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ROLE OF BANKS IN FINANCIAL INCLUSION IN INDIA : ISSUES, CHALLENGES AND STRATEGIES

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Abstract: Access to finance by the poor, disadvantaged and underprivileged group is a prerequisite of poverty alleviation on one hand and the economic growth on the other. In the struggle against poverty, the financial inclusion is a crucial element. Large sections of the rural population have no access to financial services and their only recourse is to borrow from moneylenders at the exorbitant charges causing exploitation. The main reason why the large section of the rural population still remains under below poverty is financial exclusion, which is proving to be a major obstacle in the path of India's economic growth. The Reserve Bank of India (RBI)'s dictate (2005) obligated the Banks to adopt the national policy of financial inclusion and take initiatives and suitable measures therefore. The objective data derived from the RBI's reports and other empirical studies unequivocally pinpoint that the main reasons of financial exclusion are lack of opportunities and access to finance, financial illiteracy, besides poor performance, apathy and negative approaches of the Banks. Therefore, financial inclusion, today, has become the national objective and major concern for the economic policy decision makers. This paper critically addresses all concerned issues involved in achieving the national objective of achieving the complete financial inclusion. This paper critically evaluates the initiatives taken by the Banks in financial inclusion and the efforts made for IT enabled financial services, on the basis of the objective data derived from the RBI'S reports and other empirical studies.

This paper stresses the need of matured, positive attitude and approach and sound strategy to achieve complete financial inclusion. This paper also looks at some of the business models and essential elements of profitable models for financial inclusion so as to increase the meaningful and whole hearted participation of the banks in achieving complete financial inclusion.

Keywords: Poverty alleviation, financial exclusion, financial illiteracy, Financial Inclusion, RBI, Information Technology, Business and Profitable models.

I. INTRODUCTION

Financial exclusion is the main cause of poverty. Lack of opportunities and access to finance besides financial illiteracy are the main causes of financial exclusion. Financial exclusion is proving to be a major thorn in the path of Indian economic growth. Access to finance by the poor, disadvantaged and unprivileged group is a prerequisite for poverty reduction and social upliftment. One of the main reasons why the large section of the rural population still remains under below poverty line is lack of opportunities and access to finance besides financial illiteracy.

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Large sections of the rural population have no access to financial services and their only recourse is to borrow from money lenders, who charge exorbitant rates. Also, ignorance is rife, with concepts like insurance virtually unheard of. One of the main reasons why mass poverty is persisting in India is that the problem of financing the poor still remains unresolved (RBI, 2011a). With almost all states show more than 60% of populations below the poverty line. Projections based on NSSO data present a disturbing picture as population cut offs for average consumption for almost all states fall between the sixth and seventh deciles, statistics for which are available in its report "Key indicators of household expenditure in India." Further fine tuned, they deliver a precise percentage of population below the average spends (Sunday Times, 2012).

The large section of population below the expenditure curve also points to a worrying inequity in incomes, something that should concern planners as the government looks to target benefits for those who need them through initiatives like food security and employment guarantees (Sunday Times, 2012). India's schemes might be off target, or suffering from poor reach while benefits of economic growth are not meeting the government's objectives of "inclusive growth" as it is evident from the data (vide Table-I) that there is a concentration of buying power in the top 30%-35% of the population. The 60-plus% of population below the average monthly spending is clearly not progressing as fast as the segment whose income and expenditure is disproportionately influencing the statistical mean (Sunday Times, 2012). Among the states, there is not much to choose between those often stigmatized as "backward" like UP and Bihar, Gujarat and Maharashtra. Even in the better off states, the percentage of rural populations below the average monthly expenditure line is above 60%. In urban areas, it is a shade under 60% for Gujarat, but almost 70% for Maharashtra (Sunday Times, 2012).

II. FINANCIAL EXCLUSION

Nature, Causes Costs and Consequences of Financial Exclusion

Financial exclusion is broadly defined as the lack of access by certain segments of the society to suitable, low-cost, fair and safe financial products and services from mainstream providers. Thus the essence of financial inclusion is to ensure that a range of appropriate financial services is available to every individual and enable them to understand and access those services. Apart from the regular form of financial intermediation, it may include a basic no frills banking account for making and receiving payments, a savings product suited to the pattern of cash flows of a poor household, money transfer facilities, small loans and overdrafts for productive, personal and other purposes, insurance (life and non-life), etc. (Chattopadhyay, 2011). Two major factors have often been cited as the consequences of financial exclusion. First, it complicates day to day cash flow management- being financially excluded means households and micro and small enterprises deal entirely in cash

Table I

State	Rural		Urban	
	Average monthly spending	*% Below This*	*Average monthly spending*	*% Below This*
Andhra	1,234	63.9	2,238	67.8
Arunachal	1,546	64.0	1,947	61.9
Assam	1,003	59.4	1,755	60.2
Bihar	780	60.6	1,238	66.2
Chandigarh	784	62.1	1,674	66.0
Delhi	2,068	62.1	2,654	63.2
Goa	2,065	61.2	2,644	62.5
Gujarat	1,110	60.6	1,909	60.0
Haryana	1,510	60.6	2,321	**69.2**
Himachal	1,536	64.5	2,654	64.9
J&K	1,344	61.0	1,759	66.6
Jharkhand	825	64.6	1,584	67.9
K'taka	1,020	62.8	2,053	64.6
Kerala	1,835	67.3	2,413	69.0
MP	903	64.0	1,666	66.8
Maharashtra	1,153	61.0	2,437	**69.1**
Manipur	1,027	60.1	1,106	68.7
Meghalaya	1,110	61.0	1,629	59.8
Mizoram	1,262	59.5	1,947	58.0
Nagaland	1,476	60.8	1,832	60.8
Orissa	818	62.4	1,548	67.0
Punjab	1,649	65.9	2,109	65.5
Rajasthan	1,179	67.0	1,663	65.3
Sikkim	1,321	68.7	2,150	53.5
TamilNadu	1,160	63.3	1,948	64.9
Tripura	1,176	63.8	1,871	64.4
Uttar Pradesh	899	62.8	1,574	70.0
Uttarakhand	1,747	83.6	1,745	62.6
West Bengal	952	60.6	1,965	68.4
All India	1,054	64.47	1,984	66.7

Notes: Average daily consumption expenditure per capita per day for rural areas is Rs. 35.10 and for urban areas in Rs. 66.10.

Source: Sunday Times of India, "Times Nation" New Delhi Edn. 29 April 2012, P. 15.

and is susceptible to irregular cash flow. Second, lack of financial planning and security in the absence of access to bank accounts and other saving opportunities for people in the unorganized sector limit their options for providing for themselves for their old age (Rabha, 2012).

The Report on Innovative Financial Inclusion from the Access through Innovation Sub-Group of the G20 Financial Inclusion Experts Group underlines the world scenario of financial exclusion:

- More than two billion adults do not have access to formal or semi-formal financial services;
- One billion people with mobile phones do not have even a basic bank account, (G-20, 2010).

Broadly, the issue of cost of financial exclusion may be conceived from two angles, which are intertwined. First, the exclusion may have cost for individuals/ entities in terms of loss of opportunities to grow in the absence of access to finance or credit. Second, from the societal or the national perspective, exclusion may lead to aggregate loss of output or welfare and the country may not realize its growth potential. Access to a bank account, credit and insurance are now widely regarded as essential supports for personal financial management and for undertaking transactions in modern societies (Rabha, 2012).

The financial exclusion can impose significant costs on individuals, families and society as a whole. These include (i) barriers to employment as employers may require wages to be paid into a bank account; (ii) opportunities to save and borrow can be difficult to access; (iii) owning or obtaining assets can be difficult; (iv) difficulty in smoothening income to cope with shocks; (v) exclusion from mainstream society. The principal barriers in the expansion of financial services are often identified as physical access, high charges and penalties, conditions attached to products which make them inappropriate or complicated and perceptions of financial service institutions which are thought to be unwelcoming to low income people (Rabha, 2012). The lack of accessibility to financial services to the poor and disadvantaged class has been identified as one of the serious threat for including the poor in the process of inclusive growth (NABARD, 2012).

III. ACCESS TO FINANCE: CONCEPTUAL FRAMEWORK

Concept and Definition of Financial Inclusion

The term 'Financial Inclusion' was first coined in British lexicon when it was found that nearly 7.5 million persons did not have a bank account. Defining financial inclusion is considered crucial from the viewpoint of developing a conceptual framework and identifying the underlying factors that lead to low level of access to the financial system (Raju, 2006).

Review of Literature

A review of literature suggests that there is no universally accepted definition of financial inclusion. The definitional emphasis of financial inclusion varies across countries and geographies, depending on the level of social, economic and financial

development; the structure of stake holding in the financial sector; socio-economic characteristics of the financially excluded segments; and also the extent of the recognition of the problem by authorities or governments. Broadly, financial exclusion is construed as the inability to access necessary financial services in an appropriate from due to problems associated with access, conditions, prices, marketing or self-exclusion in response to discouraging experiences or perceptions of individuals/entities.

The poor need financial services mainly for three purposes, all of which call for equal attention (Rutherford, 2001) :-

- Firstly, to defray expenses related to education, house-building, invariably go in for loans.
- Secondly, there are emergencies such as serious illnesses, death in the family, and property loss due to accident.
- Thirdly, there are investment needs to buy or build income-earning assets.

Over the years, several definitions of financial inclusion/exclusion have evolved. The working or operational definitions of financial exclusion generally focus on ownership or access to particular financial products and services. The focus narrows down mainly to the products and services provided by the mainstream financial service providers. Such financial products may include money transmission, home insurance, short and long-term credit and savings. The review of literature suggests that the most operational definitions are context-specific, originating from country-specific problems of financial exclusion and socio-economic conditions. The operational definition of financial inclusion, based on the access to financial products or services, also underscores the role of financial institutions or service providers involved in the process (Rabha, 2012).

The scope of financial inclusion (Rabha, 2012) can be expanded in two ways-

(a) Through state driven intervention by way of statutory enactments, and

(b) Through voluntary effort by the banking community itself for evolving various strategies to bring within the ambit of the banking sector the large strata of society. When banks do not give desired attention to certain areas, the regulators have to step into remedy the situation. This is the reason why the Reserve Bank of India (RBI) is placing a lot of emphasis on financial inclusion.

Indian Approach to Financial Inclusion

Broadly, the policy approach adapted to financial inclusion in India can be divided in two categories - the minimalist approach and the expanded approach : (a) The minimalist approach for financial inclusion focuses on the provision of a bouquet of basic financial products and services; whereas, (b) The expanded approach for financial inclusion focuses not only on the provision of the basic banking products

but also other important ancillary financial products, which would also entail focus on consumer protection and education, particularly financial literacy for the new entrants to the formal financial system (Khan, 2012).

Importance of Financial Inclusion

In majority of the developing countries, access to finance (Khan, 2012) is now being perceived as a public good, which is as important and basic as access, say, to safe water or primary education. A question that arises is whether financial inclusion can be interpreted as a public good. A good is considered a public good if it meets the conditions of (a) 'non-rivalness' in consumption and (b) non-excludability. Financial inclusion meets these two criteria. One of the important effects of financial inclusion is that the entire national financial system benefits by greater inclusion, especially when promoted in the wider context of economic inclusion.

Financial Inclusion: India's Position Compared with other Countries

The extent of financial exclusion in India is (Khan, 2012) found to be higher as compared with many developed and some of the major emerging economies. The wide extent of financial exclusion in India is visible in the form of high population per bank branch and low proportion of the population having access to basic financial services like savings accounts, credit facilities, and credit and debit cards. State wise percentage of households (GoI-FM, 2012), availing Banking Services in 2011 (vide Table II), clearly show that there still remain a large number of households which do not avail banking services, resulting to financial exclusion.

Table II
State wise Percentage of Households availing Banking Services in 2011

Sr. No.	*India/State/Union Territory #*	*Percentage of Households availing Banking services*
1.	A & N Islands	89.3
2.	Andhra Pradesh	53.1
3.	Arunachal Pradesh	53.0
4.	Assam	44.1
5.	Bihar	44.4
6.	Chandigarh	80.1
7.	Chhattisgarh	48.8
8.	Dadra & Nagar Haveli	56.7
9.	Daman & Diu	65.4
10.	Delhi	77.7
11.	Goa	86.8
12.	Gujarat	57.9
13.	Haryana	68.1
14.	Himachal Pradesh	89.1
15.	Jammu & Kashmir	70.0

contd. table

Sr. No.	*India/State/Union Territory #*	*Percentage of Households availing Banking services*
16.	Jharkhand	54.0
17.	Karnataka	61.1
18.	Kerala	74.2
19.	Lakshadweep	85.3
20.	Madhya Pradesh	46.6
21.	Maharashtra	68.9
22.	Manipur	29.6
23.	Meghalaya	37.5
24.	Mizoram	54.9
25.	Nagaland	34.9
26.	Odisha	45.0
27.	Puducherry	64.0
28.	Punjab	65.2
29.	Rajasthan	68.0
30.	Sikkim	67.5
31.	Tamil Nadu	52.5
32.	Tripura	79.2
33.	Uttar Pradesh	72.0
34.	Uttarkhand	80.7
35.	West Bengal	48.8
	All India	58.7

Source: Census of India 2011, (GoI-FM, 2012).

The following table summarizes India's performance in the area of financial inclusion as compared with other developing as well as developed countries (vide Table III).

Table III

Country	*No.of branches (per 1 lakh adults)*	*No. of ATMs*	*Bank credit (as % of GDP)*	*Bank deposits*
India	10.91	5.44	43.62*	60.11*
Austria*	11.81	48.16	35.26	32.57
Brazil	13.76	120.62	29.04	47.51
France	43.11	110.07	56.03	39.15
Mexico	15.22	47.28	16.19	20.91
UK*	25.51	64.58	467.97	427.49
United States	35.74	173.75*	46.04	53.14
Korea	18.63	250.29*	84.17	74.51
Afghanistan	2.25	0.50	11.95	21.4
Philippines	7.69	14.88	27.57	53.02

Source: World Bank, Financial Access Survey, (2) Indian Exps 27-7-2012, (3) Khan, (2012)

Notes: (1) Data given in the Table pertains to 2010. However, for rows/cells indicated as* Data pertains to 2009. (2) As at end of 2010-11, [a] the number of ATMS per 1 lakh population stood at 6.3, [b] Bank Credit and Bank Deposit as a percentage of GDP stood at 50.10% and 66.10% respectively.

Measuring Financial Inclusion

The Rangarajan Committee (2008) has defined Financial Inclusion as -

> "Financial Inclusion is 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."

One of the measures of the level of financial inclusion is the Financial Inclusion Index (Sarma, 2008). This index is based on, three basic dimensions of an inclusive financial system:- (i) Banking penetration, (**D1**); (ii) Availability of the banking services (**D2**), and (iii) Usage of the banking system (**D3**).

(a) The first parameter (D1), - 'Banking penetration' - is definitely the most critical parameter for measuring the depth financial inclusion and is measured as a ratio of bank accounts to the total population.

(b) The second parameter (D2), - 'Availability of banking services',- provides an indication to the number of bank outlets available per 1000 people to deliver financial services. The bank outlets may include the brick and mortar branches, ATMs, business correspondents, etc.

(c) The third parameter (D3) seeks to determine the 'Usage of banking services' going beyond mere opening of accounts. Therefore, this is evaluated on the basis of outstanding deposits and credits. Accordingly, the volume of outstanding deposit and credit as proportion on the net district domestic product is used for measuring this dimension.

According to the value of the index, Indian States can be classified into three categories, (Table IV) i.e.,

[A] States having HIGH extent of financial exclusion.

[B] States having MEDIUM extent of financial exclusion.

[C] States having LOW extent of financial exclusion.

According to the empirical results, (vide the above Table IV) :

(a) Kerala, Maharashtra and Karnataka are some of the States having wider (high) extent of financial inclusion as compared to other States of India.

(b) Tamil Nadu, Punjab, Andhra Pradesh, Himachal Pradesh, Sikkim and Haryana fall under the category of medium financial exclusion.

(c) The extent of financial exclusion is found to be significantly low in North-Eastern and Eastern States, i.e., Assam, Nagaland, Manipur, Odisha, Bihar, West Bengal, etc.

The afore-stated analysis implies that all the States, except three categorized as/under HFI have to go a long way in achieving financial inclusion.

Table IV
State-wise Index of Financial Inclusion (IFI) based on Select indicators of Financial Inclusion: Cross Country Analysis

State	*D1 (Penetration)*	*D2 (Availability)*	*D3 (Usage)*	*IFI (Index of FI)*	*IFI Rank*
High Financial Inclusion (0.5-1)					
Kerala	0.70	0.81	0.28	0.54	1
Maharashtra	0.62	0.29	1	0.53	2
Karnataka	0.72	0.47	0.46	0.53	3
Medium Financial Inclusion (0.3-0.5)					
Tamil Nadu	0.70	0.43	0.38	0.48	4
Punjab	0.45	0.69	0.29	0.45	5
Andhra Pradesh	0.56	0.30	0.41	0.41	6
All-India	0.27	0.22	0.55	0.33	7
Himachal Pradesh	0.42	0.40	0.18	0.33	8
Sikkim	0.28	0.33	0.34	0.32	9
Haryana	0.39	0.50	0.12	0.32	10
Low Financial Inclusion (<0.3)					
West Bengal	0.24	0.38	0.23	0.28	11
Gujarat	0.32	0.30	0.16	0.26	12
Uttar Pradesh	0.28	0.31	0.15	0.24	13
Meghalaya	0.21	0.28	0.14	0.21	14
Tripura	0.31	0.22	0.08	0.20	15
Orissa	0.26	0.23	0.11	0.20	16
Rajasthan	0.25	0.22	0.12	0.19	17
Arunachal Pradesh	0.20	0.16	0.14	0.17	18
Mizoram	0.13	0.26	0.09	0.16	19
Madhya Pradesh	0.18	0.21	0.08	0.16	20
Bihar	0.15	0.24	0.08	0.15	21
Assam	0.17	0.17	0.07	0.13	22
Nagaland	0.03	0.04	0.07	0.05	23
Manipur	0.00	0.01	0.01	0.01	24

Source: RBI Working Paper (Chattopadhyay, 2011)

Financial Inclusion and Inclusive Growth: What the Empirical Evidence Suggests?

Inclusive growth as a strategy of economic development has received renewed attention in recent years owing to rising concerns that the benefits of economic growth have not been equitably shared. Growth is inclusive when there is equality of economic opportunities.

Financial inclusion makes growth broad based and sustainable by progressively encompassing the hitherto excluded population. Financial inclusion is no longer a policy choice but a policy compulsion (RBI, 2011b). Empirical evidence shows that countries with large proportion of population excluded from the formal financial system also show higher poverty ratios and higher inequality. The inclusive growth

country analytics has a distinct character focusing on the pace and pattern of growth. Rapid pace of growth is unquestionably necessary for substantial poverty reduction, but for this growth to be sustainable in the long run, it should be broad-based across sectors, and include a large part of the country's labour force. This analytics of inclusive growth implies a direct link between the macro and micro determinants of growth. Some of the important factors determining the level of financial inclusion in a country are per capita GDP, income inequality, adult literacy and urbanization. Further, physical and electronic connectivity and information availability such as telephone and internet usage also play positive role in enhancing financial inclusion.

The empirical findings strengthen the argument that financial exclusion is indeed a reflection of social exclusion, as countries having low GDP per capita, relatively higher levels of income inequality, low rates of literacy, low urbanization and poor connectivity appear to be less financially inclusive. Financial inclusion, therefore, assumes importance as a policy objective (RBI, 2011b).

All Banks in the Country were advised by RBI, since November 2005, to take all measures and adopt suitable strategies. One element of the strategy enumerated, to achieve the desired target of Financial Inclusion, is through - (a) No-frills accounts, (b) diluted Know-Your-Customer (KYC) norms, (c) Banking Correspondents (BCs) and (d) use of Information Technology. Accordingly, all Public Sector Banks (PSBs), Private Banks (PBs), Cooperative Banks (CBs), undertook the mandated task, willingly or unwillingly, either in a phased manner or otherwise. They either started opening their branches at the suitable villages or appointed their bank correspondents or adopted outsourcing method.

The progress of financial inclusion plans in India as on March 31, 2012 is depicted in the Table V, [vide next page]

Table V
Progress of Financial Inclusion Plan in India
(as on March 31, 2012)

Banking outlets	
Rural branches	24701
BC outlets	120355
Other modes	2478
Total	**147534**
Total number of 'No frill accounts'	**103.21 million**
	(increase of 39.6%)
Operations in NFA (2011-12)	
Outstanding balance	Rs. 932.89 billion
Overdrafts	Rs. 3.39 billion
Transactions through ICT based BC outlets (2011-12)	119.77 million
KCC credit	Rs. 2.15 million
GCC credit	Rs. 0.22 million

Source: Khan (2012)

IV. MAJOR ISSUES, CHALLENGES & STRATEGIES IN FINANCIAL CHALLENGES

There are several issues, challenges and strategies to achieve the target of complete financial inclusion; however, for restricting to the theme of the paper and space constraints, only major issues, challenges *vis-à-vis* strategies have been dealt with.

1. **Change in the approach of Banks: Only access to credit or banking is NOT the financial inclusion: Achieving complete Financial Inclusion:** It is often noticed that mere opening a Bank Account is taken or claimed as achieving the target of financial-inclusion. Many empirical studies and Usage Analysis reveal that after opening such bank accounts, hardly there are any transactions take place in such bank accounts. Banks must genuinely strive to provide the directed services under the category or scheme of financial inclusion to the rural population, since they are the main pillars for the desired success. On this backdrop, the claims of policy-makers, banks, etc., the illusions created and mythical success stories spread must be tested on the basis of parameters enumerated on the background of the RBI's norms and expectations, (NABARD, 2012). Basically, though, the financial inclusion is meant to include all the sections of the society, who are mainly out of the net of the financial institutions, (Chattopadhyay, 2011), yet, financial inclusion does not mean merely opening of saving bank account but signifies creation of awareness about the financial products, education and advice on money management, offering debt counseling, etc. by banks. Every society should ensure easy access to public goods, (Seth, 2011). Therefore, banking service being a public good should also be aimed at providing service to the entire population. However, empirical studies show that :

   (a) Some banks have no desire to achieve the complete financial inclusion;

   (b) Some banks have formed opinion that the complete financial inclusion is not possible and/or it is an empty and useless exercise;

   (c) The Banks are ready or eager, but their branch employees are reluctant or give lame excuses to implement the scheme of financial inclusion.

   (d) Those who, unwillingly and reluctantly implement the scheme of achieving financial inclusion, assume that merely opening a bank account is the implementation of scheme of financial inclusion.

   (e) Affordable credits are made available only as compulsions.

   (f) Only in rare cases some of the banks make attempts to provide financial advice to the poor or disadvantaged people.

   (g) The costs of serving the poor can be significant in the short-term, thereby, impacting profitability.

This attitude or mindset reflects a very narrow approach to tackling the problem of financial inclusion. Bankers should, therefore, change their mindsets, view

financial inclusion as a viable business proposition and adopt innovative methods and low-cost delivery models to reach out to the poor. They should study the different markets across India thoroughly and offer region-wise customized products and services riding on the higher levels of trust enjoyed by them over the other financial service providers in rural India. It was in the context of financial inclusion of the excluded and to facilitate the electronic benefit transfer that banks were directed (GoI-FM, 2012), to ensure opening of one bank account per family. In order to accomplish the objective and to have proper monitoring of the progress various modalities have been suggested. One of the vital obligatory modalities is regarding opening of one bank account per family. The Finance Ministry's recent (May 15, 2012) directives regarding opening of one bank account per family to facilitate electronic benefit transfer and financial inclusion, (GoI-FM, 2012), mandate the banks that families must have one account in a bank on Core banking Solution and having NEFT facility.

The statistics given in these directives depict that:

(a) Nearly 10 crore households were not availing banking services.

(b) As per 2011 census, about 58.7% households, comprising of 54.4% rural households and 67.8% urban households, had reported availing banking facilities.

(c) Out of the 24.69 crore households, 14.48 crore households reported availing banking services.

(d) Under *Swabhimaan*, over 3.25 crore bank accounts in rural areas have been opened.

2. **Relaxation in Regulatory Framework:** The RBI, initially, in November 2005, set the population benchmark, which will help it, for taking its financial inclusion drive to the next level, mandating all Banks to reach out the villages, all habitations with population in excess of 2000, as per the 2001 census, either through the Bank Branches or through Business Correspondent (BCs). However, since 2011-12, the population benchmark is reduced to 1600 and above. Very recently, on 11 August 2012, the RBI asked Banks to drop the 'no-frills' tag from the basic savings accounts as the nomenclature has become a stigma. The RBI asked Banks to provide the 'zero-balance' facility in the basic banking accounts along with ATM-cum-Debit Cards without extra charge. The Finance Ministry directed the Banks were directed to reach out to villages with population of 2000, as the population benchmark that all habitations with population in excess of 1600 must have a bank branch, which will help it take its financial inclusion drive to the next level. The Finance Ministry, very recently, directed all state-run Banks to ensure that every household has at least one savings bank account by end of June 2012, a move seen as a precursor to direct transfer of benefits under the government's financial inclusion plan. For this purpose, the Banks

have been asked to launch a campaign to ensure that opening of new accounts and changes required in existing accounts are completed by June 2012, (Khan, 2011).

3. **Self Help Group-Bank Linkage Programme (SLBP):** In the last two decades, the major institutional innovation in India for expanding financial system access and usage for the poor and marginalized sections of the population has been the SBLP. The project provided a cost-effective SBLP model for providing financial services to the underserved poor. Being a 'savings-first, credit later' model, credit discipline became a norm for Self Help Groups (SHGs) and 'social collateral' made them bankable. The model was initially successful in providing solution to the twin problems faced by banks, i.e., low recovery of loans in rural areas and high transaction costs in dealing with small borrowers at frequent intervals, with a major positive impact of generating social and economic empowerment of the membership. However, despite the noteworthy accomplishments of SHGs certain issues, such as, inadequate outreach in many regions, delays in opening of SHG accounts and disbursement of loans, impounding of savings by banks as collateral, non-approval of repeat loans by banks even when the first loan was repaid promptly, multiple membership, borrowings by SHG members within and outside SHGs, adverse consequences of unhealthy competition between NGO promoted SHGs and Government promoted/subsidy oriented SHGs and limited banker interface and monitoring continued to affect the programme in many areas. While the basic tenets of the SHGs being savings led credit product remain true even today, recent developments have given rise to the need for crucial changes in the approach and design of SBLP to make it more flexible and client friendly. The revised NABARD guidelines, popularly known as SHG2 (version 2), have sought to address some of the shortcomings of the earlier version, (Khan, 2011).

4. **Microfinance Institutions (MFIs):** The MFIs have served the underserved/ unserved populace in the last few years and improved access to credit though there have been quite a few debatable issues on the style of corporate governance and ethics of conducting business on part of some of the MFIs. However, it has been often realized that the MFIs do help in financial deepening and can remain an important segment of the Indian financial market keeping in view the present level of penetration of the banking system. The conceptual framework underlying MFIs requires a change. MFIs will have to revisit the mission and business strategy and reinvent the sector to remain relevant in the system. A new category of 'Non Banking Financial Company-Micro Finance Institutions' (NBFC-MFIs) prescribed by the Malegam Committee (2011), created in December 2011 by RBI, is also facing difficulties primarily into micro financing. The NBFC-MFIs has got some relief from the RBI, which issued revised 'Directions cum Modifications' in August 2012, (RBI, 2012). On this background,

these institutions have to revisit their business models to support the income earning ability of the borrowers and, at the same time, they remain economically viable. NBFC-MFIs will have to work hard in pursuit of transparency and responsible finance, shaking off the perception that their motto is profiteering at the cost of the poor but not profitability for sustainable and viable growth on one hand and take initiatives to retool the product redesign for garnering new customers and acquiring more share of the market on the other (Khan, 2011).

5. **Business Facilitators (BFs)/Business Correspondents (BCs):** The ICT based agent bank model through BFs/BCs for ensuring door step delivery of financial products and services, prescribed by the RBI to act as intermediaries for providing financial and banking services and ultimately addressing the proverbial last mile problem, initially created by the banks themselves, and later improvised by number of innovations, bridging the connectivity gap between the service seekers, i.e., under-served populace, and the service providers, i.e., the banks, have, however, raised a number of issues both for the partner banks and also for the regulators. Viability of the BFs/BCs model in general has remained a critical issue for which the model has not taken off as expected. Further, banks and their BFs/BCs also exposed to huge risk of cash management, particularly as cash dependence of the economy continues to be very high. There is also huge requirement of hand-holding and training of the BFs/BCs to enhance the trust level of the end customers. In this context, the current thinking of having lean, brick and mortar outfits of the banks (e.g. ultra small branches) to provide support to and supervise work of certain number of BFs/BCs appears to be a step in right direction. The success of BFs/BCs model also hinges on adoption of technology, which in turn, is dependent on the degree of compatibility and integration of technology being used by the banks and their BFs/BCs. There is a view that banks could also have their in-house BF/BC outfits in the form of separate trusts/subsidiaries with separate recruitment and remuneration structure but under closer supervisory control.

6. **Product Initiatives:** To ensure that more and more people come within the banking fold the banks should offer all the customers a 'basic savings deposit account' with certain minimum common facilities and without the requirement of minimum balance. The services provided in this account should include deposit and withdrawal of cash at the bank branches as well as ATMs, receipt/credit of money through electronic payment channels or by means of deposit/collection of cheques drawn by Central/State Government agencies and departments. Innovation of products for the specific needs of the poor is necessary for achieving the ultimate objective of inclusive growth (Khan, 2012).

7. **Mobile Banking:** With the rapid growth in the number of mobile phone subscribers in India, banks in collaboration with telecom companies are seeking to develop an alternate channel of delivery of banking services. Keeping in

view the issues relating to diversity of network providers in India, remittance centric approach of such model and Know Your Customer (KYC) related concerns, the RBI has advocated bank-led mobile banking model and issued operative guidelines to banks for effecting mobile-based banking transactions. The empirical studies indicate that banks are yet to fully exploit this technology even for their existing customers. The banks and the mobile operators reach a workable understanding while protecting their mutual interests. Such an approach would result in a 'win-win' situation for both and, more importantly, serve the larger cause of public good of financial inclusion (Khan, 2012).

8. **Aadhaar-enabled Payment Systems (AEPS):** The AEPS having the ability to service customers of many banks based on the unique biometric identification data stored in the Aadhaar database is expected to empower a bank customer to use Aadhaar as his/her identity to access the respective Aadhaar enabled bank account and perform basic banking transactions like balance enquiry, cash withdrawal and deposit through the BC. A pilot scheme in four districts of Jharkhand state is currently being carried out under which MGNREGA wages to labourers are credited to their Aadhaar enabled bank accounts.
9. **Innovative product lines & processes:** Banks have to look at their policies and procedures to develop new product lines rather than merely adopting the complex products of urban India in the rural milieu.
10. **Financial literacy and awareness:** There is a strong concern about the pathetic attitude of the banks to arrange regular campaigns for spreading awareness about financial inclusion and financial literacy need to be intensified. Banks need to do efforts in this area through innovative dissemination channels including films, documentaries, pamphlets and road shows.
11. **Customer service and consumer protection:** Customer service is another issue that needs closer attention. Mind-set, cultural and attitudinal changes at the grass-root levels and user friendly technology at the level of branches of banks and BC outlets are needed to extend holistic customer service to the new entrants to the banking system. Government, regulators like Reserve Bank of India, banks, service providers and consumers themselves have to play important role in developing a comprehensive approach to consumer protection (Khan, 2012).
12. **Issues and Challenges in ICT based Financial Services: Tapping Technology Platforms:** Banks need to make significant investments in Technology based applications, related research and development efforts, comprehensive Management Information Service (MIS) and monitoring and evaluation systems on one hand and **collaborate** with technology service providers (TSPs), mobile network operators (MNOs), corporate houses and various categories of BCs to develop efficient delivery models with a strategy aiming to create a facilitating eco-system, leveraging on technology and promote partnerships of brick and

mortar branches including ultra-small branches with the ICT-based BC outlets for evolving an effective financial inclusion delivery mechanism. Today, banks can provide a bouquet of financial services through the various networks of agents and branches by leveraging and fine tuning technology platforms. Technology holds the key to providing models for efficient delivery of small value transactions in large volumes while reaping economies of scale. The implementation of such effective, scalable and platform-independent technology will help drive down the cost of providing banking services to the poor. Further, technology helps in spreading financial literacy both as a delivery channel and as an intrinsic part of the learning process (e.g., instructional computer). Today, both the service providers and service seekers have a number of technology options, such as, smart cards, micro-ATMs, ATMs, mobile technology, Aadhaar Enabled Payment Systems (AEPS), etc. to choose from to provide/seek financial services irrespective of their geographic locations. For the success of the ICT-based models, resolving technology related issues is the key.

13. **Financial Inclusion as a Business Opportunity *vis-à-vis* Profitable Models for Financial Inclusion:** Financial inclusion initiatives would provide banks with a low-cost and stable source of funds, helping them improve their asset-liability management (ALM). Rural India presents a remarkable opportunity for banks and financial institutions to seek their fortunes and bring prosperity to the aspiring poor through financial inclusion. In a fast growing economy like India the poor are the middle class of tomorrow and banks could, therefore, ill-afford to ignore this segment. Banks, however, argue that while the benefits of financial inclusion can be easily understood, the costs of serving the poor can be significant in the short-term, thereby impacting profitability. Banks, therefore, need to take bold decisions and reach out to rural India with strategies and business models which are beyond the realm of conventional thinking. Banks should refrain from deliberately adopting a uniform business model. Banks need to build its own strategy in line with its business model and comparative advantage. A successful model should also represent a better way than existing alternatives and also answer management guru Peter Drucker's age-old questions: (a) Who is your customer? (b) What does the customer value? & (c) How do you deliver value at an appropriate cost? A (Ramon, 2011) profitable business model should consist of four elements: • a customer value proposition • a profit formula • key resources • key processes.

    Profitable models for financial inclusion could, therefore, have the following features* *(*Note: These are concluding compilation of various options guided/suggested on this theme to the banks by various authorities, viz., RBI-2008, RBI-2011a, RBI-2011b, RBI-2011c, RBI-2011d, NABARD-2012; and also by various experts and authors on this theme, including : Chaia et al.-2010, Khan-2011, Karmakar-2011, Nadkarni-2012, Nair-2012, Rabha, 2012, Raj-2011, Ramon-2011)***:**

(a) Offering a clear customer proposition and customized bouquet of products**:-** To succeed in their financial inclusion initiatives, banks would need to offer customers a clear proposition and a customized bouquet of product offerings. Banks need to offer the following services at a minimum costs and charges, as part of an overall **'package'** to attract customers:

- Advice on monetary issues, problems, needs and plans
- Savings cum Overdraft account;
- Remittance-products;
- Kisan Credit Card/General Credit Card
- Disbursements of Grants & Financial Assistance awarded by & in accordance with the Central Govt., State Govt., Local authorities, other Funding agencies, NGOs, etc.;
- Micro-Credits as per Bank's own schemes;
- Govt. directed Priority sectoral lending
- Entrepreneurial Credit
- Micro-Insurance.

-Each of these offer significant value to customer and enable banks to generate value through transaction fees.

(b) Scalable business model with simple, user friendly low-cost technologies:- Profitable business models, (Raj, 2011) would need to be scalable and incorporate simple, user-friendly and low-cost technologies so that investments would be recouped and profits begin showing up as the number of people serviced by a particular branch or outlet increases over time.

(c) Collaborate with local agents and for-profit companies:- According to consulting giant (Raj, 2010 from Chaia *et al.*, 2010), the basic problem of 'last mile access' can be solved if banks can team up with retail outlets (business correspondents) in low-income, often hard-to-reach areas to offer financial services to rural masses, thereby, creating value both for themselves and their customers.

(d) Banks need to learn from both corporate India and the informal sector:- Banks need to innovate and improve service levels in order to provide the same level of accessibility as the local money lender, friend or relative and open branches/banking outlets in villages as inclusive banking goes beyond the conventional notions of commercial banking.

(e) Subsidiary model to drive down costs**:-** Indian banks should explore the subsidiary route to drive down distribution costs in their financial inclusion drive.

(f) Strategy to gain benefits from Government scheme of MGNREGA :-, Banks need to mould their strategies to gain benefits amendments made in August

2011 making mandatory under the law for state governments to ensure that every beneficiary of the MGNREGA scheme has a bank/post office account and the disbursements are made exclusively through these channels, which provide opportunities to the banks and positively benefit financial inclusion initiatives.

(g) Innovate and test-market pilot products/services:- Banks need to keep their MIS updated and keep ground realities in mind while designing their products/services for the poor. McKinsey's report (2010) also suggests that financial service providers should test-market low-cost pilots to see which products/services are found acceptable before large-scale introduction.

VII. CONCLUSION

The problem of financial exclusion needs to be tackled with urgency if we want our country to grow in an equitable and sustainable manner. Traditional and conventional banking solutions may not be the answer to address the problem of financial inclusion in India. Banks, therefore, need to innovate and think 'out-of-the-box' for solutions to overcome the problem of financial exclusion in India. They need to deploy new technologies and create financially viable models to take forward the process of financial inclusion in an effective manner. This way banks in India would be doing a great service to the cause of financial inclusion and make their name in history. Financial inclusion may be a social responsibility for the banks in the short-run but will turn out to be a business opportunity in the long-term. Financial Inclusion is no longer an option, but it is a compulsion. The entire world is looking at this experiment in India and it is important that banks rise up to this challenge and meet it successfully. The current policy objective of inclusive growth with financial stability cannot be achieved without ensuring universal financial inclusion. Pursuit of financial inclusion by adoption of innovative products and processes does, however, pose challenge of managing trade-offs between the objective of financial inclusion and financial stability. In the Indian context, the Reserve Bank has always sought to balance the risk of partnerships and product innovations with the ability to achieve greater penetration in a safe, secured and prudentially sound manner. The underlying belief is that only sound and strong institutions can promote financial inclusion in a sustainable manner and, towards this end, prudent regulations have to be in place to achieve inclusion while protecting financial stability and consumer interest. By adopting appropriate regulatory framework for innovations in policies, partnerships, processes and products meant for financial inclusion, the Reserve Bank has sought to further the cause of inclusion without falling short of the policy goal of financial stability. The stakeholders have come to realize the need for viable and sustainable business models which focus on accessible and affordable financial services, products and processes, synergistic partnerships with non-bank entities including the technology

service providers for efficient handling of low value, large volume transactions, particularly in remote, banking shadow areas and appropriate regulatory and risk management policies that ensure financial inclusion and financial stability move in tandem.

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