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THE DIMENSIONS OF FINANCIAL INCLUSION OF UNDER-PRIVILEGED SECTIONS OF THE SOCIETY IN INDIA - A REVIEW

J. Praveen Paul and M. Silambarasan
Department of Management Studies, Mepco Schlenk Engineering College, India

Abstract

Financial inclusion (FI) has received renewed attention of researchers and policy makers in all countries. FI refers to households accessing institutional credit including commercial banks, cooperative banks, self-help groups, and credible microfinance institutions. Many financially underprivileged people of the society are exploited by moneylenders at very high interest rates because they do not use the banking system. It is therefore necessary to design appropriate policy for FI. This review paper is part of a project sponsored by the ICSSR-IMPRESS. This project creates a model in which the opinion leaders and influencers such as panchayat ward members, panchayat presidents, and PDS workers of the underprivileged sections of the society are roped in to be educated on the benefits of using the mainstream financial instruments, thereby, making banks as their primary and major source of savings and financial transactions. This will enable them to escape from loan sharks, moneylenders, pawn brokers and lead an enriched life and help in the growth of our economy and nation.

Keywords:

Financial Inclusion, Underprivileged, Panchayat, Microfinance

1. INTRODUCTION

This review paper is part of a project sponsored by the ICSSR-IMPRESS. The primary goal of the project is to create a model for financial inclusion (FI) of the underprivileged of the society. The main objective of rural development is to improve the quality of life of the rural people by eradicating poverty through the instrument of self-employment and wage employment programmes, by providing community infrastructure facilities such as drinking water, electricity, road connectivity, health facilities, rural housing and education, promoting decentralisation of powers to strengthen the Panchayati Raj institutions, etc [1]-[3].

Financial inclusion is imperative for rural development. It acts as a lubricant, which oils the wheels of development [4]. It assists millions of poor rural households who are out of reach of financial services through micro credit, micro savings, money transfers, micro insurance, etc. [5]. In India, about 70% of rural households have no access to financial services, but the need for financial services arises for the purchase of agriculture inputs, obtaining veterinary services, maintaining infrastructure, contracting labour for planting/harvesting, transporting goods to markets, managing peak season incomes to cover expenses in low seasons, investing in education, shelter, health, etc. [6]-[8]. The new rural finance paradigm is premised on the fact that rural people are bankable. Ensuring their financial inclusion can unlock the considerable economic potential of rural areas which ultimately leads to overall rural development [9].

Financial inclusion has become central to the Indian policy making over the past few years and various attempts to expand the scope of financial inclusion have been made. On November 14, 2018, the Prime Minister said that financial inclusion has become a reality to 1.3 billion Indians. In the past three years, under Jan Dhan Yojana, the government was successful in opening 330 million new bank accounts. The PM said that these are 330 million new identity, dignity and opportunity created for the under privileged.

Although the Government of India has given enormous thrust on the financial inclusion of the Under-privileged Sections of the Society, and has made a large section of the society to have a bank account, it is still a challenge to convince the people to use the system regularly to the fullest possible extent. This review aims to understand the implications of FI on the Under-privileged Sections of the Society and to use banks to the fullest possible extent and deliver the banking services to the vast sections of disadvantaged and low-income groups.

Selected researches carried out in many parts of the world including India regarding Financial Inclusion are discussed below.

2. 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 [11]. According to recent data from the Global Financial Inclusion database [12], worldwide, 57% of adults report having saved money in the past 12 months, but only 27% have done so in a formal institution [12]. For India, figures amount to 38% of individuals reporting current accumulation of savings, but only 14% had savings in a formal institution. In 2006, a first ‘financial inclusion program’ was launched by the Reserve Bank of India (RBI), whose main objective was to provide a bank account for all households with a fixed address, with a particular focus on rural areas [13].

In the case of credit, the proper definition of the financially excluded would include households who are denied credit in spite of their demand. Although credit is the most important component, financial inclusion covers various other financial services such as savings, insurance, payments and remittance facilities by the formal financial system to those who tend to be excluded [14]. Recently the issue of financial inclusion has received renewed attention of researchers as well as of policy makers of both developed and developing countries.

In a broad sense, financial inclusion refers to delivery of formal financial services to each and every member of an economy. The dimensions of financial inclusion are shown in Fig.1. Thus, financial inclusion can be defined as a process that serves to remove the barriers and overcome the inabilities of some societal groups and individuals, including the poor and disadvantaged, to access and use low-cost, fair and safe formal financial services, such as credit, deposits, insurance and payments, whenever needed [11] [14]-[17].

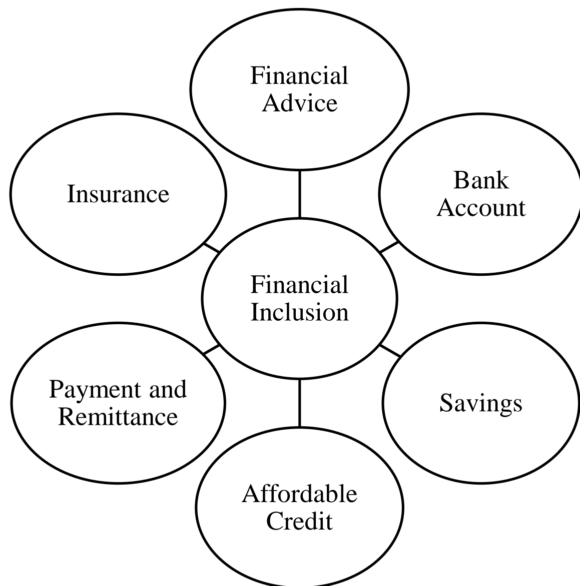

Fig.1. Dimensions of Financial Inclusion

3. EASE OF ACCESS TO CREDIT - ADVANTAGES

Easy access to credit enables households to smooth consumption expenditure over time, which may also facilitate education of children and reduce child-labor [18] [19]. Moreover, greater access to formal credit services can augment self-employment and, thus, reduce the extent of unemployment and underemployment [20]. In the case of credit, many households are being exploited by moneylenders at very high interest rates (50 to 60%) and, therefore, these households should not be seen as being financially excluded. Financial inclusion refers to households accessing institutional credit including commercial banks, cooperative banks, RRBs, NABARD SHG-linkage and other self-help groups, and credible microfinance institutions [21]. It is possible that in order to fulfil targets of financial inclusion, more bank accounts may be opened in the formal system. However, opening a bank account itself is not sufficient. Financial inclusion also refers to making more efforts towards covering small and marginal farmers and vulnerable social groups. A broader definition of inclusion should also focus not only on credit but also on an increase in productivity and sustainability of farmers and other vulnerable groups [21].

Since well-being of a population depends on many attributes such as income, health, housing etc., access to financial services can as well be regarded as a basic ingredient of human well-being. It is therefore necessary to design appropriate policy for financial inclusion [22]. In the context of financial institutions, financial inclusion concerns the spread of its activities among different sections of the population. The domain of activities of financial institutions can be quite large and it may vary across our country [22]. Initiated in August 2014, the Pradhan Mantri Jan Dhan Yojana (PMJDY), literally translated as Prime Minister's People Money Scheme, is aimed at ensuring universal and clear access to banking facilities to every Indian starting with basic banking accounts and an overdraft facility after six months and a RuPay debt card with an in-built accident insurance cover of USD 1500 [23].

The Indian government has recently advocated the triad of Jan Dhan Yojana (financial inclusion program), Aadhaar (biometric identification for residents) and Mobile connectivity for every resident [24]. Acronymed as JAM, the idea is to exploit these three modes of identification to deliver direct subsidies to the poor of the country. The government is also undertaking manifold policy measures, including dedicated applications for money transfer, payment system enablers based on biometric identifiers for those without mobile or debit card facilities, digital locker facilities for sending/storing electronic documents to provide a thrust to this digital initiative [25].

From an analytical standpoint, it is possible to advance several reasons as to why financial inclusion can enhance economic growth. First, consumers gaining access to the formal financial system are likely to increase savings, which in turn, can impact long-run economic growth [26]. Second, financial inclusion improves the penetration of credit and thereby raises aggregate economic activity [27]. Third, greater levels of financial inclusion strengthen the case for the use of interest rate as a primary policy tool [28]. Several studies have empirically explored the financial inclusion-growth nexus and uncover a positive relationship. Burgess and Pande [29] for example, show that concerted efforts by the Indian authorities for adopting a branch-led expansion strategy exerted a positive effect on state-level economic growth. Similarly, Dabla et al. [30] show that, by eliminating the blockages to the flow of credit, financial inclusion has contributed a 0.2 to 0.6% increase in the investment-GDP ratio. In sum, these studies veer around the view that financial inclusion has a salutary effect on economic growth.

The levels of financial inclusion vary substantially at the sub-national level. There is a broad consensus among policymakers that the growth needs to be more inclusive and broad-based, if the benefits are to permeate all segments of the population [33] [34]. Studies on the interlinkage between mobile banking and financial inclusion are limited, and often of indirect nature. McKay and Pickens for instance, find that branchless banking (including mobile money) to be nearly 20% cheaper, on average. Mas and Radcliffe [36] notes that some of the attractive features of M-PESA including strong latent demand for domestic remittances driven by a rapidly rising urbanization ratio, enabling regulatory environment, a dominant mobile operator with low airtime commissions and simple and transparent pricing have augmented the scalability of the process.

Virta et al. [37] show that mobile telephony facilitates economic growth. Similar findings are also echoed in cross-country research by Chakraborty and Nandi [38] who, in addition, observe that fixed-line teledensity and GDP per capita reinforce each other in both the long- and the short-run. Exploiting cross-national data on African economies, Andrianaivo and Kpodar [39] show that mobile telephony plays a key role in augmenting economic growth, although this effect differs across economies depending on the intensity of mobile penetration. Thus, the definitions on financial inclusion/exclusion, conceptual as well as functional, provide an indication that financial exclusion occurs mainly among people who are at the margins of the society [40]. Thus, in some instances where banks reported 100% bank account coverage among some Indian districts [41], successes in achieving financial inclusion might have been declared prematurely.

4. IMPORTANCE OF FINANCIAL INCLUSION

To eradicate poverty, reduce disparity in income and accelerate economic growth for the weaker, poor and the disadvantageous people, providing affordable, safe and easy access financial inclusion is the key [42]. Financial inclusion helps in creating a strong infrastructure, which further helps in the growth and development of the country. The study in [43] has debated the importance of financial inclusion in attaining sustainable growth. The study in [44] exposed that financially including the huge segment of people, who represent the bottom of the pyramid, leads to huge savings which in turn has a great impact on our economy. Engaging the underprivileged sections of the society through the formal financial systems will improve their standard of living and financial situation. Thus, they could develop financial asset, generate income, which will add to the macroeconomic factors [45]. Financial inclusion creates a chance for bring in the previously excluded people into the mainstream of the economy [46].

The following are the benefits to the banks by financially including the underprivileged people. Due to more people investing money, banks' financial assets increase thus their profits and market share [47]. It leads to the transfer of resources from the surplus source to the deficit sources, which leads to a sustained and a well balanced growth for the banks and the economy therefore [48] [49]. Financial inclusion increases the economic activity locally, thus enabling the government to achieve its important objective [5]. FI also benefits the society by providing social benefits [50] which change the financial background of the financially excluded at the micro level [51]. The above said benefits are only possible when the financially excluded people learn to invest, borrow and save from the formal financial institutions.

5. APPROACH TOWARDS FINANCIAL INCLUSION IN INDIA

Numerous measures are used by various countries to combat financial inclusion. India uses a bank-focused approach model to counter financial inclusion using the financial products like investments, savings and borrowings [52]. Banks in India are highly structured and have the ability to provide a suite of financial products which can combat the problem and eradicate financial exclusion. Banks are also supported by technology partners and other intermediaries. Financial institutions like Non-Banking Financial Companies, Non-Governmental Organization and Micro Finance Institutions find it difficult to achieve financial inclusion. The range of products and services they have are not sufficient to bring on financial inclusion on their own.

5.1 ROLE OF COOPERATIVES IN FINANCIAL INCLUSION

Enough research studies have been conducted for understanding the possibilities of achieving FI using cooperatives [53]-[59]. The above studies have helped to understand that the cooperatives make the financial inclusion process much easier, as the weaker sections of the society have better access to cooperatives than other financial institutions. Moreover, the Cooperatives have a wide range of network for reaching the rural masses. Thus, cooperatives are deemed to play a crucial role in financially including the rural people of India [60], and it is established by its attempts that are already made to reach the masses with its financial products [1]. The labour costs and the operating costs of cooperatives are comparatively much lower than the commercialised banks. This will enable them to reach the target towards achieving FI efficiently and economically [2].

The study in [61] proposes a new idea for the cooperatives for having better reach of the targeted masses by introducing representatives who will work on commission basis. They are highly cost effective and self-motivated in helping the cooperatives. The study in [62] suggests that the current strategies followed may not work for the lower income group. There should be a different strategy altogether planned for the lower income group and this should be part of their corporate social responsibility. The study in [63] encourages the cooperative banks to have a sole aim of providing credits to the underprivileged sections of the society and the farmers rather than focusing on other services like insurance and savings. The study in [64] suggests that the cooperatives could focus on those regions of the rural part of the country where micro finance institutions have very little availability.

In a study conducted by [65] in Nigeria, it was found that female entrepreneurs are the major takers of the loans provided by cooperative banks than from commercial banks due to their reasonable interest rates and flexible repayment structure.

6. DIMENSIONS OF FINANCIAL INCLUSION

Mandira Sarma [66], who is one of the leading researchers on financial inclusion index, only uses three dimensions to calculate 'the index of financial inclusion' for 2004. These dimensions are (a) banking penetration (the number of bank accounts per 1000 adults), (b) availability (the number of bank branches and number of ATM's per 1000 adults), and finally, (c) usage (deposits plus credits as a percentage of GDP). Similarly, the study in [67] analyses the association between financial inclusion index and other country-specific factors using simple ordinary least squares regression.

In another example, Arora [68] uses more dimensions and indicators when constructing their financial inclusion index by adapting IMF's classification of two primary groups of ninety-eight countries: advanced and developing economies. They use more dimensions and indicators than [40], except for the usage dimension. Furthermore, Kumar and Mishra [69] measured separate financial inclusion indices, using both supply and demand side indicators, for the years 2002 and 2003, for all the states of India. They found a great amount of variations across rural and urban regions even within a state. They explored the presence of informal financial services and discovered its significance in rural areas. Such dependency on the informal financial services could be reduced by providing the rural people with a larger variety of financial inclusion policies and widening the scope of these policy initiatives. But, on the contrary, higher values for the average size of loan or deposit to per capita income indicate that banking services are more limited in use, since they are likely to be afforded only by the other sections of the society [70].

Based on the population density for rural and urban areas as obtained by the Office of the Registrar General of India and the

Census Commissioner in the 2001 and 2011 census, researchers have separately worked out the rural and urban areas of a state and the respective population. Thereafter, financial inclusion numbers are computed as (a) at the all-India level; (b) separately for access and use; and (c) for access and use disaggregated further by rural and urban areas.

In the UK, the following are the three major dimensions of financial inclusion that are considered:

(a) Access to banking,

(b) Access to affordable credit, and

(c) Access to face-to-face money advice.

While these three dimensions are important for other countries as well, it seems to be important that a significant part of formal financial services in countries like India be directed toward priority sectors such as agriculture, small business activities, and economically backward sections of the population.

The capability set of a financial system is suggestive of its functional capacity, which would determine the extent of financial inclusion that it could achieve. Hence, any proposed index of financial inclusion is a measure of the performance efficiency of the financial system deployed. A higher value of the index will indicate a better performance, since an improvement in the formal financial institutions' activity in a dimension will represent a higher value. Such an index may be referred to as a functioning achievement index.

Evidently, the low contributing activities require attention from policy point of view for improving their levels in order to achieve a higher position in the performance scale. We can isolate such dimensions if the financial inclusion index enables us to calculate the percentage contributions made by different functioning to the overall level of financial inclusion. In other words, this type of breakdown enables us to identify the causal factors for low global performance. In this paper we suggest an index of financial inclusion that fulfills this property. Our index relies on the axiomatic approach developed in the realms of human development [10] [31] [71] - [73].

In a recent development, Schuetz and Venkatesh argue that blockchain technologies hold the potential to overcome most of these challenges pertaining to financial inclusion issues in India [32]. Similarly, in another study, situation-actor-process and learning-action-performance models are applied to present a comprehensive view on status of financial inclusion in India [35].

7. CONCLUSION

Literature has identified financial exclusion as a manifestation of social exclusion. The aim of financial inclusion is to promote sustainable development and generate employment for a vast majority of the population, especially, for the underprivileged sections of the society and for those in the rural areas.

In this paper, we have attempted an extensive review of the factors associated with financial inclusion. Financial inclusion follows the fundamental premise that development and poverty alleviation should be pursued through an expansion of financial markets, a financialization process in the guise of inclusive development.

There are a number of factors that hamper the weaker sections of the Indian society from accessing the formal financial services. The impeding factors from the demand side or the general public in need of financial inclusion could be lack of awareness about the importance of personal finance management, lack of awareness about the role of banks to help in financial independence, low income preventing usage of banks, social exclusion, and illiteracy. The factors that affect financial inclusion or act as barriers on the supply side or the banks are the distance of patrons from bank branch, mismatch of bank timings with the patrons' convenience, cumbersome banking procedures, requirements of documents for opening bank accounts, unsuitable banking products or schemes that do not align with the requirement of patrons, and the inappropriate attitude of bank officials.

This study has thus scrutinized the pros and cons of various existing and proposed means of financial inclusion for the under-privileged sections of the society in India, and has inferred that financial inclusion shall certainly play a vital role in helping the Indian nation to not only eradicate rural poverty but also the urban poverty among the under privileged sections of the society to achieve inclusive growth in India.

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