Financial Inclusion for Inclusive Growth of India - A Comprehensive Study

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Abstract

India is a developing country, it is one of the largest and fastest growing economies of the world, but what has been the most troubling fact about its growth is that its growth is uneven and also discrete. So the need arises for inclusive growth comes in the picture of Indian economic development. However to attain the objectives of inclusive growth there is a need for resources, and for resource generation financial inclusion is required. It plays a very crucial role in the process of economic growth. The present paper focuses on to understanding inclusive growth phenomenon its need and financial inclusion as an instrument to attain it with reference to its extent in India. The research has been done using secondary data source. Analysis of natural hierarchical grouping cluster is done considering parameters like GDP per capita, literacy rate, unemployment rate and index of financial inclusion (Johnson R.A. & Wichern D.W., 2000).

Keywords: **Inclusive Growth &Financial Inclusion**

INTRODUCTION

India is one of the largest and fastest growing economies of the world, but what has been the most disturbing factabout its growth is that its growth has not only been uneven but also discrete. It has been uneven in the sense that there hasbeen no uniformity in its growth performance and it has been discrete and disconnected with regard to growth anddistribution of growth benefits to certain sections society. The Indian economy, though achieved a high growthmomentum during 2003-04 to 2007-08, could not bring down unemployment and poverty to endurable levels. Further, avast majority of the population remained outside the ambit of basic health and education facilities during this high growthphase. In recent decades, economic and social inequalities have increased alongside high growth rates which haveincreased regional inequalities. Over 25% of Indians continue to live in under poverty line. As a result, Government of India considered Inclusive growth as a national policy objective. And thus the need for inclusive growth comes in the pictureof Indian economic development. In context of Indian growth planning it is a relatively new terminology which got theattention of policy makers in the Eleventh Five Year Plan.Inclusive growth as the literal meaning of the two words refers to both the pace and the pattern of the economicgrowth, it basically means, broad based, shared, and pro-poor growth. As per the Planning Commission of India “The term“inclusive” should be seen as a process of including the excluded section of society whose participation is essential in the verydesign of the development process and not simply as welfare targets of development programmes.” In a simpler and widersense it means that inclusive growth as a strategy of economic development should not only aim at equitable distribution ofgrowth benefits but also at creating economic opportunities along with equal access to them for all. In the present paper aneffort has been made to understand the inclusive growth phenomenon its need and financial inclusion as an instrument toattain it with reference to its extent in Indian States.

LITERATURE REVIEW

Levine (1997) empirically tested the neo-classical view and finds that countries with larger banks and more activestock markets grow faster over subsequent decades even after controlling for many other factors underlying economicgrowth. Equally important is access to finance by all segments of the society (Levine 1997, Pande and Burgess 2003)**.**Finance can also play a positive role in poverty reduction. A well developed financial system accessible to all reduces information and transaction costs, influence saving rates, investment decisions, technological innovation, and long-rungrowth rates.

(Beck *et al.* 2009). Evidences from Binswanger and Khandker (1995) and Pande and Burgess (2003) suggestthat Indian rural branch expansion program significantly lowered rural poverty, and increased non-agriculturalemployment.A key objective in development economics is to work out ways to uplift people out of poverty. Access to finance hasbeen seen as a critical factor in enabling people to transform their production and employment activities and to exit poverty
(Aghion and Bolton 1997, Banerjee 2001, Banerjee and Newman 1993, Pande and Burgess 2003, Yunus 1999).In recent years, financial inclusion has assumed public policy relevance. Many countries like India (Governmentof India 2008) and the United Kingdom (UK) (2006) and International organizations like the United Nations (2006), WorldBank (2008, 2009) have set up task force/committees to understand financial inclusion and to improve its scope. Thesestudies throw light on various aspects of financial inclusion. However, the measurement aspect of financial inclusion has,so far, not extensively been covered by these reports.For India, being a very well diversified economy and society, it is imperative to give adequate attention to measurement of financial inclusion. There are few scholars who have attempted to measure some aspects of financialinclusion.

Honohan (2007) estimated the fraction of the adult population using formal financial intermediaries using theinformation on number of banking and MFI accounts for more than 160 countries, and then correlated with inequality (GiniCoefficient) and poverty. Sarma (2008) developed an Index for financial inclusion using aggregate banking variables likenumber of account, number of bank branches and total credit and deposit as proportion of GDP for 55 countries. Mehrotra*et al.* (2009) also built up an index for financial inclusion using similar kind of aggregate indicators like number of ruraloffices, number of rural deposit accounts, volume of rural deposit and credit from banking data for sixteen major states ofIndia. Moreover, World Bank (2008) provides a composite measure of access to financial services, that is, the percentage of adult population that has an account with a financial intermediary for 51 countries. While World Bank (2009) in*Banking the Poor* analyzed the association between access to banking services, as measured by the number of bankaccounts per thousand adults in each country, and several other factors like transactions offered at banks, or required bybanks, and regulations adopted by country authorities that may affect banking access for 45 countries.

Sadhan Kumar Chattopadhyay in a working paper for RBI on Financial Inclusion in India: A case-study of WestBengal (2011), has examined the extent of financial inclusion in West Bengal. According to the study there has been animprovement in outreach activity in the banking sector, but the achievement is not significant. An index of financialinclusion (IFI) has been developed in the study using data on three dimensions of financial inclusion viz- banking penetration (BP), availability of the banking services (BS) and usage of the banking system (BU). The paper provides acomparable picture between different states on the basis of IFI rankings.The present paper focuses onto financial inclusion as an instrument for attaining inclusive growth- in context ofIndia, for which a fair deal of effort has been taken to understand the extent of financial inclusion in India as a whole andstates as its part.

OBJECTIVES OF THE PAPER

The Specific Objectives of the Research Paper are as Follows

- To study & understand the meaning and need for inclusive growth.
- To study the role of financial inclusion in inclusive growth.
- To know the extent of financial exclusion/inclusion in India.

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RESEARCH METHODOLOGY

The research has been done using secondary data .Analysis of natural hierarchical grouping cluster is done. For this analysis parameters like GDP per capita, literacy rate, unemployment rate and index of financial inclusion were considered (JohnsonR.A. & Wichern D.W., 2000). The choices of measure of similarity are based on Euclidean distances betweenmultidimensional observations.

Need for Inclusive Growth

India needs inclusive growth in order to attain rapid growth. It is necessary forsustainable development and equitable distribution of wealth and prosperity. Achieving inclusive growth is one of the biggest challenges for India. The challenge is to take the levels of growth to all section of the society and to allparts of the country. Rapid growth in the rural economy, sustainable urban growth, infrastructure development, reforms ineducation, health, ensuring future energy needs, a healthy public-private partnership, intent to secure inclusivity, makingall sections of society equal stakeholders in growth, and above all good governance will ensure that India achieves what itdeserves. The main thrust areas for need of inclusive growth can be summarized as below:

- Reduction in regional disparity
- For social sector development
- Protecting environment
- Removal of poverty and unemployment
- Removal of income inequalities
- Agricultural Development

However for attaining the objectives of inclusive growth there is a need for resources, and for resource generationand mobilization financial inclusion is required. It plays a very crucial role in the process of economic growth. Financialinclusion through appropriate financial services can solve the problem of resource availability, mobilization and allocationparticularly for those who do not have any access to such resources. Thus in the current paper an effort is made to study the Role of financial inclusion in inclusive growth.

Financial Inclusion

Financial inclusion, we mean the delivery of financial services, including banking services and credit, at anaffordable cost to the vast sections of disadvantaged and low-income groups who tend to be excluded. The variousfinancial services include access to savings, loans, insurance, payments and remittance facilities offered by the formalfinancial system.

Rangarajan Committee (2008) viewed financial inclusion as "The process of ensuring access to financial servicesand timely and adequate credit where needed by vulnerable groups such as weaker sections and low income groups at anaffordable cost"In simpler terms financial inclusion is about including the excluded in the financial system of the country, and toensure that their financial & social security needs are taken care of through appropriate financial service providers.

Role of Financial Inclusion

Financial Inclusion is imperative for inclusive growth of India, with more than 25 % of its population living inwretched poverty government's obligation towards their growth and development is huge, and inclusive finance is one suchmeasure if it is targeted and attained in right manner will provide a right solution to the severe problems of poverty and unemployment.

Providing access to financial services has significant potential to help lift the poor out of the sequence of poverty.Financial inclusion promotes thrift and develops culture of saving among the people and also enables efficient payment mechanismstrengthening the resource base of the financial institution which benefits the economy as resources become available forefficient payment mechanism and allocation. Poors are typically more vulnerable to financial exclusion this is simply because their major problems arise fromthe need for funds. The formal banking services, by making judicious use of targetedsubsidies may help to reduce or remove market imperfections and facilitate financial inclusion of the vulnerable group of the society, ultimately leading tohigher incomes. The access to financial services by poors would lead to their consumption smoothing and investments inhealth, education and income generating activities, and expanding growth opportunities for them. Inclusive growth if besieged systematically it may lead to financial stability, asset building and economic mobilityand empowerment of the low income group people. Thus if we are talking about inclusive growth with stability, it is not possible without financialinclusion.

However one should understand that inclusive finance is a long run phenomenon which cannot be achieved overnight, especially developing country like India where the access to financial products is controlled byseveral factors such as lack of awareness, unaffordability, high transaction costs, and inconvenient, too many documents, inflexible and unsuitable products.

Extent of Financial Inclusion in India

Recent years almost all the countries across the globe look at financial inclusion as the means for a more comprehensive growth,wherein, each citizen of the country is able to use his/her earnings as a financial resource that they can put to work toimprove their future financial status and simultaneously contribute to the nation's progress.Financial inclusion has always been accorded high importance by the Reserve Bank and Government of India toaid the inclusive growth process for the economy, the history of financial inclusion in India is actually much older than theformal adoption of the objective.The nationalization of banks, Lead Bank Scheme, incorporation of Regional Rural Banks,(Karnataka Grameen Bank) Service Area Approachand formation of Self-Help Groups - all these were initiatives aimed at taking banking services to the masses. The brickand mortar infrastructure expanded; the number of bank branches multiplied ten-fold - from 8,000+ in 1969, when the firstset of banks were nationalized, to 99,000+ today.

Table-1 below provides a glimpse of the manifold expansion of bankbranches in India with their percentage distribution in rural areas as well.

Table-1: Bank Branches

Year	Rural	Semi-urban	Urban &Metropolitan	Total	Rural share (%)

1969	**1833**	**3342**	**3087**	**8262**	**22**
1970	**3063**	**3718**	**3350**	**10131**	**30**
1975	**6807**	**5598**	**6325**	**18730**	**36**
1980	**15105**	**8122**	**9192**	**32419**	**47**
1990	**34791**	**11324**	**13637**	**59572**	**58**
2000	**32734**	**14407**	**18271**	**65412**	**50**
2005	**32082**	**15403**	**20870**	**68355**	**47**
2010	**32554**	**21035**	**34824**	**88441**	**37**
2011	**33813**	**23236**	**36750**	**93799**	**36**
2012	**35653**	**25542**	**38698**	**99884**	**36**

Sources: RBI

It can be clearly observed from the above given data that there has been tremendous growth in the spread ofbanking network in the country since 1969. However despite this wide network of bank branches spread across the lengthand breadth of the country, the extent of financial exclusion in India is staggering.Out of the total habitations in the country, only about 36,000+ had a commercial bank branch. Just about 40per cent of the population across the country has bank accounts. The proportion of people having any kind of life insurancecover is as low as 10 per cent and proportion having non-life insurance is awfully low at 0.6 per cent.People having debit cards comprise only 8 per cent and those having approval cards only a marginal 2 per cent of the population.

Below given data in **Table-2**shows a few States Index of Financial Inclusion, GDP per capita, literacy rate andrate of unemployment in the different states of India.On the basis of IFI developed it can be clearly identified that which are the states where there is need for increasing banking penetration (BP) , as well as the stateswhere there is need for increasing availability of banking services and need to push usage of banking system. Moreover itis felt that there is need of a comprehensive financial inclusion plan for India as a whole along with region specificinclusion plans targeting its typical requirements based on its existing level of financial inclusion.

Table -2: A Few States Index of Financial Inclusion

State	D1	D2	D3	IFI	IFI rank	GDP (per capita)	Literacy rate	Umemployment rate
High Financial Inclusion								
Kerala	0.70	0.81	0.28	0.54	1	83,725	93.9	2.5
Maharashtra	0.62	0.28	1	0.53	2	101,314	80.1	2.6
Karnataka	0.72	0.47	0.46	0.53	3	68,374	75.6	2.4
Medium Financial Inclusion								
Tamil Nadu	0.70	0.42	0.39	0.49	4	94786	80.3	2.1
Punjab	0.45	0.68	0.29	0.46	5	74,605	76.7	1.6
Andhra Pradesh	0.56	0.30	0.41	0.40	6	71,580	67.7	NA
All-India	0.27	0.22	0.55	0.33	7	60,598	74.04	NA
Himachal Pradesh	0.42	0.40	0.18	0.33	8	74,898	83.3	1.3

Sikkim	0.28	0.33	0.33	0.32	9	121,441	82.2	NA
Haryana	0.38	0.50	0.12	0.32	10	109,858	76.6	NA
Low Financial Inclusion								
West Bengal	0.24	0.37	0.23	0.28	11	54,830	77.1	NA
Gujarat	0.32	0.30	0.16	0.26	12	81,400	79.3	0.9
Uttar Pradesh	0.28	0.31	0.15	0.23	13	30,052	71.4	2.1
Meghalaya	0.21	0.28	0.14	0.21	14	52,976	74.5	1.3

Source:*- Financial Inclusion in India: A Case-Study of West Bengal, 2011Census-2011

From the data given in the above table it is quiet evident that the states which have high to medium degree offinancial inclusion also account for literacy rates and GDP per capita (per annum) higher than the country's average i.e.74.04 % &Rs.60,603 respectively, Andhra Pradesh being the only exceptional state to be with medium degree of financialinclusion with literacy rate 67.7 %, less than the country's average .

CONCLUSION

Inclusive growth attainment depends a great deal on equitable distribution of growth opportunities and benefits.And financial inclusion is one of the most crucial opportunities which need to be equitably distributed in the country inorder to attain comprehensive growth. It needs to be understood by the state that in order to bring orderly growth, orderneeds to be developed with regard to inclusive finance. The percentage of financial inclusion in the different states of thecountry varies differently. For instance Kerala, Maharashtra and Karnataka accounts for higher rate of financial inclusionbut the states such as Gujarat, West Bengal, Gujarat, Uttar Pradesh, etc stand poorly on the groundsof financial inclusion.Undoubtedly the issue of expanding the geographical and demographic reach poses challenges from theviability or sustainability perspectives and appropriate business models are still evolving and various delivery mechanisms arebeing experimented with by the various government agencies at the central and state level. But somewhere the efforts takenare not good enough to encounter this challenging issue of financial exclusion. Financial literacy and level of awarenesscontinue to remain an issue with regard to usage of financial services/products. It calls for coordination of all thestakeholders like sectoral regulators, banks, governments, civil societies, NGOs, etc. to achieve the objective of financialinclusion. Challenges of financial exclusion are faced by most of the states of the country and in order to solve it stateshave to develop its own customized solutions drawing upon its own experiences and features and those of its peers across the country.

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