International Journal of Research in Social Sciences
Vol. 11 Issue 03, March 2021
ISSN: 2249-2496 Impact Factor: 7.081
Journal Homepage: http://www.ijmra.us, Email: editorijmie@gmail.com
Double-Blind Peer Reviewed Refereed Open Access International Journal - Included in the International Serial Directories Indexed & Listed at: Ulrich's Periodicals Directory ©, U.S.A., Open J-Gate as well as in Cabell's Directories of Publishing Opportunities, U.S.A

FINANCIAL INCLUSION : WAY FORWARD

- **Kumar N Lohit**

1. Introduction

Inclusive growth is an essential prerequisite for economic, financial, political or social stability. Financial Inclusion which has caught the attention of all across the world- government, development agencies, economist, banks etc. is being considered as a driver for bringing about inclusive growth. Governments are making provisions in the budgets to bring in the excluded population in the formal financial net. Development agencies are allocating funds to help bring in transformation in the target segment.

With so much focus by various agencies, question arises whether Financial Inclusion is a pressing concern – if at all then what needs to be done.

2. Extent of Financial Exclusion

The extent of exclusion varies from country to country. China has the highest number of households who are financially excluded (263 million) followed by India (135 million) and Africa (130 million). India has more financially excluded households than US, Latin America, Middle East and Europe combined together. (IDBI Bank, 2005). According to a study by Mckinsey (2010), China with More than half the world's working-age population does not have quality, affordable financial services. That's about 2.5 billion adults—2.2 billion of whom live in Africa, Asia, Latin America, and the Middle East.

3. Financially Excluded segment

On a daily basis, we come across names of numerous banks- small, medium and big spread across geographies providing various products & services to the customers. Yet there exists certain section of the society which has remain untouched by even the basic banking services. This segment is constituted by:

(a) Migrants
(b) Ethnic Minorities
(c) Retired Population
(d) Over-indebted people
(e) Students
(f) Physically Challenged
(g) Illiterate
(h) Unemployed people
(i) Rural population

This segment exist not only Third World Countries but also in the Emerging and Developed nations as well.

4. Banking & Bottom of the Pyramid

Bottom of the Pyramid is a term coined by Prof. (Late) C.K. Prahlad. This concept caught the fancy of the FMCG and white goods companies who have encashed upon this segment. Companies like Unilever, Pepsi Co, Coca-Cola and various others saw a latent business opportunity in this segment. The regular products, packaging & pricing were tweaked and distribution channel was leveraged to reach to the masses. During the good times, this segment helped in improving the bottom line and the top-line and during rainy days, it protected both the vital parameters. One can find various examples from the business world.

Yet banking is one sector which has stayed away from this segment. This has allowed informal sources of finance to cater to the financial needs of the unbaked segment. Taking advantage of the void created by absence of formal banking channel, informal channels have exploited the needy to their benefit. Places where banking nodes exists, these channels have emerged as necessary evils for the people. This is an own creation of the banking sector. The norms laid down by the banking sector makes it difficult for the people to make full use of the banking sector. This makes the people to visit local moneylenders to raise finances with ease even though at higher interest rates.

5. Implications of Financial Exclusion

Lavinia Mitton (July 2008) identified the implications of Financial Exclusion:

- Denying access to credit results in people seeking funds form informal sources at higher cost.
- Lack of savings and investments makes people vulnerable to various shocks that arise from time to time.
- Leakages arising during transfer payments in absence of electronic payment system of banking channel.
- Masses are denied access to various additional services of the banks like remittances, payments etc.
- Banks are denied access to additional source of cheaper funds.

6. What creates Financial Exclusion?

Like any market place, disequilibrium in demand and supply for banking products and services results in glut or shortage. In banking, this mismatch results in Financial Exclusion.

Mitton (July 2008), Kempson and Whyley (1999a, 1999b) and Kempson et al. (2000) have provided reasons for Financial Exclusion. These reasons are intertwined and can be resolved as under:

- **Geographical Spread:** Due to absence of branch network certain geographies tend to be classified as unbaked or underbanked. This situation arises due to closure of branches or unwillingness of the banks to venture into such areas.

- **Socio-Cultural Factors:** At times, societal & cultural factors influence a person to shun the banking system. They prefer to rely on the financial system that has developed within the community over a period of time. Even though, such systems perform efficiently within the community, as people are not included in the formal channel, they are counted as excluded.

- **Product Features:** Type of banking products required by the excluded population is different from the one required by the affluent section of the society. The product features are embedded by the banks with a view towards risk aversion, prudence or regulatory compliance. These tend to reduce the marketability of the product in the unbanked and underbanked section.

- **Cost of Delivery and Pricing:** Lack of reach and absence of banking channels tend to increase the cost of delivery of bank services to this section. This cost is generally passed on to the customers in terms of higher pricing making product & services unaffordable.

- **Willingness of Banks:** Very often, banks are not willing to cater to this segment as serving this segment tends to affect their Financial Statements in the short run.

7. Financial Inclusion: Is it actually required?

Various agencies have stepped up their ante in favour of financial inclusion. This initiative or movement, as it may be referred, involves costs, technology, manpower and policy making. Yet certain sections keep on dwelling whether it is actually required.

Proponents of this movement occasionally point out to the need of inclusive growth. A large section of the society, represented by the Bottom of the Pyramid, has been deprived of the banking facilities. This has tilted the growth curve of the economies towards the prosperous and the rich.

Banks, in rudimentary terms, perform the task of channelling the funds from surplus sector to deficit sector. This channelling allows wealth creation & accumulation and leads to economic growth. Involving the deprived section in this cycle will not only create wealth but also increase consumption. Fruit of this benefit will be shared by all the sections and bring in more broad based and equitable growth for the economy. A broad-based growth is beneficial to any economy. In times of external shocks, domestic market is of prime importance to sustain the economy. Including larger section of the society in previous growth pattern will allow any economy to face the tough economic conditions and will be able to maintain decent growth rate. In recent times, India is one such example, where various development activities in the country and active role of the banks in the same, has helped maintaining a healthy growth rate when the world economy is reeling under debt-crises.

As of now, rural locations are disjointed from the urban economies yet they have self-sufficient economy. Rural economy is also a significant contributor to the overall economic growth of a nation primarily in the poor and the developing countries. Yet they have remained poor cousin to the urban location. In an ideal scenario, there has to be a backward and forward linkage between the rural and the urban economies. To achieve this scenario, it is imperative that rural economy be given due importance.

Turning to the business side of banking, underbanked and unbanked population varies from 40%-80% across geographies (IBA, 2010). This shows the market that has been left untapped by the banks. If this market is tapped with a resolute strategy, financial institutions will be able to generate good amount of business in the both deposits and lending arena. Off-late, certain Non-Banking Financial Institutions, MFIs, Insurance Companies etc. have taken a lead over banks in penetrating this segment. These institutions products have designed to suit this market segment. Yet there is enough scope for other institutions to enter with more new products. This entry has to be complemented with friendly policy & regulatory environment for the both the customers as well as the financial institutions.

Need for credit exists is such economies but financial institutions have mental make-up that prohibits them from lending in the rural areas. Institutions have always raised questions on the credit-worthiness of the borrowers from these areas. Examining the issue deeply, one will find out that one of the major factors is that of documentation. Illiteracy level combined with lack of documentation makes it difficult for the rural populace to access credit facility. Close look at the banking data, on the other hand, proves that rural population is more religious in clearing of their debt. Also the amount of credit required by the rural population is small when juxtaposed with the requirement in the urban areas. Banks also benefit with smaller ticket size which is accompanied by reduced risk.

8. Way Forward :

With emphasis from various quarters, seriousness about Financial Inclusion can be gauged. Various institutions are following different models for implementations of Financial Inclusion. It has been argued that the goal of financial inclusion is better served through mainstream banking institutions as they have the capability to provide suite of products required to bring in effective/meaningful financial inclusion (Chakrabarty, 2012). However, despite focused campaigns, the desired results are yet to be achieved.

To begin with, players in this space needs to adopt appropriate business model. This should be done after considering various factors like geography, market size, customer psychology, technology, capital – fixed and working etc.

In most of the countries, players are trying to harness the mobile technology for financial inclusion. M-Pesa is one such example. At times, non-bank led models have been considered as Financial Inclusion. Rather, it is partial inclusion as the customer does not become a part of any financial institution. In such cases, customers tend to rely completely on the network of the service provider.

Financial Inclusion will be achieved in totality provided the excluded section gets the same level of customer service and experience as that of normal customer. Blindly relying on just one type of technology or business model is fraught with its own risk. Financial Institutions should rather opt for a mix of bank-focused, bank-led and non-bank led model.

In the present economic environment, telecom companies have made substantial investments in their network to provide connectivity to all sundry. This network availability should be harnessed by the banks and other institutions to reach out to the masses with seamless integration to the banking network. Technological advent and numerous communication terminals have made this possible.

Impact through Financial Inclusion can be the most provided right kind of product mix coupled with appropriate features is offered to the target segment. It will be foolhardy to expect that the customers of the target market in question will be able to fully benefit from the products being offered to normal & regular customer. These new and exclusive products will not just serve the requirements of the population but also will help the formal institutions in building their reputation within this population set. Moreover, financial institutions will be able to test the market and gather enough knowledge on customer preferences and understanding to develop right kind of product. Once the customers gain confidence in the formal banking system, then will gradually move away from the traditional sources of finances.

To begin with, concept of micro-savings, micro-credit and micro-investments need to be introduced. Microsave, an institution in this, space innovatively utilized concept of barter economy to induce impoverished to start saving.

Occasionally, it has been observed that documentation is one of the major hindrances that the population in question in this paper tend to lack documentation or have documents that are not enough to avail banking services. This limitation needs to be a key consideration at the time of development of products.

Role of the Financial Institutions should not be restricted as provider of banking services. They also need to play the role of mentor. Concept of Village Enterprises, pioneered by China during the early years of Communism, need to be re-introduced in the current context. With proper guidance, grooming and information from the banks, the rural populace will be able to access the market and benefit from the overall growth of the economy.

Success of Financial Inclusion is a lot dependent on Financial Literacy. They are complementary to each other. This is needed in both the developed and the under-developed countries. Degree of awareness will vary from country to country based on the development, education level and spread of banking within a particular country. Financial education will not only spread awareness about the banking system and the facilities but will also provide a window to the institutions to market themselves as also create demand for various products/services.

In this initiative banks have to incur huge capital costs – fixed as well as working. Returns are low and delayed, putting strain in the already vulnerable financial position of the banks. In order to prop up the financial institutions to become a part of financial inclusion, incentives may be provided by the development agencies and the government. Part of these can be passed on to the customers. This will be a win-win situation for the bank as well as the customer. Banks will be able to recover their costs. It needs to be noted here that such grants/ incentives should not be continued infinitely as this will distort the pricing of products and services. Banks should be given timelines by which they have to attain profitability in operations in under-banked and unbanked areas.

Last but not the least and one of the most important is the policy environment. Friendly and stable policy environment will be needed by all the stakeholders to prepare their roadmap for the long-run. Frequent changes in the policy will lead to disturbance which will eventually affect the implementation of the strategy. This will also see cost over-runs in implementation thereby hampering the achievement of overall objective of financial inclusion.

9. Conclusion

It is evident that Financial Inclusion is a phenomenon that is going to stay for quite some time. It is understood that it is a capital intensive initiative with a long gestation period. In this whole, patience of all the stakeholders will be of prime importance.

At any point of time, it should not be seen as a corporate social responsibility. Rather, it should be viewed as business opportunity which remained untapped for a long duration. Successful implementation of Financial Inclusion with efforts of all will bear fruits that can be enjoyed by the complete society without any discrimination.

In pursuit of financial stability and overall inclusive growth, the focus of policy makers and market participants should be to recognise the harmonious relationship between Financial Inclusion, Financial Literacy and Consumer Protection.

Source : Chakrabarty (2012)

References

Chakrabarty, K.C (2012), Panel Discussion on Financial Literacy and Consumer Protection, Washington, DC.

Collard, S. (2007) 'Toward financial inclusion in the UK: progress and challenges', *Public Money and Management*, Vol. 27, No. 1, pp. 13–20

Collard, S., Kempson, E. and Dominy, N. (2003) *Promoting Financial Inclusion: An Assessment of Initiatives Using a Community Select Committee Approach*. Bristol: Policy Press

Collard, S., Kempson, E. and Whyley, C. (2001a) *Tackling Financial Exclusion in Disadvantaged Areas*. Bristol: Policy Press

IDBI Bank Report (2010) '*Financial Inclusion : Way Forward',* Mumbai, India.

IBA (2010). Committee on Inclusive Growth, Mumbai, India.

Kempson, E., Whyley, C., Caskey, J. and Collard, S. (2000) *In or out? Financial Exclusion: A Literature and Research Review*. London: FSA

Kempson, E. and Whyley, C. (1999a) *Kept out or Opted out? Understanding and Combating Financial Exclusion*. Bristol: Policy Press

Kempson, E. and Whyley, C. (1999b) 'Understanding and combating fi nancial exclusion', *Insurance Trends*, Vol. 21, pp. 18–22.

Mckinsey Report (2010), *Global Financial Inclusion*.

RBI Annual Report (2011)