, there are many other challenges which need to be addressed in order to effectively achieve financial inclusion –

1. **Low penetration of banks -** Also, there is lower percentage of new bank branches opened in the unbanked areas and lower percentage of 'no-frills' accounts with overdraft facility.
2. **Low level of credit extended against accounts -** Metropolitan centres accounted for more than half of the total banking business of the Indian banking sector whereas rural areas accounted for only a small proportion of credit (8.4 per cent as of March 2014).
3. **Need for greater use of technology** - On the operational side, despite the convenience offered by ATMs in providing banking services, the debit card penetration continued to be low with only 30 per cent of deposit account holders having a debit card.
4. **Demand Side Factor -** Factors such as lower income or asset holdings, lack of awareness about the financial products, perceivably unaffordable products, high transaction costs, products which are not convenient, inflexible, not customized and of low quality are the major barrier for gaining access to the financial system.
5. **Costs and risks in using technology -** Costs in terms of increasing expenditure on IT deployment and risks in terms of monetary loss, data theft and breach of privacy are a concern. Thus, banks need to be extremely cognizant of such risks.
6. **BCs high attrition rate** - High attrition rate of BCs is another challenge of financial inclusion which needs more focus and attention.
7. **Cyber Security -** Nearly 16 crore new accounts, have been opened in 8 months and many of these are first time users. This can be a threat to cyber security especially when know-your-customer norms have been diluted.
8. **Overlapping Instructions -** The creation of MB would require that the existing regulators need to ensure that there are no overlapping of guidelines and instructions, so that implementing agencies at grass-root level are not confused. This is especially relevant because the RBI is envisaging giving licenses for small banks and many existing MFIs have already applied for license too.

Section VI: 20 year Plan for Financial Inclusion and Select Recommendations

In the last 20 years, substantial changes have taken place in the banking and financial industry, in India and abroad. The commercial viability of financial inclusion has been established and the governments, globally, have been making efforts to extend financial services to large segment of the population because financial inclusion promotes economic equality and economic growth. Financial institution provide low cost access to banking facilities, safe guarding funds and providing convenient accounting in addition to rewarding depositors with interest payment. Banks intermediate between savers and investors and thereby provide resources for growth. Therefore, people may not have savings but may have need for resources which can be used for generating employment as well as stirring activity in the economy.

In India, financial inclusion has witnessed different spurts of growth as already discussed in earlier sections. The strongest impulse was provided by the Prime Minster in August 2014 by virtue of which nearly 16 crore accounts have been opened in the last eight months. The scenario for the next 20 years may have to take into account the following –

a) Indian economy is closely associated with agriculture and rural activities because nearly 70 percent of the population still resides in rural areas.
b) India accounts for 16 percent of world population and only 4 per cent of water resources. The critical shortage of water would become apparent for the agriculture sector especially with rising population.
c) The impact of climatic change because of global warming would be apparent on food production in terms of unseasonal rain falls, El Nino and similar natural phenomena.
d) The climatic change would also impact wheat production and quality of wheat with rise in temperature as well as production of rice because of depleting water levels.
e) The scarcity of land, because of rising population as well as increasing urbanization and industrialization would imply higher cost of producing food grains and agricultural production. Thus, the burden on the common man would be higher.
f) As on March 31, 2014 there were 123 crore deposit accounts holding Rs. 80 lakh crore as compared with 14 crore credit accounts, accounting for Rs. 63 lakh crore. In addition Post Offices hold 28 crore accounts with amount of Rs.4 lakh crore.
g) The Jan Dhan accounts have resulted in creating nearly 16 crore new accounts in banks with a balance of Rs. 17,000 crore. In addition, the Prime Minster has announced social security schemes which will operate through the banking system. Further MUDRA bank will also encourage banking activity at the lower end of the economic spectrum.
h) The new accounts under Jan Dhan as well as other schemes that have recently been announced would result in opening of accounts and expectations of banking services at places which do not have bank branches and would need to be serviced through the business correspondent model. This would imply higher cost of serving at remote places by commercial banks.
i) The government has announced that it would directly transfer resources to the people using technology as well as bank accounts. The direct benefit transfers would imply additional financial resources with the public, generally low income group. These financial resources would be in addition to resources that would be available in the rural areas on account of gold monetization scheme. The higher food prices are also leading to increase in purchasing power of the rural areas.
j) The proportion of population that would emerge out of poverty would need to be estimated. In view of rising prices of water and food, poverty levels may not improve and therefore financial inclusion would continue to be a challenge for the bankers and policy makers.
k) In view of the increasing complexity of financial resources in the rural sector there may be a need for a regulator.

An issue of interest rates

It is necessary to examine the factors that impede financial inclusion. One significant factor is interest rates. It needs to be recognized that though the money lender is generally blamed for charging high interest rates, they have survived many generations in the same neighborhood. Interestingly, it emerges that borrowers tend to go to the money lender ignoring a branch of a commercial bank, even if it is closer. Therefore, there is need to study the reasons as to why money lender is popular and persistently successful despite high interest rates. There is a probability that it may not just be the interest rate that is a factor that influences borrowing decisions. After all, historically, according to literature, Chanakya's interest rate structure was risk-weighted, and the rate of interest would increase with the risk involved in the borrower's business. Illustratively, interest rates that prevailed in ancient India were 15 percent per annum for general advance while traders were charged a rate of 60 percent. If the goods were to pass through the forest, the trader had to pay 120 percent while those engaged in export and import business had to pay 240 percent per annum.

Policy Recommendations

Some of the policy recommendations to be considered to improve the extent of financial inclusion are –

Commercial Viability

Success of financial inclusion depends upon the commercial sustainability of the operations and not on subsidies and incentives. Therefore, to achieve sustainability, volumes through suitable instruments is necessary.

Instruments

a. There is a requirement for need based innovative products especially tailored for poor segments of the society.
b. Also, specially designed content and appropriate delivery mechanism of the material and instruments are needed which are suitable to the particular targeted group.
c. Banks should create demand-oriented savings, credit and remittance products that are customized to lifestyle pattern and income streams of the population they are aiming to serve.
d. There should be disbursement of bank loans in collaboration with other financial services like insurance and pension schemes.

Financial Literacy

a. There is a need for the expansion of the counseling and advisory services on financial literacy in order to reach the vulnerable sections.
b. There is a requirement to tailor differential literacy and counseling mechanisms depending upon the need of different segments of the society. In this context, literature in different languages and different medium needs to be considered.

Technology

a. Incentivizing usage of Plastic cards and e-commerce in the economy.
b. Mobile banking has tremendous potential and the benefits of mobile-commerce need to be explored to enhance banking penetration.
c. There would be a need to explore out-of-box methods for mass banking. TV can be helpful in banking transactions and spreading financial literacy.

Institutions

a. There is an increasing need for an institutional focus on the emerging complexities in the rural market.
b. There is a need to focus on synergy between post-offices and ATMs. ATMs could be opened in post offices. Provision of electronic card reading machines could also be considered in post offices to facilitate transactions.
c. To avoid duplicate banking between post office and banks, banking activities should be restricted to banking institutions exclusively. The Post Offices which started banking in late 1800's in absence of commercial banks then, should not be allowed to compete with banking activities during the present times, when commercial banks are active.

Regulations

There is a need for regulating the formal and informal financial institutions who are competing for collecting savings of rural people and offering credit. NABARD could be tapped to ensure smooth development of rural financial markets.

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