ISSN 2320-5407 International Journal of Advanced Research (2014), Volume 2, Issue 2, 649-655

ISSN NO. 2320-5407

Journal homepage: http://www.journalijar.com

INTERNATIONAL JOURNAL OF ADVANCED RESEARCH

RESEARCH ARTICLE

FINANCIAL INCLUSION -THE WAY TOWARDS INCLUSIVE GROWTH

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Manuscript Info

Manuscript History:

Received: 12 December 2013
Final Accepted: 15 January 2014
Published Online: February 2014

Key words:
Financial Inclusion, Financial Inclusion Policy, Financial Literacy, Voluntary Exclusion, Inclusive Growth, Financial Institutions.

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Abstract

Inclusive growth as the literal meaning of the two words refers to both the pace and the pattern of the economic growth. The inclusive growth approach is long term in nature which focuses on the productive employment which increases the means of incomes of the excluded section. Inclusive growth allows people to contribute to and benefit from economic growth. The eleventh five year plan (2007-2012) envisions inclusive growth as the key objective. In this paper the authors explores how financial inclusion acts as a means towards the inclusive growth of the vast excluded population. “Financial inclusion is the process of ensuring access to appropriate financial products and services needed by vulnerable groups such as weaker sections and low income groups at an affordable cost”. Reserve Bank of India in collaboration with the Government of India had formulated a policy namely Financial Inclusion Policy (2005) for financially including of the excluded. The policy was framed with the objective of employment generation, asset creation and income increase which would help in the upliftment of the weaker or poor people. Also, the paper recognises the challenges which hinder the inclusion of the excluded section and the possible opportunities which can be explored for the inclusion. Formal financial institutions, NGOs and SHGs help in the inclusive growth through financially including the low income and weaker section of the population.

Introduction

The concept of inclusive growth has gained wide importance in several countries including India (Bolt, 2004). Inclusive growth implies participation in the process of growth and also sharing of benefit from growth. Growth is considered to be pro-poor as long as poor benefit in absolute terms, as reflected in some agreed measure of poverty (Ravallion and Chen, 2003). Growth with equity is the only road to success. It has been globally recognized that high national income growth alone does not address the challenge of employment promotion, poverty reduction and balanced regional development. Nor does growth in itself improve human development. Consequently, all the efforts of government – in agricultural and rural development, in industry and urban development, in infrastructure and services, in education and health care – sought to promote inclusive growth.

A rapidly modernizing economy needs effective social, economical and financial policies for those who had left behind. From 2006-2010, the growth rate was arranged at 8.6% making India as one of fastest growing economies in the world, but the growth is not equitable. The Eleventh Five Year (2007-2011) Plan provides “an opportunity to restructure policies to achieve a new vision based on faster, more broad-based and inclusive growth. It is designed to reduce poverty and focus on bringing the various divides that continue to fragment our society” (GOI, 2006: 1). The policies aim at increasing the income and employment opportunities on the one hand and on the other hand it tries to finance programmes which are capable of making the growth more inclusive.

Rural areas, where 70% of Asia’s poor live, continue to lag behind and the reasons identified were (1) limited access to financial services; (2) poor infrastructure, notably power, transport, and communications; (3) limited information about market opportunities; (4) a lack of education and training; and (5) limited access to new technologies, including information and communication technology. Hence greater efforts are required for them to participate in trade and growth. In this paper the authors tries to explore the role of government of India (GOI), Reserve Bank of India (RBI) & financial institutions in the inclusive growth of the excluded.

Financial Inclusion –The Way Towards Inclusive Growth

Savings and investments help in poverty alleviation and also add to GDP growth in any economy**.** But accessing of formal financial system is still a distant dream to a vast section all over the world, and India is not an exception to it. Financial exclusion leads to social exclusion. The excluded section comprise of the marginal farmers, landless laborers, self employed, and unorganized sector, enterprises, urban slum dwellers, migrants, ethnic minorities and socially excluded group, senior citizens and women (Rangarajan Committee Report). The policies for tackling financial exclusion offers integrated solutions for social exclusion also (Marshal 2004).

Literature review

Empirical evidence using household data indicates that access to basic financial services such as savings, payments, and credit can make a substantial positive difference in poor people's lives (Caskey, Duran, and Solo 2006), Dupas and Robinson, 2009). Access to a well functioning financial system, by creating equal opportunities, enables economically and socially excluded people to integrate better into the economy and actively contribute to development and protects themselves against economic shocks. A large body of empirical literature suggests that developing the financial sector and improving access to finance may accelerate economic growth along with a reduction in income inequality and poverty (RBI).

Substantial proportion of households, especially those with low income and those living in rural and remote areas are at present outside the ambit of formal financial system. The impact of financial exclusion is experienced not by the individual itself but their families and their households and their communities and wider society. The impact of financial exclusion includes: **a)** barriers in accepting employment as employer want to pay the salary directly to bank account, **b)** higher cost in bill payment, **c)** no access to affordable credit, **d)** high cost from door step money lender, **e)** unable to save money in a safe custody**, f)** no insurance coverage, **g)** unable to manage what little money they have, **h)** lacks financial literacy (Kempson, 2004, Allison & Deborah 2005).

Now the question is why are they excluded from the formal financial section? The literature reveals that ; **a)** Identity requirements (Collard et al, 2001; Connolly and Hajaj, 2001; Department of Finance, Canada, 1998; Kempson et al, 2000), **b)** Terms and conditions (Caskey 1997; CLCV, 1999; Department of Finance, Canada, 1998; Kempson et al, 2000), **c)** Bank charges, **d)** Refusal by banks, (Belgium, Bayot, 2002; TestAchats, 2001), the UK (Collard et al, 2001; Kempson and Whyley, 1998; Kempson et al, 2000) the US (Belsy and Calder, 2004; Caskey, 1997; Kempson et al, 2000) and Canada (Department of Finance, Canada, 1998), **e)** Physical access problems caused by bank closure (Caskey 1997; CLCV, 1999; Department of Finance, Canada, 1998; Kempson et al, 2000), **f)** Psychological and cultural barriers, **g)** Social security problems (Kempson and Whyley, 1998; Kempson and Whyley, 1999) etc are concerned to be the problems of financial exclusion (Eline and Kempson, 2004). Lacking financial products can contribute to more general social exclusion and most households in this position identify key areas of unmet need (Kempson & Whyley 1999).

In order to include these excluded to the formal financial sectors, financial inclusion was introduced. Government all over the world took various initiatives for financial inclusion. India was also not an exemption to it. The Reserve Bank of India also introduced various measures to encourage expansion of financial coverage in the country.

Defining Financial Inclusion:

"Financial inclusion may be defined as 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."

: - Rangarajan Committee Report, 2008

Financial inclusion is the delivery of banking services at an affordable cost to the vast section of disadvantaged and low income group and to have unrestrained access to public goods and services is the sine qua non of an open and efficient society. Financial inclusion is considered essential for fostering economic growth in a more inclusive fashion in a developing country like India.

How financial inclusion leads to inclusive growth?

For financial inclusion to promote growth, it has to move from “opening an account” in the Bank, to regular savings and finally to a relationship which enables the borrower to access loans on a regular basis. Inclusive Growth happens through financial inclusion because it helps in satisfying the following objectives.

Economic objectives	**Social and Political Objectives**
Equitable Growth	Poverty Alleviation
Mobilization of Savings	Sustainable Development
Larger Markets for the Financial System	Wider Inclusion in Society
	Effective Direction of Government Programmes

Initiatives of RBI for Financial Inclusion

The following is a summary of the key national financial inclusion initiatives over the last four decades so that it may help in the economic development of the poor and thereby the country’s inclusive growth.

1960s, 70s

- Focus on increasing credit to the neglected economy and weaker sections of society.
- Development of the rural banking ecosystem including RRBs, rural and semi-urban branches.
- Implementation of the social contract with banks.
- Lead Bank Scheme launched for rural lending.

1980s, 90s

- Branch licensing policy to focus on expansion of commercial bank branches in rural areas.
- Establishment of National Bank for Agriculture and Rural Development (NABARD) to provide refinance to banks providing credit to agriculture.
- SHG-Bank Linkage Program launched by NABARD.

2000s

- The term 'Financial Inclusion' was introduced for the first time in RBIs’ Annual Policy Statement for 2005-06 and a policy namely “Financial Inclusion Policy” was framed.
- 100 percent financial inclusion drive launched.
- Restrictions on ATMs deployment removed.

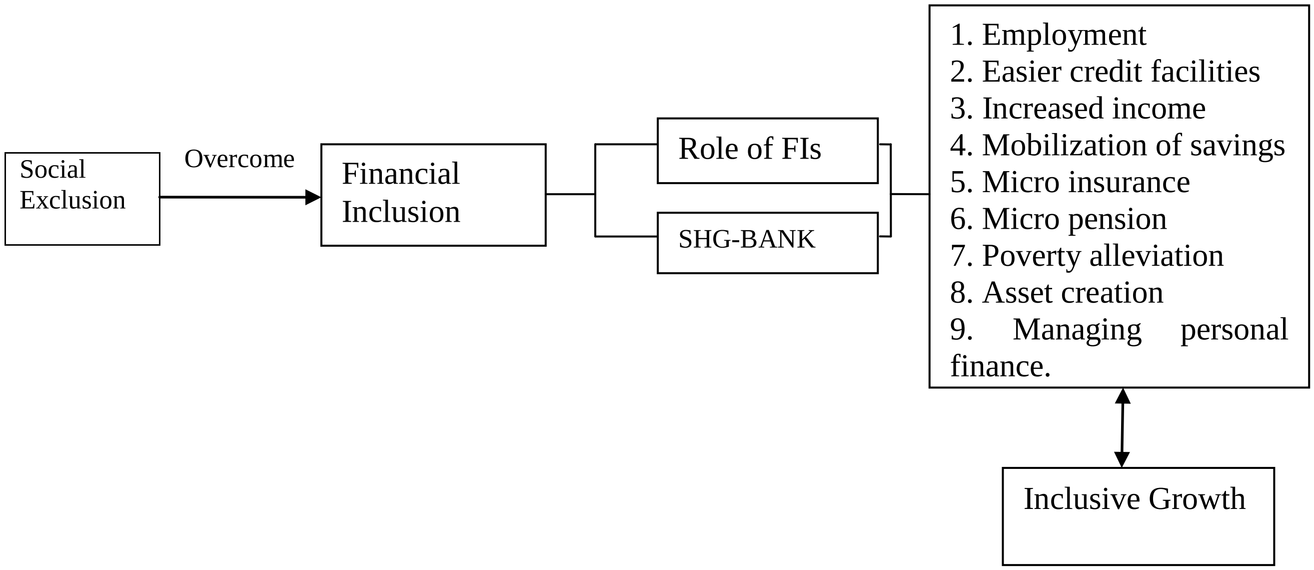
The above mentioned are the various measures undertaken for financial and economic benefit of the vast disadvantaged section. But still more than half of the population remains socially and financially excluded from the formal financial sector. Hence in the year 2005 a Policy namely Financial Inclusion Policy was introduced by RBI according to the instruction of GOI.

Financial inclusion policy comprises the following:

1. No Frills Accounts
2. Simplification of KYC norms
3. Use of Intermediaries
4. Introduction of General Credit Cards
5. Use of Technology
6. Use of Regional Language
7. One-time Settlement
8. Financial Education

Financial Inclusion-Inclusive Growth Model

Financial inclusion helps in striking a balance by channelizing the surplus to deficit units and brings the poor and disadvantaged one under the growth allegory. The concept “Inclusion” should be seen as a process of including the excluded as agents whose participation is essential in the very design of the development process, and not simply as welfare targets of development programe (Planning Commission, 2007).



[Financial Inclusion- Inclusive Growth Model (prepared by the authors itself)]

- **Social Exclusion**:
  Social Exclusion means excluding from the society due to unequal distribution of income within the economy. From the literature it was clear that social exclusion leads to financial exclusion also. Hence the way out for social inclusion is to financially include these weaker sections to the formal financial sector. By including them to the formal financial sector it would help them in easy assessing of credit and also various financial services can be availed. And it would help them increased income and thereby their standard of living can be increased. Financial inclusion could be achieved either through financial institutions or through an intermediary of the bank.
- **Financial Inclusion:**
  From the model the author tries to explain that social exclusion can be overcome by financially including them. Through the various policies low income and weaker section of the society will be able to avail various financial services when needed. Financial inclusion would also help in preventing the exploitation of the poor by the informal money lenders.
- **Role of financial institutions (FIs):**
  Banks and other financial services players largely are expected to mitigate the supply side processes that prevent poor and disadvantaged social groups from gaining access to the financial system. Financial institutions like Banks, other formal financial institutions and post office play an intermediary role between the excluded and financial products. These institutions mobilize the savings and lend them to the needy. Thus it would help the poor in better utilization of what little money they have. Also as a part of financial inclusion policy (2005) the RBI had liberalized the procedures in availing various financial service in the formal financial institutions. Hence the poor would be better served. The financial institutions were instructed to reach the poor either by opening a branch or through Business Correspondents and Business Facilitators. BCs and BFs would be appointed by the bank and adequate training is given to them about the various banking services available. BCs and BFs would meet the residents in rural area once or twice a week (varies according to bank) and would do the transactions. Hence the daily wage earners need not lose their income for visiting a financial institution for making a small transaction. Figure 1 and Figure 2 shows the penetration of banks in the unbanked areas and which had led to the economic development of poor

- **SHG-Bank Linkage Program:**
  This is one of the most popular and successful model which has being incorporated by RBI for financially including excluded section in the society. There are mainly three types of SHG-Bank Linkage models, such as (a) SHG formed and Financed by banks, (b) SHG formed by formal agencies other than banks but financed by banks, (c) SHG financed by banks using NGOs and other Agencies as financial intermediaries. Among the rural India SHG-Bank linkage program had helped in reducing poverty of the illiterate and weaker section. Easy access of money was a major factor which hinders the economic development of the poor. SHG-Bank linkage program had helped the way out by proving micro-finance to the needy. The SHGs are usually guided by NGOs – Non-Government Organizations, who help them in investing the micro loans in economically viable projects. SHG is given loans against the Group members' guarantee. Peer pressure within the group helps in improving recoveries. Through SHG - Bank linkage model, nearly 40 million households are linked with banks. Fig: 3 explains the amount of loan availed through SHG and micro –finance institutions, which means the money had led to the development of many in rural and poor people who are in needy.

- **Inclusive growth**:
  Inclusive growth means overall development of the economy. In the model the author reaches a conclusion as through financial inclusion the poor would have various advantages such as employment, income generation, asset creation, easier credit facilities, mobilization of savings, and etc. all these would help in poverty alleviation in the economy.

Conclusion

Financial inclusion is an important step towards inclusive growth. It helps in the overall economic development of the disadvantaged poor. Financial inclusion is also considered to be a business opportunity for the formal financial institutions. It would help them in penetrating into unbanked areas and thereby attaining profit. Besides the bankers, the developmental authorities also have a major role in developing the supportive infrastructure, both physical and social. Literacy, health and communication are some of the essential ingredients needed for inclusive growth. In this paper the authors had tried to explain how financial inclusion can help in the inclusive growth of the economy. To conclude, the four pillars of inclusive growth are productivity, employment, financial inclusion and infrastructure development.

"We have believed - and we do believe now - that freedom is indivisible, that peace is indivisible, that economic prosperity is indivisible"

: - Late Prime Minister Indira Gandhi

I. Banking coverage (Fig;1)

All India	2003	2008	2012
	16.00	15.00	12.7

(Source: Trends and progress of banking in India, 2010-2011)

II. Financial inclusion: Number of villages covered in Financial Year 2011 (Fig; 2)

Banks	No: Villages Covered
Public sector banks	26630 (118%)

Regional rural banks	2792 (81%)
Private sector banks	143 (60%)
Co-operative banks	4 (3.5%)
Total	29569 (108%)

(Source: Trends and progress of banking in India, 2010-2011)

III.Progress of Micro-finance program:(Fig:3)

ITEM	Number (In millions)			Amount(Rs million)		
SELF HELP GROUP						
Loans disbursed by banks during the year.	1.61	1.59	1.20	122540	144530	145470
Loans outstanding with banks.	4.22	4.58	4.79	226800	280380	312210
Savings with banks.	6.12	6.95	7.40	55460	61990	70160
MICRO–FINANCE INSTITUTIONS						
Loans disbursed by banks during the year.	581	691	469	373200	806300	760500
Loans outstanding with banks.	1915	1513	2176	50090	101480	106890

(Source: Trends and progress of banking in India 2010- 2011)

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