WHY FINANCIAL INCLUSION ?

Ramesh Subramanian,
Ph.D Research Scholar,
SCSVMV University,
Enathur, Kanchipuram,
Adjunct Faculty, IFMR,
Chennai.

Dr.N. Chandrasekaran,
Adjunct Faculty, LIBA,
Chennai, and Research
guide for First Author
(Scholar).

Dr. Meenakshisundaram,
Professor, Head CAA,
Great Lakes Institute of
Management, Chennai.

"Overcoming poverty is not a gesture of charity. It is an act of justice. It is the protection of a fundamental human right, the right to dignity and a decent life. While poverty persists, there is no true freedom."Nelson Mandela

"Poverty is the worst form of violence." - Mahatma Gandhi.

Bernanke: "Helping people better understand how to borrow and save wisely and how to build personal wealth is one of the best things we can do to improve the well-being of families and communities." (Shri.P.Vijaya Bhaskar, December 10, 2013).

ABSTRACT

Financial inclusion could be an important instrument for alleviation of poverty. Financial Inclusion would result in economic growth and lead to balanced development. Financial Inclusion is talk of the town and both the Central Government and RBI are very keen on it. Financial inclusion broadens the resource base of the financial system by developing a culture of savings among large segment of rural population and plays its own role in the process of economic development. Efficient allocation of capital would be possible by providing access to finance to the poor and this would lead to reducing the disparities in income distribution. Policy transmission of the central bank could be most effective only when the entire financial system is under the organized sector. Two-fifths of rural households still rely on informal credit. Further, *the rural folk depend on the money lenders for meeting some of their credit needs like health, litigation etc. for which the formal banking system is shy of lending. The Global Partnership for Financial Inclusion (GPFI) was officially launched on 10 December 2010 in Seoul. India as a member of G20 has rightly put financial inclusion at the top of the agenda of the Central Bank.*

KEY WORDS:

Financial Inclusion, Global Partnership for Financial Inclusion, Reserve Bank of India, Policy Transmission, Poverty Alleviation, Resource Base, Capital Allocation, Exploitation of Masses, Lower Cost of Funds.

Introduction

Financial Inclusion has been on the top of the agenda of the Reserve Bank of India and Government of India for quite some time. The Global Partnership for Financial Inclusion (GPFI) is an inclusive platform for all G20 countries, to carry forward work on financial inclusion, including implementation of the G20 Financial Inclusion Action Plan. India as a member of G20 has rightly put financial inclusion at the top of the agenda of the Central Bank. Financial Inclusion as many dimensions and viewed from different perspectives it has much to offer. The article tries to highlight the importance of financial inclusion from the national perspective and what is there for the stakeholders in furthering financial inclusion. An attempt is also made to understand the economic theories related to financial inclusion. It would be interesting to note that in India even during the Vedic period financial inclusion was given importance, though the words 'financial inclusion' was not specifically mentioned.

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. (Dr. C. Rangarajan, 2008).

Financial Inclusion, broadly defined, refers to universal access to a wide range of financial services at a reasonable cost. These include not only banking products but also other financial services such as insurance and equity products. (Rajan, 2009).

The RBI defines financial inclusion as the process of ensuring access to appropriate financial products and services needed by all sections of society in **general** and vulnerable groups, such as weaker sections and low-income groups in **particular.** This should be at an affordable cost in a fair and transparent manner by regulated, mainstream institutional players. (Dr. K.C. Chakrabarty D. G., September 6, 2013.)

While various authors have defined financial inclusion in different ways the essence of financial inclusion is to ensure delivery of financial services which include - bank accounts for savings and transactional purposes, low cost credit for productive, personal and other purposes, financial advisory services, insurance facilities (life and non-life) etc. It may also be said as simply 'access to finance'.

"Financial Inclusion has been in the top of the agenda of the Central Government and RBI. Financial inclusion is a flagship programme of the Reserve Bank. Its objective is to bring people, hitherto excluded, under the ambit of formal financial institutions." (Report, 2013)

Financial Inclusion Why?

Allocation of Capital: Economic growth could be even in the economy only if there is financial inclusion. Access to finance can benefit the poor by increasing capital flow to the underserved sections of the economy and increasing efficiency of capital allocation thereby reducing inequality. This would also result in balanced regional development.

Migration of population: People migrate to other places in search of better livelihood. This is mostly due to non-availability of vocations in their neighborhood. Access to finance would benefit this section of the society and would in turn prevent migration of population to other parts of the country. The Access to credit could enable the underserved to invest their human capital in micro enterprises. Financial inclusion could be an important instrument in alleviation of poverty.

Resource Base: For economic development an economy needs capital investment. At present India is relying heavily on external sources for financing its economic development. At end-December 2013, India's external debt stock stood at US$ 426.0 billion, recording an increase of US$ 21.1 billion (5.2 per cent) over the level of US$ 404.9 billion at end-March2013. India's external debt to GDP ratio stood at 23.3 per cent at end-December 2013 vis-à-vis 21.8 per cent at end-March 2013 (Standard, March 28, 2014). India's dependence on external debt is a source of concern as these come at cost. In addition, they are also lumpy and volatile. It would be in the country's interest that we are self-dependent. India has a vast untapped potential for raising resources. However, the progress is far from satisfactory as evidenced by the World Bank Findex Survey (2012). According to the survey findings, only 35% of Indian adults had access to a formal bank account and 8% borrowed formally in the last 12 months. Only 2% of adults used an account to receive money from a family member living in another area and 4% used an account to receive payment from the Government. The miniscule numbers suggest a crying need for a further push to the financial inclusion agenda to ensure that the people at the bottom of the pyramid join the formal financial system, reap benefits and improve their financial well being(Dr. K.C. Chakrabarty D. R., September 6, 2013).

Policy Transmission: When a huge segment of the country is financed by the unorganized financial sector the monetary policy transmission of the central bank would be ineffective to a large extent and hence inflation control which is mandate for the central bank would not be effectively achieved. Only 40 per cent people in the country have formal banking accounts (K. R. Kamath, 2012).It is analogous to constructing a dam in at one place across the river Ganges while allowing the free flow of water from the other side. Policy transmission of the central bank could be most effective only when the entire financial system is under the organized sector.

State Revenue: From revenue point of view too financial inclusion is important as it would ensure that the role of the unorganized financial sector is minimized and there would be an audit trail financial sector which would in turn add to the revenue mopping up and would well go to reduce the fiscal deficit.

Protecting the wealth of the masses: Covering low income households within the frame of financial sector the financial inclusion will protect their financial wealth. The financial scams in the country have caused a huge loss of savings of the low income households. Unscrupulous elements mop up the scarce financial resource of the countrymen – particularly the vulnerable section of the society. This impinges on the resource mobilization of the mainstream financial institutions. It is another matter that these institutions are not there in the first place and hence the society is forced to take recourse to the unscrupulous elements to deposit their hard earned savings. The recent financial scams in the country point to the urgent need to offer access to finance to the masses.

Exploitation of the masses: Exploitation of vulnerable sections by the usurious money lenders by facilitating easy access to formal credit can be taken care by financial inclusion. Working paper Series 5/20/13 of RBI "Persistence of Informal Credit in Rural India: Regulatory Policies Need to Recognize Changing Landscape." Authored by Narayan Chandra Pradhan, the paper is an updation of sorts.The central bank applying its forensic skills to an examination of the magnitude has found that informal lenders continue to exist in varying degrees across the country as important conduits of rural credit. Two-fifths of rural households still rely on informal credit. Further, the rural folk depend on the money lenders for meeting some of their credit needs like health, litigation etc. for which the formal banking system is shy of lending.

Preventing Informal Remittance Channels: In addition, in the absence of financial inclusion the migrant population is also totally dependent on the informal 'Tappawala' services for remittance of money to their near and dear ones staying away from their work places. Ganjam migrants in Surat send home Rs.100 crore a year, through the unique Tappawala courier system (P.Sainath, 2009).Relying on informal remittance channels throws its own challenges to the migrant population and the consequences are obvious.

Lower Cost of funds for the Banks: Banks as financial intermediaries would always focus on lower cost of funds. By bringing in the un-banked in their fold the cost of funds would be lowered to enable them to encourage entrepreneurial activities. Lower cost of funds would lead to lower lending rates and hence cost of production and ultimately lead to lower inflation levels.

Insurance and Pension: The proportion of people having any kind of life insurance cover is as low as 10 per cent and proportion having non-life insurance is abysmally low at 0.6 per cent (Dr. K. C. Chakrabarty, November 5, 2012).T he pension coverage too is abysmally low.

G20 Initiatives: Around the world, 2.7 billion adults still do not have access to basic financial products such as savings accounts, loans, insurance, payments systems, pension plans and remittance facilities. This situation creates particular challenges, especially for poor people, whose incomes are not only low, but often irregular and less reliable. In Los Cabos, G20 Leaders announced initiatives on financial inclusion, financial education and consumer protection to address these issues that have the potential to make a tremendous difference to the well-being of millions of people.

Global Partnership for Financial Inclusion: The Global Partnership for Financial Inclusion (GPFI) is an inclusive platform for all G20 countries, interested non-G20 countries and relevant stakeholders to carry forward work on financial inclusion, including implementation of the G20 Financial Inclusion Action Plan, endorsed at the G20 Summit in Seoul. At the G20 Summit in Seoul, the Leaders of the G20, recognizing financial inclusion as one of the main pillars of the global development agenda, endorsed a concrete Financial Inclusion Action Plan. Financial inclusion was also highlighted as an important component under the financial sector reform agenda. Subsequently, the Leaders announced the establishment of the GPFI to institutionalize and continue the work began by the Financial Inclusion Experts Group (FIEG) in 2010. The GPFI was officially launched on 10 December 2010 in Seoul. India as a member of G20 has rightly put financial inclusion at the top of the agenda of the Central Bank.

Economic Theories: An early field of study in economic theory (Bagehot 1873, Schumpeter 1911, Robinson 1952, Goldsmith 1969), highlights the role of finance in economic growth and development. This has also been amplified in the late eighties with endogenous growth theory and the empirical tests initiated by King and Levine (1993). The finance – growth relationship has been widely tested during the last two decades. Empirical evidence suggests a positive link between financial depth (measured by the ratio broad money to GDP or credit to the private sector to GDP) and economic growth and poverty alleviation (Levine, 2005, Beck et al. 2007, Beck et al. 2011).

Empirical research also states that that the long-run economic growth is stimulated by the services provided by the financial system. Building on the foundations laid by Walter Bagehot in the late 19th century and Joseph Schumpeter in the early 20th century, among others, recent research has produced a key result that countries with better-developed financial systems tend to grow faster.

Cross-countries comparisons also suggest that countries with large financial sectors, for instance in east-Asia have reached higher growth rates than countries having narrow financial systems, located in sub-Saharan Africa (Beck et al., 2011).

Though emphasis on financial inclusion has gained strategic importance in the Indian banking sector only recently, it is often not realized that it has a long historical reference, going back into the Vedic period. (Thingalaya, 2012).All India Rural Credit Survey Report, which was the first report recommending bank nationalization in 1955, had quoted a Sanskrit saying, which had recognized the crucial role of village money lender. An ideal village is defined as "one that has a perennial stream, a priest to administer to soul, a Vaidya to heal in case of sickness and a money lender from whom to borrow money, when needed". A perennial stream is required to irrigate land, so that enough food grains and other farm products could be grown in the village. The presence of a priest symbolizes the availability of a teacher in the village. Health facilities are provided by the village Vaidya. One notable addition is the existence of a money-lender in the village from which money can be borrowed when in need. Manu, the Vedic law-giver, also has considered money-lending as a lawful occupation. He has stipulated the role of the state in allowing the smooth operations of the money-lending transactions. Interest rates are stipulated by him, quoting the rates prescribed by sage Vashista.

Conclusion

Financial inclusion would definitely lead to symmetric distribution of wealth and for balanced regional development since it is a poverty alleviation tool which lies in the hands of the central bank and State. The Vedic period economic theory has flagged financial inclusion as most important for a country's progress. It is not that the only central government that would benefit from financial inclusion but also the federated states. States like Madhya Pradesh have taken lead in this regard and the effort of the government to bring bank accounts closer to the people has also paid off. A network of ultra-small banks has been established across the State's 51 districts. Christened Samruddhi scheme has been able to penetrate far flung and unbanked areas, delivering cash just a few kilometers away from the villagers' homes (Mehra, 2014). As the objective of both the central and federated states is welfare of the people, financial inclusion is a valuable tool for economic development of the country. It can, therefore, be concluded that Financial Inclusion is a sine-qua-non for the economic development of a country and the wellbeing of masses. Financial inclusion broadens the resource base of the financial system by developing a culture of savings among large segment of rural population and plays its own role in the process of economic development.

Bibliography :

1. Dr. K. C. Chakrabarty, D. R. (November 5, 2012). Financial Inclusion – Issues in Measurement and Analysis. *BIS-BNM Workshop on Financial Inclusion Indicators* . Kuala Lumpur : Reserve Bank of India.

2. Dr. K.C. Chakrabarty, D. G. (September 6, 2013.). Keynote Address . *Finance Inclusion Conclave* . New Delhi : Reserve Bank of India.

3. Dr. K.C. Chakrabarty, D. R. (September 6, 2013). Keynote address . *Finance Inclusion Conclave* . New Delhi : Reserve Bank of India.

4. Dr.C.Rangarajan. (2008). *The Committee on Financial Inclusion* . New Dehli.

5. K. R. Kamath, C. P. (2012). Function to release Social Audit Report of Shriram City Union Finance Ltd. *News item Hindu Business Line.* New Delhi.

6. Mehra, P. (2014 , June 2). Inclusion from the bottom. *Hindu Business Line* .

7. P.Sainath. (2009, July 18). Put your money down boys. *The Hindu* .

8. Rajan, D. G. (2009). *Committee on Financial Sector Reforms.* New Delhi: Sage on behalf of Government of India.

9. Report, R. A. (2013). *RBI Annual Report 2012-13, page 75.* Mumbai: Reserve Bank of India.

10. Shri.P.Vijaya Bhaskar, E. R. (December 10, 2013). Financial Inclusion in India – An Assessment . *MFIN and Access-Assist Summit.* New Delhi: Reserve Bank of India .

11. Standard, B. (March 28, 2014). New Report. *Business Standard - Ministry of Finance, Government of India* .

12. Thingalaya, D. N. (2012, April - June). Role of Rural Banks in Achieving Financial Inclusion. *Bank Quest* , p. page 12 .