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Financial inclusion-Relevance and importance: Special emphasis on East Godavari district

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Abstract: Financial Inclusion of the poor has a multiplier effect on the economy as a whole, through higher savings pooled from the vast segments of the population present at the bottom of the pyramid. There is a potential for transforming the lives of these excluded groups by providing access to formal savings arrangements and extension of credit by banks for emergency and entrepreneurial purposes, thereby enabling the poor to create assets, generate stable income, build resilience to meet macro-economic and livelihood shocks and bring about an improvement in their financial condition and living standards.

Keywords: stable income, financial inclusion, Self Help Groups

INTRODUCTION

Financial inclusion is defined as '*the process of ensuring access to appropriate financial products and services needed by all members of the society in general and vulnerable groups in particular, at an affordable cost in a fair and transparent manner by mainstream institutional players*'

Financial inclusion efforts are not new to India; both the Government and the Reserve Bank have been pursuing this goal over the last several decades through building the rural cooperative structure in the 1950s, the social contract with banks in the 1960s and the expansion of bank branch networks in the 1970s and 1980s. These initiatives have paid off in terms of a network of branches across the country. Yet, the extent of financial exclusion has been staggering. Out of the 600,000 habitations in the country, only about 30,000 had a commercial bank branch. Just about 40 per cent of the population across the country had bank accounts. The proportion of people having any kind of life insurance cover was as low as 10 per cent and proportion having non-life insurance was an abysmally low 0.6 per cent. People having debit cards comprise only 13 per cent and those having credit cards only a marginal 2 per cent. The National Sample Survey data revealed that nearly 51 per cent of farmer households in the country did not seek credit from either institutional or non-institutional sources of any kind. A sound system of institutions and instruments of intermediation is essential for promoting an efficient system. Increasing access to credit for the poor has always remained at the core of Indian planning in its fight against poverty. Nationalization of banks, massive expansion of branch network in rural areas, mandatory directed credit to priority sectors of the economy, subsidized rates of interest and creation of RRBs & NABARD are some of the notable measures in this direction. Though these measures resulted in impressive gains in rural outreach and volume of credit, the structure built up was 'quantitatively impressive but qualitatively weak'. We still have a long way to go to fully realize the original objectives of inclusive growth.

IMPORTANCE OF FINANCIAL INCLUSION

The importance of financial inclusion, based on the principle of equity and inclusive growth, has been engaging the attention of policy makers internationally. Achieving universal financial inclusion is, indeed, a global objective and has multiple dimensions. RBI has reported that the financial exclusion in India leads to the loss of GDP to the extent of two percent. The externality of asymmetric information between the financial institutions and the disadvantaged section of the population may be the main cause of this exclusion. Besides, the geographical distance from bank, diffident, financial illiteracy, gender-inequality, paucity of income and collateral assets, lack of proof of identity of the disadvantaged people are the plausible causes of financial exclusion. So, there is a vast scope of achieving total financial inclusion in a country if it adopts necessary steps to reduce the information gap. Against this backdrop, India has taken several steps towards financial inclusion. The prime objective of these steps is to provide banking services at an affordable cost to the weaker section of population. Since 2004 the Government and the financial regulators of India have been encouraging financial institutions to solve these problems. In this context the SHG-centric microfinance program has also received a deep attention.

Some exclusive steps like facility of 'no frills' account, Kisan Credit Card, have also been adopted to achieve total financial inclusion by 2015. In India financial inclusion has been started with opening 'no frills' account and issuing a few General Purpose Credit Cards for all. However, it is not the end of the story of financial inclusion. It emphasizes on the access to basic formal financial services at an affordable cost in a sustainable manner for the vulnerable people. Therefore, Financial Inclusion refers to a situation where people, in general, have connection with the formal financial institutions through holding savings bank account, credit account, insurance policy etc. It may help the person to have affordable access to financial services like formal savings, credit, payments, insurance, remittance etc. It accelerates the circulation of currency and thereby increases the GDP. Therefore, financial inclusion is important for faster inclusive growth.

The unique aspect of Finance Inclusion in India is that it is delivered through a variety of channels. These include branches of commercial banks and Regional Rural Banks (RRBs) directly dispensing micro credit and through their Business Correspondents (BCs), Self Help Groups (SHGs) linked to bank branches, cooperative banks and primary cooperative societies, micro finance institutions (MFIs) as NBFCs and in other forms, obtaining funds from a variety of sources, domestic and external. Ultimately, it is an issue of reaching out to low-income families in a cost-effective, hassle-free and sustainable manner, particularly to those who, otherwise, would not have had such access to financial services.

The broad principle behind Financial Inclusion initiatives is: (i) to act as a cost effective avenue for the formal financial sector to expand its coverage of poor; (ii) to develop effective collateral substitutes; (iii) to emphasize on the poor masses, both rural and urban, especially women; and (iv) to focus on the objectives of macro-economic growth. Indirectly, Financial Inclusion improves schooling, health and women's empowerment.

To meet the criterion of availability of banking services, a minimum of four basic products must be offered to customers:

- A check-in account with emergency credit facility
- Payment services and remittance facility
- A pure savings product such as a recurring deposit
- Facility of entrepreneurial credit to deserving people

Financial Inclusion of the poor has a multiplier effect on the economy as a whole, through higher savings pooled from the vast segments of the population present at the bottom of the pyramid. There is a potential for transforming the lives of these excluded groups by providing access to formal savings arrangements and extension of credit by banks for emergency and entrepreneurial purposes, thereby enabling the poor to create assets, generate stable income, build resilience to meet macro-economic and livelihood shocks and bring about an improvement in their financial condition and living standards. Today, banking connectivity has reached nearly 2,04,800 villages through brick and mortar branches, Business Correspondents (BCs) and other modes. During the last 3 years, 96.25 million Basic Savings Bank Deposit Accounts (including erstwhile No Frill Accounts) have been opened.

STEPS TOWARDS FINANCIAL INCLUSION:

In the context of initiatives taken for extending banking services to the small man, the mode of financial sector development was characterized by:

- a hugely expanded bank branch and cooperative network and new organizational forms like RRBs;
- a greater focus on credit rather than other financial services like savings and insurance, although the banks and cooperatives did provide deposit facilities;
- lending targets directed at a range of 'priority sectors' such as agriculture, weaker sections of the population, *etc*;
- interest rate ceilings;
- significant government subsidies channeled through the banks and cooperatives, as well as through related government programs;

a dominant perspective that finance for rural and poor people was a social obligation and not a potential business opportunity.

FINANCIAL INCLUSION IN ANDHRA PRADESH:

Andhra Pradesh has witnessed various attempts at financial inclusion – including the creation of a commoditized microfinance market, presumably to address the financial needs of those at the bottom of the pyramid, that is, the poor. These attempts may be broadly divided into two categories: a) government attempts at financial inclusion, and b) private attempts at financial inclusion, particularly to include the bottom of the pyramid through the spread of microfinance institutions (MFIs). In spite of being extolled as a tool for poverty eradication, microfinance loans were high cost loans that could be accessed by anybody able to form a group either in the form of an SHG or a Joint Liability Group (JLG). Microfinance companies facilitated this easy access through a system that had few prudential norms for borrowers and lenders, with little oversight of the end use of funds.

By 2010, the MFI business in AP thrived on a combination of ever-increasing quantum of credit aided by incentives of commission based on volumes, and increasing ability of the SHGs and JLGs to borrow from several MFIs. However, the increased lending by MFIs often did not lead to any growth in the incomes of the borrowers, since only a small component of this debt was channeled into income generating activities. In the mean time, increased profitability of the MFIs fuelled growing investor interest, especially from global private equity players, which culminated in the listing of SKS Microfinance Limited on the stock exchanges in 2010. The success of the initial public offering (IPO) of SKS Microfinance – over-subscribed by institutional investors 13 times11 – reinforced the investors' thinking that lending to the poor was a high return investment with charitable ends.

After analyzing some of the attempts to expand financial inclusion within and beyond the formal banking sector, which yielded mixed results and a number of spectacular failures, there is a need for an optimal strategy to expand financial inclusion would be through the expansion of the formal banking sector, especially the public sector banks. Although both the public and private sector banks are subject to the same prudential norms, that give incentives to prevent adverse selection, we emphasize the public sector banks because:

a) Public sector banks have much larger branch presence in the "unbanked" areas, especially if their regional rural bank branches are also included;

b) Despite its potential problems, political pressure, especially at the district level, is much higher on the public sector banks than on the private sector banks;

c) Public sector banks play a much larger role in government sponsored schemes, especially those that are subsidy linked.

This has given rise to the opportunity to open up new initiates for the Financial Inclusion in the state. The people are suspicious about the BC or other indirect modes of financial services provided by the banks.

One of the major challenges in AP in the realm of financial inclusion is the complexity in regulating consumer finance, especially in regulating savings: The rural poor can neither find nor understand financial information as financial literacy is non-existent across most of the state. In a number of districts, it is common for the poor to save small amounts – varying from Rs. 10 to Rs. 50 – on a daily basis. The absence of saving products offered by formal financial institutions, coupled with financial illiteracy, allows the plantation and real estate companies to fill the vacuum and collect deposits from the poor, in complete contravention of the RBI guidelines. The plantation companies offer a return of about 8 percent on savings that are modeled on a recurring deposit product of the banks. These companies mask this deposit collection under such pretense as receiving advances against the sale of land, which rarely exists.

FINANCIAL INCLUSION PLAN – ACHIEVEMENTS SO FAR

Snapshots of the progress in certain key parameters in the recent period (March 2010 – Dec 2012) are given below:-

i. Banking connectivity to more than 1,88,028 villages upto Dec 2012 from 67,694 villages in March 2010.

ii. All unbanked villages with population of more than 2000 persons, numbering around 74,000 are now connected with banks.

iii. Number of BCs increased to 1,20,098 from 34,532.

iv. More than 70 million basic banking accounts have been opened to take the total number of such accounts to 147 million.

v. About 36 million people/families have been credit linked.

The emphasis would be on the use of electronic payment products and services that can be accessed anywhere and anytime by anyone at affordable prices. Thus, the seven cornerstones of financial inclusion, i.e., **A**ccessibility, **A**vailability, **A**ffordability, **A**wareness, **A**cceptability, **A**ssurance and **A**ppropriateness have been incorporated as basic principles to enable payment system to play a role of catalyst in furthering financial inclusion.

FINANCIAL INCLUSION IN EAST GODAVARI DISTRICT:

East Godavari District is covered over an area of 10805 Kms rich in rice production, Oil & Gas exploration. Large areas are under the belts of Krishna – Godavari basin. It has a population of over 51 lakhs with 3 Lok Sabha and 19 Assembly Constituencies. There are 60 mandals with over 1400 villages in the district. The total numbers of villages with over 2000 population are over 600. The villages which are covered under Financial Inclusion are 400 which mean that there are more than 1000 villages which are deprived of financial services directly.

The average number of deposit account is 65 whereas the average number of credit account is only 9 per hundred population aged seven years and above. Therefore, average savings widening of the states shows a fair picture of financial inclusion, though there is a wide variation. However, the figure of credit widening is disappointing. The standard deviations of the number of banks per lakh population and per thousand square kilometers indicate that bank branches have been extended in accordance with the strength of population but not in accordance with the physical area. It may be a cause of the high level financial exclusion. It has been seen that the average saving-income ratio of the states is fairly high. On average 47 percent of net state domestic income has been covered by institutional credit. It appears to be a good indication of financial inclusion. It reveals that in terms of financial deepening Indian states on average have achieved a commendable position. It is seen that there is a wide variation among the states in terms of per capita savings and in terms of per capita loan outstanding. There has been a noticeable expansion of SHGs across the states which include the poor people under the purview of formal financial institutions.

CONCLUSION

The emphasis on the Financial Inclusion in recent times is more as the Government has taken the initiative to implement social welfare schemes which are linked to the savings account to eradicate possible corruption in these areas.

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