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FINANCIAL INCLUSION IN INDIA: EVIDENCE FROM NORTH EASTERN INDIAN STATES

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ABSTRACT: Financial Inclusion is presenting policy challenges in large quantum and with a sense of immediacy that is totally new for developing countries where more than 90% of the world's unbanked population resides. Policymakers of all the developing economies have acceded to the contention that there are highly complex and multi-dimensional factors that abet "financial exclusion" and hence require a large variety of providers, products, and technologies that are tailor made for the socio-economic, political, cultural and geographical conditions in these countries. India as a developing country, is attempting to ensure financial inclusion and weeding out financial exclusion and this itself is a unique experience and attempt. Indian economy has registered a phenomenal economic growth for the last decade. But this growth is neither comprehensive nor inclusive. Mobile phones, E-Mail, E-Commerce and Swanky Cars, trendy dresses, plastic money and 24 -hour banking through ATMs have become a basic necessity, but only in the cities and towns. Indian villages are still wondering about metal roads and clean drinking water or access to basic medical facilities. One of the reasons for this fragmented growth in the country has been accorded to the failure of the second generation reforms which were broadly related to financial sector reforms aimed to achieve greater financial inclusion. The problem of 'Financial Exclusion' is severe in the country. The entire Seven Sisters (North Eastern) States and states like Bihar, Jharkhand, Orissa and Jammu & Kashmir are facing the major brunt of this socio-economic problem. An effort has been made in this paper to assess how serious the problem of financial exclusion is in these states? How RBI towards greater 'Financial Inclusion' & what more needs to be done to achieve full & meaningful financial inclusion.

KEYWORDS: financial inclusion, developing countries, no-frills account, unbanked population, SHGs.

1. INTRODUCTION

The access to formal financial services for the poor majority population remains stymied in developing countries because of various factors. Governments are attempting to reach to the poor by means of, designing interest rate ceilings so as to make it more attractive and affordable, through direct lending and by directing banks to enhance branch network specifically in rural areas. But still, the availability of financial services is very limited. High debt levels in developing countries have constrained the access of credit to firms and individuals, high inflation rates have further provided demotivation for savings, high cost of provisions has translated into poor physical and institutional infrastructure, majority of poor people in developing economies do not have collateral or credit record and last but not the least, many developing countries lack credit bureau. All of these, together, deter lending (Ellis, 2007).

1.1 Financial Inclusion

The necessity of proactive and efficient social inclusion policies and their importance has been accepted globally and has featured in variety educational and social forums, for more than a century but the term financial inclusion has received a limited attention up till recently. Financial inclusion broadly means that the population of an economy has easy access to a variety of quality financial products and services which broadly include information, procedure, and financial education to facilitate participation in insurance, pension schemes, loans, deposit services, and payment systems and consumer protection mechanisms. It is estimated that around 2.5 billion people worldwide don't have any access to basic formal financial services. This lack of access to financial services is known as financial exclusion and this tends to be minimal if we take developing countries into account. For example, only 4% and 9% of the population in Germany and

United States respectively are without basic access to financial services (Peachy & Roe, 2004). The figures rise to dismal heights of 88% of the population, being financially excluded in Latin American, Asian and African countries. This has given rise to the contention that challenges to financial inclusion, in developing economies are unique and need a tailor made solution which is region specific and should be able to solve the region-specific challenges (Chaia et al., 2009).

1.2 Policy Instruments for Financial Inclusion in Developing Economies

Since the developing economies are facing challenges that are unique to the region, may it be population, educational standards, cultural restrictions to name a few hence the financial inclusion cannot be addressed by a single policy instrument. The policy makers, in developing economies struggling to devise solutions which are relevant to their respective economies and are accessible to the poor population. The developing economies are devising a multi-faceted approach to minimize the financial exclusion which is in sync with their unique politico-financial and socio-economic position and is based upon their own institutional support system.

Hence countries like Brazil and Egypt are strengthening the logistical system for delivering new products; Jordan is attempting to harness macroeconomic measures and promoting interbank bond markets to increase the credit availability to poor. While countries like Peru and Indonesia are banking on people empowerment for effective utilization of existing products and El Salvador is strengthening the publicly owned banks to reach out to the unbanked population (The World Bank, 2007). Hence we can see that policy creation for financial inclusion in developing economies is witnessing salient changes and rather than developing one solution that fits for all, these countries are modulating the policy measures in sync with their specific requirements.

Still, some policy aspects like Technological Innovations, the cautious creation of saving surplus units out of saving deficit and neutral units with the help of microfinance, have started coming up as major milestones and banks are required to play the lead role in dissipating the financial exclusion.

In developing economies like India, it is widely accepted that fragmented, small and specified non-banking institutions are unable to cope up with the quantum of targeted population. Here banks are expected to be the backbone of the transfer process, the creation of which is the prime objective of any financial system. Because of unfathomable diversities in Indian masses, the banks here are required to devise their own financial inclusion plans, specific to their location and targeted population segment with prior approval of the Board.

The regulators have observed that financial inclusion is more of a distribution issue rather than a logistical issue and this often requires more and widely distributed branches to reach out to the most inaccessible areas.

Some sporadic unique attempts have been displayed by countries like Pakistan where the branch liberalization policy was revised and the State Bank of Pakistan, now facilitates branch expansion decisions within the board policy parameters. Kenya, on the other hand, is reaching to the inaccessible masses with the help of mobile phone technology and a number of branch correspondents by incorporating regulatory changes in this regard.

1.3 The Indian Economic Scenario

The Indian economy is at the threshold of playing the lead role on the global stage because of its steady growth of 8 to 9 percent over the past decade, which is actually surpassing the best in the world. Where India's forex reserves were at the lowest 1990s have now already surpassed the 400 billion mark. This exceptional economic growth, registered in last decade has resulted in phenomenal growth in per capita income and disposable income. But a substantial proportion of this growth has resulted from secondary and tertiary sectors of the economy.

The primary sector, on which 65% of the population depends, however, is moving on a low growth path. On an average, during the last decade or so it has grown at a dismal rate of 2 percent. As a result of this, the benefits of economic prosperity have not trickled down to all the sections of the society and all regions of the country.

1.4 Statement of the Problem

The process of revival and uplifting of Indian economic growth was projected in two phases. As a matter of fact, the 1st and 2nd generation reforms placed Indian economy into a high growth trajectory but this growth was sporadic and was visible only in few sectors and not the least in the primary sector, agriculture. Hence this growth was not inclusive. All the fruits of growing economy were being enjoyed by select few in big cities. E-mail, E-commerce, big cars, mobile phones, trendy clothes, ATMs, 27×7 banking were all available and being utilized by city dwellers only (P. Sing & S. Kour, 2003). There's no gainsaying that the gains of economic growth were being solemnized by select few in select cities (M. R. Khurana, 2003).

One plausible reason for this exclusive growth, being witnessed in India, could be the failure of second generation reforms which were directed towards the financial sector and its up gradation. The policy makers, during the second generation reforms, shifted their attention from primary sector to secondary and tertiary sectors and thereby these sectors started registering phenomenal growth and the primary sector, agriculture, lagged behind which result in today's scenario where large sections of population, specifically the underprivileged class, still has to vie for affordable financial services like credit, insurance, collaterals, saving safety net etc. which, incidentally, is the trigger mechanism for wholesome inclusive economic growth.

Financial exclusion is country's single most serious socio-economic problem having a reverberating effect. Despite the recent economic reforms and schemes like 'Jan Dhan Yojna', only 74% of adult population has bank accounts and last year the figures were at dismal 59%. Which means that 25% of the adult population in India still lacks the modern payment system and which, by the way, is larger than the population of many, comparable, developing countries? This picture becomes even grimmer when we look at the formal credit system. Only 14% of adult populations have loan accounts and in rural areas the figure of loan accounts drop to 9.5%. This financial exclusion problem is still persisting and has grave consequences if we look at the non-institutional finance which has covered 43% of the population and the numbers of non-institutional finance are continually going up as 17.5% in 1991 to 29.6% in 2002 and to add salt to the woe, to 37% in 2012. The only saving grace to this entire scenario is that the trend is declining in urban areas. This is happening because Indian economy is suffering from non-accessibility of affordable credit. These figures become scary, when we talk about North Eastern Region of this country where we still are suffering from poor infrastructure, lack of quality educational system, the inadequacy of medical facilities, prevalence of extremism and what not.

1.5 Break in the Clouds

Though the problem of financial exclusion is rampant in rural India where the major source of employment is agriculture and related activities. But the people who are associated with SMEs, in rural, semi-urban and urban areas, are subject to greater challenges when it comes to the easily accessible and affordable credit. Agriculture and SMEs are the two sectors which are major contributors to GDP and have tremendous growth potential. The Break in the clouds is that the financial exclusion as a fact and its associated problems are now known to the policy makers. With a view to impart growth impetus to these two sectors of Indian economy and ensure easily accessible and affordable financial services to the underprivileged and/or unprivileged classes in the country, a number of initiatives have been undertaken. The Reserve Bank of India (RBI) has issued scores of instructions to banks to ensure inclusive growth through financial inclusion, some of the instructions are as follows:

'No frills' savings accounts with zero balance and low or nil minimum charges for opening and maintaining an account.

Relaxation of 'Know Your Customer (KYC)' norms for opening a bank account facilitated with self-declaration of address and an existing account holder as an introducer to the bank in order to reach to the weaker sections of the society.

The introduction of 'General Purpose Credit Cards' with a credit limit of 25000 to manage the unplanned credit requirements of card holders, at their rural or semi-urban branches.

The simplified mechanism for one-time settlement of overdue loans up to Rs. 25,000. Banks are further instructed to treat such beneficiaries, eligible for the fresh credit.

The services of NGOs (Non- governmental Organizations), MFIs (Micro-Finance Institutions), SHGs (Self-help Groups) etc., can now be availed by the banking system.

Financial education and credit counseling have also been brought under the scope of banking services to maximize the impact of "Financial Inclusion".

1.6 Objectives of the Paper

This paper aims to study:

- The severity of the problem of Financial Exclusion in the North Eastern States.
- The specific reasons for the problem of financial exclusion in the North Eastern States.
- To suggest measures, to achieve a greater degree of Financial Inclusion in the country in general and in the North Eastern States in particular.

1.7 Problem of Financial Exclusion in North East

The term 'Financial Exclusion' is used in different ways but it is generally related to a lack of access to affordable financial services to individuals, households, and communities who are generally unprivileged in term of wealth education and location. Figure 1 outlines the key components of financial exclusion.

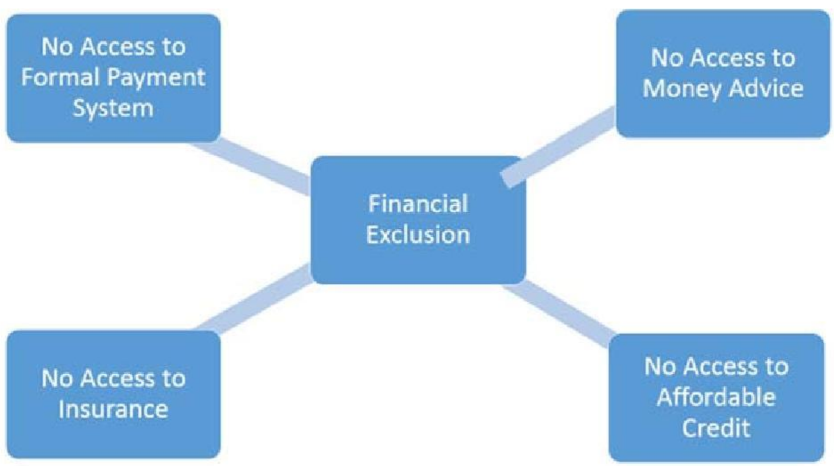

Fig: Components of Financial Exclusion

As already stated that the problem of Financial Exclusion is severe in the country. The North Eastern States are no exception to this socio-economic problem which has been analyzed in some detail in the following para analyze the problem of Financial Exclusion in these States. Access to Banking Services. Affordable Credit and Money advice to the adult population in the state has been studied.

1.8 Access to Banking Services

Financial Inclusion, as a policy tool, requires that all (100%) adults/households have access to formal payments and savings safety net. This, in turn, would require that each adult member, of the population, must have a bank account for making and receiving payments and parking savings through deposits and insurance. But as per the available data, unexpectedly large portion of these state's population is still 'Unbanked' i.e. without a bank account of any kind. As per the available data. 53 percent of the adults or 13,52,437 out of 25,51,768 households in the North Eastern Region have been found without access to any kind of bank account which is more than the all-India average of 41 percent. These figures are also more than most of the states in the country.

Further analysis of the data about the unbanked population in the state reveals that unbanked households are mainly concentrated to the lower strata of the society. As can been seen from the Figure 3. 79 percent of the unbanked households in the states (North Eastern) belong to the lower income group. This finding corresponds with the findings at the national level as well at the international level. Further the data on location distribution characteristics, highlighted in Figure 4 reveals that overwhelming majority of unbanked households are located in rural areas followed by suburban areas. As can be observed from the figure that 62 percent or 5.19.531 out of the total 8.37.954 unbanked households are located in rural North Eastern Region. It can also be observed that only 9% of the unbanked households belong to the urban North Eastern Region. This finding again falls in line with the general trend at the national level.

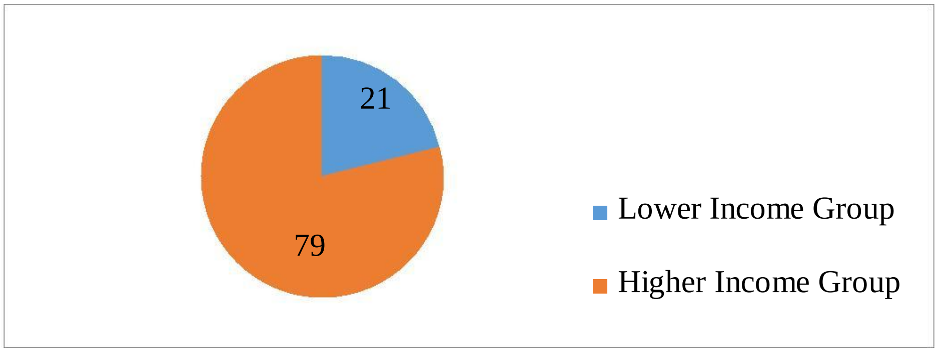

Fig: Banked and Unbanked Population
Source: Reserve Bank of India

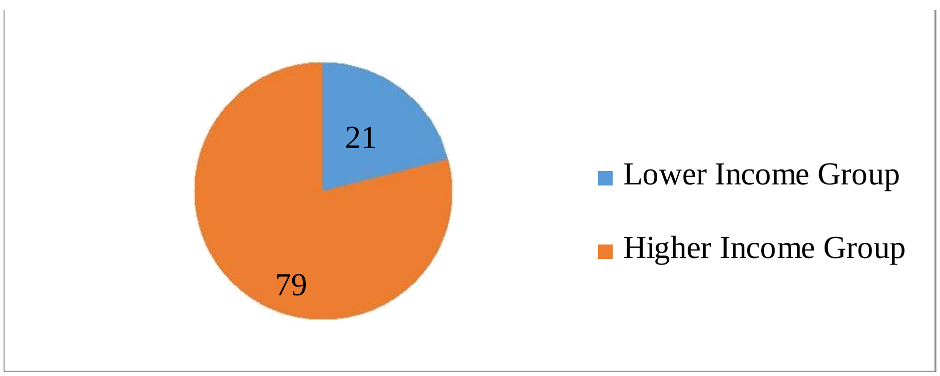

Fig: Distribution of Unbanked Population among Lower Income Group and Higher Income Group
Source: Reserve Bank of India

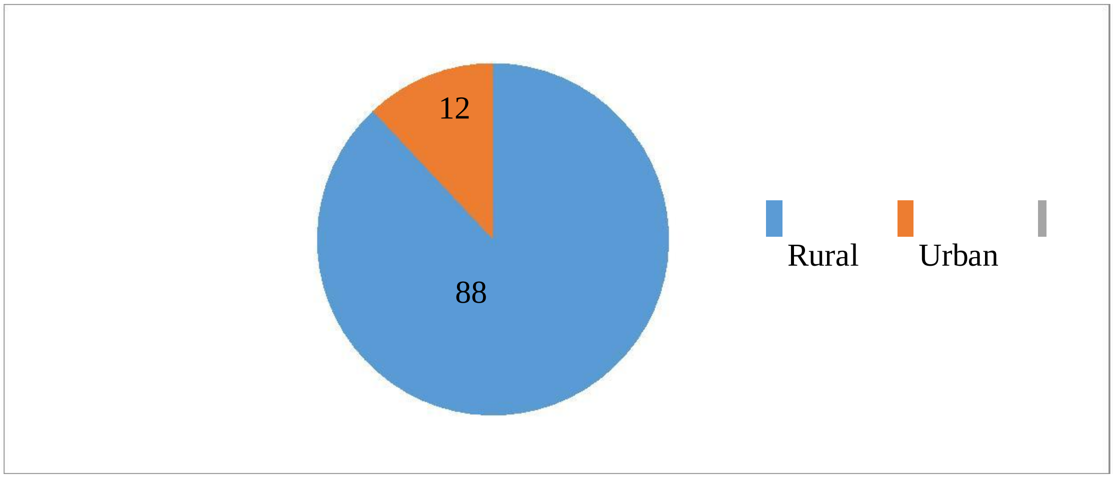

Fig: Location Characteristics of Unbanked Population of North Eastern Estates
Source: Reserve Bank of India

2. ACCESS TO AFFORDABLE CREDIT

The problem of Financial Exclusion in respect of access to credit is much worse than the problem of access to banking services in the state. The data on access to formal credit reveals that majority of the households in the state lack access to Formal Credit markets. As on 2006-07, out of the total 15,51,768 households, only 1,00,709 households enjoyed access to formal credit system which accounts for just 6.49 percent of the total households in the state. The comparative data on access to credit clearly reveals that the Northeastern States are far behind to the national averages and also to the similar type of states like Himachal Pradesh etc. At the national level, 9.5 percent of the total households as on 2011 -12 lacked access to credit which is little better than the Northeastern States. On the whole, the country suffers on this front of financial exclusion.

The problem of financial exclusion in respect of easy access to credit is more prevalent in rural areas than the urban areas of the valley. Out of the total 14, 51,059 households which are without any access to a formal credit system, overwhelming majority i.e. 88.01 percent belonged to the rural areas. The reason for this more distribution towards rural areas is that 82.29 percent of total households are rural and also that the problem of financial exclusion is more in the farm sector.

The more problem of credit exclusion among the rural households is not only the state-specific problem but at the national level also more households without any access to formal credit system belongs to rural areas for obvious reasons.

Further analysis of the data reveals that most of the households without any credit coverage under the formal financial system, raise credit from non-institutional sources like moneylenders, relatives, friends, and neighbors, however, money lenders constitute an important component of all non-formal sources. Again the non-institutional credit is more prevalent in rural areas than the urban areas. It has also been found that the share of non-formal credit in urban areas has declined over the period which is somewhat pleasing to note.

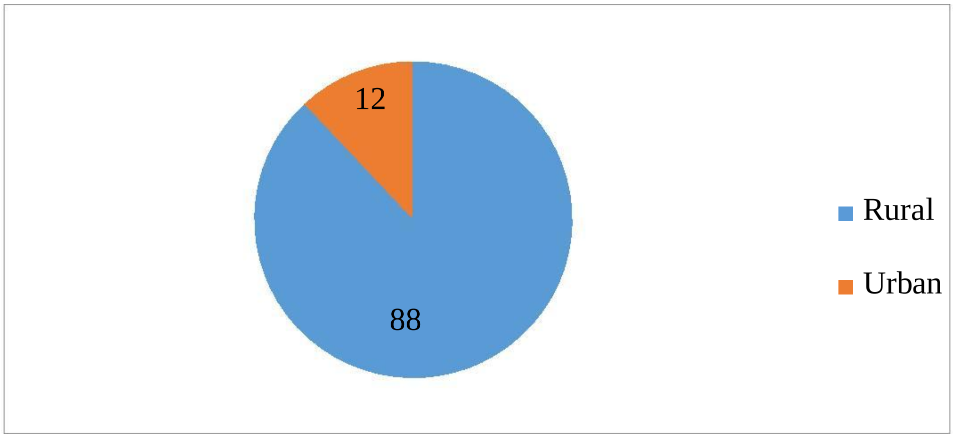

Fig: Accessibility and Non-Accessibility of households to formal credit system
Source: Reserve Bank of India

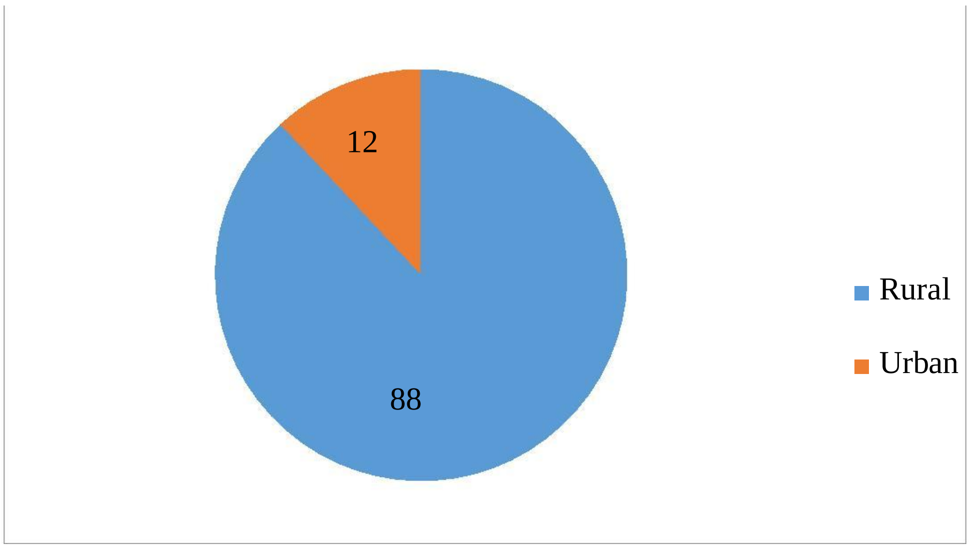

Fig: Non-Accessibility to formal credit system among Rural and Urban Households
Source: Reserve Bank of India

2.1 Initiatives for Total Financial Inclusion

From the above, it becomes clear that the vast majority of people particularly those belonging to the farm sector and the artisans lack access to affordable financial services in particular access to cheap bank credit. This is also acting as a constraint in the much needed socio-economic development of the unprivileged sections of the society in the country. Ms. U. Throat (2007) has held that the limited access to financial services to the people belonging to the farm sector and unorganized sector is acting as an impediment to growth in these sectors, thus acting as a dampener in the overall socio-economic growth scenario. The Central Bank authorities in the country were aware of this fact and in order to achieve greater 'Financial Inclusion' in each geographical/regional sector, the designated banks have been asked to implement certain measures in their designated areas. In 2006, one district in each state was identified by the State Level Bankers Committee (SLBC) for 100% Financial Inclusion.

To achieve greater success in its mission of achieving total financial inclusion, certain RRBs are using the following strategies:

In the first place, it mainly focused on bringing the excluded people into banking savings net by opening a no-frills account.

To achieve the targets for opening the no-frills accounts; the bank launched a vigorous campaign in the district by holding awareness camps. The bank also utilized the services of 'Village Level Worker' (VLWs) to mobilize people for awareness camps in different villages.

DLRC/DCC meetings on a quarterly basis were held in order to assess the progress in financial inclusion where generally defaulting banks were impressed upon to bring forth the results. Organized loan camps for the farmers where loans were sanctioned on the spot.

2.2 Impact of Financial Inclusion Drive

The analysis of achievements made on the 'Total Financial Inclusion' front in the designated district by the various banks reveals some success and some failures. It can be seen from the data contained in table 1 that of the different banks entrusted with the responsibility of achieving greater financial inclusion in the district, only J&K Bank Ltd. has achieved some worthwhile results. It is disheartening to note that other banks viz, SBI, PNB, IDBI Bank, Allahabad Bank, UCO Bank and UBI Bank have failed miserably towards achieving their targets of financial inclusion. As can be seen from the said table that , IDBI Bank, Allahabad Bank, UCO Bank and UBI Bank have failed to open even a single 'No-frills Account' while as State Bank of India (SBI) could open just 64 'No- frills Account' which account for just 0.0007% of the total households in the district. These banks seem to have failed to achieve their targets partly due to poor branch network and more importantly due to the lack of any serious initiative to achieve greater financial inclusion in the designated district. Moreover, on the credit front, the performance of the banks has been even more pathetic. In the two years period, (2011 - 12 & 2012 - 13), the bank could issue General Credit Cards (GCC) to 291 households only which account for 0.00254 percent of the total households in the district. The total amount of Credit disbursed through GCCs by JBanks in the region has been a meager amount of Rs. 65.13 lacs. SBI which has opened some no-frills accounts in the region, but has totally failed on the credit front by not issuing any GCC.

Impact of Financial Inclusion in the North Eastern States

State Bank of India	2011-12	2012-13	Total
No. of no. frills accounts	57	17	64
Amount Mobilized	0.11 Lacs	0.07 Lacs	0.18 Lacs
% age of families covered	0.00054%	0.00016%	0.0007%
% age of Village Covered	NA	NA	NA
Punjab National Bank	Nil	Nil	Nil
IDBI	Nil	Nil	Nil
UBI	Nil	Nil	Nil
Uco	Nil	Nil	Nil
Allahabad Bank	Nil	Nil	Nil

Source: Official Record of SBI

3. CONCLUSIONS

From the above, the following three important inferences can be drawn about the total financial inclusion in the designated district:

- Except SBI all other banks have failed completely towards achieving total financial inclusion in the district. The SBI has succeeded in opening some of the 'no-frills' accounts.
- All the banks including SBI have failed in achieving total financial inclusion in terms of providing affordable credit to the people. Like other parts of the country, banks in the state have unfortunately

focused mainly on the opening of No-frills accounts and less on providing affordable credit to the unprivileged classes of the society which is a rather more important aspect of total financial inclusion. As such making total financial inclusion more meaningful, ensuring affordable credit calls for more attention on the part of banks.

- A perusal of records and discussions with the officers of SBI bank revealed that the bank has also targeted students of colleges and schools in order to bring them within the banking realm for the purpose of achieving targets towards total financial inclusion is objectionable. This is owing to the fact that only those shall have to be included for financial inclusion whose family has no previous bank account. Further, only adults are required to be covered for financial inclusion but the fact is that most of the college/school children are minors.
- Towards achieving the total financial inclusion in some states, banks in association with insurance companies have also taken steps to provide social security to unprivileged social class through innovative insurance schemes. But in Northeastern Region, banks have totally ignored this aspect of financial inclusion.

4. SUGGESTIONS FOR GREATER FINANCIAL INCLUSION

Although many of the banks in the state have failed to achieve their targets towards total Financial Inclusion, yet SBI through its large branch network has helped the northeastern states to achieve financial inclusion to a satisfactory level, in the selected district, however, to the extent of opening of ‘no-frills' accounts only. In fact, all other banks in the state have failed miserably in bringing the financially excluded into ‘Credit Net'. The failure of the banks in the state is being partly attributed to the lack of any serious effort on their part towards the same and partly due to the lack of any well-conceived strategy to cover the financially excluded under the affordable credit net. The fact is that the most important element of financial inclusion is to ensure access to affordable credit to the financially excluded people to uplift them economically. As such banks in the state would need to pay equal attention rather more attention to this aspect of financial inclusion. Towards this goal, the following few suggestions are made:

- In many states, banks have involved SHGs to achieve greater financial inclusion which has proved successful.
- Similarly, banks in the state should use the mechanism of SHGs to cover financially excluded under the banking net. The successful use of SHGs would require taking the following steps:

1. Conduct Awareness-cum-training Programs for SHGs to educate the groups about the rationale of financial inclusion and train how to plan and control their finances.
2. Ask SHGs to prepare the ‘Micro Credit Plans' (MCP) for each member of the group which should include capital investment and working capital for proposed economic activity. It may also include credit needs for social activities. The bank official may participate in the deliberation of a Group, however, as an observer only.
3. Branch Manager should convene meetings with each member along with group leader to validate the MCP.
4. On the basis of MCP fix credit limit. The limit should meet the requirement of the member fully. Further, the loan should be tailored to meet the specific needs of members. It is also important that the loans should at provided at concessional rates and without any requirement of collateral.

SHGs are presently meant for women only. However, for the purpose of total and meaningful financial inclusion, men also should be allowed to form SHGs which would enable to enlarge the canvas of financial inclusion.

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