Financial Inclusion in India: Challenges and Way Forward

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In view of the success of PMJDY, a new gap clearly emerged and that is regulation of the micro and rural sector. The RBI, set up in 1934 regulates and supervises the banking system. In addition, though financial inclusion has been pursued by commercial banks for many decades, the focused approach has been missing. It may now be necessary to assign the regulation and supervision of financial inclusion to NABARD, with experience of more than four decades, with clear accountability and responsibility

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 make 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) defined 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 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.

Historical Developments

In fact, contrary to general belief, historically, India is a pioneer in financial inclusion. The Cooperative Credit Societies Act, 1904 gave an impetus to cooperative movement in India. The objective of cooperative banks was to extend banking facilities, mainly availability of credit on easy terms compared to money lenders who were well known to charge high rates of interest. In India, financial inclusion exercise explicitly started with the nationalization of State Bank of India in 1955. In 1967, there emerged a debate on social banking and consequently, 14 private sector banks were nationalised in 1969 to serve the unbanked population, mainly weaker sections of society as well as rural areas. The concept of priority sector lending became important by 1974 which implied directed lending to unbanked areas, and in 1980, eight more private banks were nationalized to extend banking in rural and remote areas. Since then, there has been a considerable reorientation of bank lending to accelerate the process of development, especially of the priority sector, which had not previously received sufficient attention.

Since 2005, Government of India along with the Reserve Bank of India (RBI) and National Bank for Agriculture and Rural Development (NABARD) has been initiating a number of concerted measures to

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enhance financial inclusion in India. These measures include Self Help Group-bank linkage programme, use of business facilitators and correspondents, easing of 'Know-Your-Customer' (KYC) norms, electronic benefits transfer, use of mobile technology, opening 'no-frill accounts' and emphasis on financial literacy. Other measures initiated by the Government to support financial inclusion include opening customer service centres, credit counselling centers, Kisan Credit Card, National Pension Scheme-Like, Mahatma Gandhi National Rural Employment Guarantee Scheme and Aadhaar scheme. The banking penetration, despite concerted efforts, was low.

In this context, to ensure a banking account in every household, the Prime Minister, in his maiden speech from the Red Fort on August 15, 2014, announced the need for focused efforts. The objective of Pradhan Mantri Jan Dhan Yojana (PMJDY) was widening access to various basic financial services like basic savings bank account, need-based credit, remittances facility, and insurance and pension to excluded sections, mainly weaker sections and low-income groups. The Government continued its efforts towards achieving financial inclusion by introducing Micro Units Development Refinance Agency (MUDRA) to focus on providing credit to small entrepreneurs. Similarly, having successfully achieved the distinction of ensuring that more than 95 percent of Indian households have bank accounts through the PMJDY by 2015, in a logical and well-sequenced step, the Central government extended social security to the masses. The flagship scheme, Atal Pension Yojana (APY) aims to provide old age income security to the working poor in the unorganized sector; Jeevan Jyothi insurance scheme providing a one year cover, renewable annually, offering life insurance; and Suraksha insurance scheme, renewable annually, providing insurance to cover death or disability on account of an accident.

The PMJDY has made significant progress since its launch and as on April 10, 2018, a total of 31.4 crore accounts had been opened of which 18.5 crores were in rural areas, 12.9 crores in urban areas and 16.6 crores were female account holders. The number of Rupay cards have also increased to 23.7 crores. The progress has been impressive, considering that total amount of bank deposits with commercial banks was Rs. 79,012.1 crore as on April 10, 2018.

Challenges

The key challenges in extensively extending financial inclusion are-

1. Some Accounts under PMJDY are not operative–In some cases, 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 a 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 a large number of new accounts, in remote parts of India.
6. Ease of transaction- Lack of ease in transaction related activities in banks is clearly demonstrated by the repetitive behavior of rural households' persistence in taking loans from the money lenders.
7. 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.
8. 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, and not customized to the rural sector income pattern are a major barrier for gaining access to the financial system.
9. 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.
10. Cyber Security-Nearly 31 crore new accounts have been opened in previous 3 years under PMJDY and nearly 80 percent of these are first time users. This can be a threat to cyber security especially when know-your-customer norms have been diluted.

Road Ahead

In the last two decades, 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 segments of the population because financial inclusion promotes economic equality and economic growth. Formal financial institutions provide low-cost access to banking facilities, safeguarding funds and providing a 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 to place as deposits but may have a need for resources which can be used for generating employment as well as stirring activity in the economy.

In India, the scenario for the next few decades may have to take into account the following –

a) Indian economy is closely associated with agriculture and rural activities because nearly 66 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 scarcity of land, because of rising population as well as increasing urbanization and industrialization would imply a higher cost of producing food grains and agricultural production.

d) As on March 31, 2014, there was 123 crore deposit accounts. In addition, Post Offices held 28 crore accounts. PMJDY has resulted in creating nearly 31 crore new accounts in banks. In addition, the Prime Minister 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.

e) The new accounts under Jan Dhan as well as other schemes that have recently been announced would result in massive banking operations and expectations of banking services at places which do not have bank branches. This would imply a higher cost of serving at remote places by commercial banks.

f) 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 to the public, generally low-income group. The higher food prices are also leading to increase in purchasing power of rural areas. The PM has also promised to double of farmer's income by 2022. The proportion of the population that would emerge out of poverty would need to be estimated.

Conclusion and Recommendations

The objective of financial inclusion is to provide financial resources to the consumers at affordable rates. In view of the increasing complexity of financial inclusion, there may be a need to consider a roadmap as well as a regulator.

The issue of digitization, necessary for achieving higher financial inclusion, is serious and needs analysis. India is a very diverse country in terms of languages and scripts. Also, the country has a low level of literacy of about 70 per cent, with English literacy of not more than 10 per cent of the population. Given the fact that all electronic devices have English numerals and all communication on digital banking is also in English, there is the natural barrier to completely digitalize Indian economy during the immediate period. India continues to have 30 per cent of its population or nearly 40 crore people below the poverty line and 90 percent operating in the informal sector. These people could also be slow in embracing digital economy. In addition, low volume of business in rural shops, shopping sheds, rural makeshift kiosks may not justify the cost of installing equipment to read and safely secure the data on plastic money. The cost of providing equipment in remote parts of the country and ensuring seamless connectivity at the affordable cost would be another challenge that would need to be addressed. The use of e-money, at present, is largely restricted to urban areas, and more educated youth from rural areas. Even if there are smartphones in the rural areas, these are restricted to only one member of the family which implies that banking activities, private in nature, would be restricted. Therefore, it may be helpful if a long-term plan with cost implications and a stipulated timeline is prepared to decide on various aspects of building a digital economy. To rapidly digitalize India, probably, there is a need for a Committee to understand the problem, become aware of the challenges, and then prepare a roadmap to achieve success. As the government has addressed the issue of smart cities by announcing a list of select 100 cities where technological amenities would be provided in a phased manner, a similar strategy, pilot based projects, and operations, could be adopted for digitalization.

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BASELINE RANKING OF ASPIRATIONAL DISTRICTS

The NITI Aayog launched the baseline ranking for the Aspirational Districts recently. These ranking are to be based on published data of 49 indicators (81 data points) across five developmental areas of Health and Nutrition, Education, Agriculture and Water Resources, Financial Inclusion and Skill Development, and Basic Infrastructure. The ranking was released by Shri Amitabh Kant, CEO of NITI Aayog. The 'Champions of Change' Dashboard for real-time data collection and monitoring was open for public viewing from April 1. The dashboard facilitates District Collectors of all the aspirational districts to input the latest available data of their respective districts. Districts can learn from each other's experiences using the "Best Practices" document that NITI Aayog has prepared and circulated to the district collectors.

Launched by the Prime Minister in January, the 'Transformation of Aspirational Districts' programme aims to quickly and effectively transform some of the most underdeveloped districts of the country.The broad contours of the programme are Convergence (of Central and State Schemes), Collaboration (of Central, State level 'Prabhari' Officers and District Collectors), and Competition among districts driven by a Mass Movement or a Jan Andolan. With States as the main drivers, this program will focus on the strength of each district, identify low-hanging fruits for immediate improvement, measure progress, and rank districts.

To enable optimum utilization of their potential, this program focusses closely on improving people's ability to participate fully in the burgeoning economy. Health and Nutrition, Education, Agriculture and Water Resources, Financial Inclusion and Skill Development, and Basic Infrastructure are this programme's core areas of focus.After several rounds of consultations with various stakeholders, 49 key performance indicators have been chosen to measure progress of the districts. Districts are prodded and encouraged to first catch-up with the best district within their state, and subsequently aspire to become one of the best in the country, by competing with, and learning from others in the spirit of competitive and cooperative federalism.