*Financial Inclusion in India: Journey so far and way forward**

K. C. Chakrabarty

Mr. M Narendra, Chairman, Indian Overseas Bank; Mr. Y M Deosthalee, CMD, L&T Finance; Mr. Arun Tiwari, ED, Allahabad Bank; Ms. Shereen Bhan, Managing Editor, CNBC-TV18, delegates to the conclave; friends from the media fraternity; ladies and gentlemen! It is a pleasure for me to be present here today at the Conclave organised by CNBC TV 18 on the very topical subject of financial inclusion. I am particularly happy that a business news channel which has built up a credible reputation for its reportage and analysis of the financial markets is taking this initiative to lend its voice to the needs and expectations of the unbanked and excluded, yet silent mass of our population. Considering the power of the media and its unique ability to influence public opinion and generate awareness, there is immense potential for initiatives such as this to galvanise financial inclusion efforts in India. I heartily congratulate CNBC TV 18 for this creditable endeavor and hope that this is the first in a series of many such initiatives in the days to come.

Introduction

2. Poverty and exclusion continue to dominate socio-economic and political discourse in India as they have done over the last six decades in the post-independence period. Poverty reduction has been an important goal of development policy since the inception of planning in India. Various anti-poverty, employment generation and basic services programmes have been in operation for decades in India. The ongoing reforms attach great importance to removal of poverty and to addressing the wide variations across states and the rural-urban divide. Though the Indian economy recorded impressive growth rates until recently, its impact has sadly not fully percolated to the lowest deciles. Despite being one of the ten fastest growing economies of the world, India is still home to one-third of the world's poor. Further analysis shows that poverty is getting concentrated continuously in the poorer states.

3. In developing economies like ours, the banks, as mobilisers of savings and allocators of credit for production and investment, have a very critical role. As a financial intermediary, the banks contribute to the economic growth of the country by identifying the entrepreneurs with the best chances of successfully initiating new commercial activities and allocating credit to them. At a minimum, all retail commercial banks also provide remittance facilities and other payment related products. Thus, inherently, the banking sector possesses a tremendous potential to act as an agent of change and ensure redistribution of wealth in the society.

4. However, it is disheartening to note that the number of people with access to the products and services offered by the banking system continues to be very limited even years after introduction of inclusive banking initiatives in the country through measures such as the cooperative movement, nationalisation of banks, creation of regional rural banks, *etc.* As Nobel Laureate Prof. Amartya Sen has also noted, "the thrust of developmental policy in India has undergone a paradigm shift from an exclusive focus on efficiency to one on equity; from the rate and pattern of growth, and on inequalities, distribution of income and wealth to the extent to which people are deprived of the requirements for leading a fulfilling life and suffer 'capability deprivation'. Over the past five years, the Reserve Bank of India, as also other policy makers have resolutely pursed the agenda of financial inclusion and achieved discernible progress

---

* Keynote address delivered by Dr. K. C. Chakrabarty, Deputy Governor, Reserve Bank of India at the Finance Inclusion Conclave organised by CNBC TV 18 at New Delhi on September 6, 2013. Assistance provided by Ms. Sushma Vij and Ms. Mruga Paranjape is gratefully acknowledged.

in improving access to financial services for the masses. However, the progress is far from satisfactory as evidenced by the World Bank Findex Survey (2012). According to the survey findings, only 35 per cent of Indian adults had access to a formal bank account and 8 per cent borrowed formally in the last 12 months. Only 2 per cent of adults used an account to receive money from a family member living in another area and 4 per cent used an account to receive payment from the Government. The miniscule numbers suggest a crying need for a further push to the financial inclusion agenda to ensure that the people at the bottom of the pyramid join the formal financial system, reap benefits and improve their financial well-being.

5. The importance of financial inclusion has been emphatically underlined in the wake of the financial crisis. As we all know, the crisis has had a significant negative impact on lives of individuals globally. Millions of people have lost their livelihoods, their homes and savings. One of the prominent reasons for the crisis was that the financial system was focused on furthering its own interests and lost its linkage to the real sector and with the society at large. The crisis also resulted in a realisation that free market forces do not always result in greater efficiency in the financial system, particularly while protecting the interests of the vulnerable sections of society. This is due to the information asymmetry working against these sections, thereby placing them at a severe disadvantage. In wake of the crisis, therefore, Financial Inclusion has emerged as a policy imperative for inclusive growth in several countries across the globe. However, though much lip service has been paid to Financial Inclusion, the actual progress has remained far from satisfactory. As I always mention, it is regrettable that the entire debate surrounding financial inclusion has generated significant heat and sound, but little light.

6. In my address today, I intend to recount some of the measures taken by the Reserve Bank of India, dwell on progress achieved and also highlight the way forward in conquering the challenges that hinder our quest for universal financial inclusion in the country.

Objectives of Financial Inclusion

7. Let me begin with what we in the RBI seek to achieve as part of our financial inclusion drive. We have defined Financial Inclusion as the *"process of ensuring access to appropriate financial products and services needed by all sections of the society in general and vulnerable groups such as weaker sections and low income groups in particular, at an affordable cost in a fair and transparent manner by regulated, mainstream institutional players".* We consider Financial Inclusion and Financial Literacy as twin pillars where Financial Inclusion acts on the supply side *i.e.,* for creating access and financial literacy acts from the demand side *i.e.,* creating a demand for the financial products and services.

8. Unrestrained access to public goods and services is the *sine qua non* of an open and efficient society. Banking services are essentially for welfare of the public. It is imperative, therefore, that the availability of banking and payment services to the entire populace without discrimination is the avowed objective of public policy. In our considered view, providing access to basic banking services is the first phase of the financial inclusion process. We are also convinced that only the mainstream, regulated financial players are capable of bringing about meaningful financial inclusion as they have the ability to make the necessary investment in the build up phase and also cross-subsidise the services in the initial stages till they become self-sustaining. Our focus on banks as the principal vehicle for financial inclusion also stems from the fact that only they can offer the entire suite of products that would facilitate meaningful financial inclusion.

9. Let me now turn to how Financial Inclusion can help the society and the economy. Financial Inclusion

has the ability to generate positive externalities: it leads to increase in savings, investment and thereby, spurs the processes of economic growth. It also provides a platform for inculcating the habit of saving money, especially amongst the lower income category that has been living under the constant shadow of financial duress, mainly because of absence of savings, which makes them a vulnerable lot. Presence of banking services and products aims to provide a critical tool to inculcate the savings habit. It also creates avenues of formal credit to the unbanked population who are otherwise dependent on informal channels of credit like family, friends and moneylenders. Availability of timely, adequate and transparent credit from formal banking channels will allow the entrepreneurial spirit of the masses to increase outputs and prosperity in the countryside. It will open the doors of formal remittance facilities to the low income and unbanked populace who, presently, are forced to use all kinds of informal and costly ways of sending money from one place to another. As we all know, Financial Inclusion has now been viewed as a remedy to plug gaps and leaks in distribution of government benefits and subsidies through direct benefit transfers to beneficiaries' bank accounts rather than through subsidising products and making cash payments. Thus, on the whole, Financial Inclusion has the potential to bring in the unbanked masses into the formal banking system, channelise their savings, stoke their entrepreneurial ambitions by making available credit and thus give a fillip to the economy.

Approach to Financial Inclusion

10. Let me now turn to the RBI's approach towards Financial Inclusion. We have adopted a structured, planned and integrated approach towards financial inclusion (FI) by focusing on both the demand and supply side constraints. Some of the defining features of our approach to FI are:

- We have adopted a bank-led model for FI, but have permitted non-bank entities to partner banks in their FI initiatives.
- As a philosophy, we have always encouraged banks to pursue FI as a commercial activity and to not view it as social service or charity. The self-sustainability and commercial viability of the FI initiatives are important if banks have to scale up their operations to cover more unbanked areas.
- We have encouraged banks to leverage technology to attain greater reach and penetration while keeping the cost of providing financial services to the minimum. While we remain technology neutral, we require banks to seamlessly integrate whatever technology they choose, with their core banking solution (CBS) architecture.
- We have advised banks to adopt innovative business models and delivery channels to expand their FI efforts. There is a need for banks to develop new products and design new delivery models that are customised to the unique needs of the financially excluded population, both in the rural and urban areas.
- Considering that financial Literacy is an important adjunct for promoting financial inclusion, consumer protection and ultimately financial stability, the RBI has adopted an integrated approach wherein efforts towards Financial Inclusion and Financial Literacy would go hand in hand. Besides the various initiatives taken by the RBI individually to encourage financial literacy, a National Strategy for Financial Education (NSFE) has also been finalised under the aegis of the Financial Stability and Development Council (FSDC) to co-ordinate efforts of various stakeholders involved in this process.
- The Reserve Bank has been playing a supportive role in FI by creating a conducive regulatory environment and providing institutional support to banks in their FI efforts. Importantly, we have provided banks the freedom and the space to determine their own strategies for rolling out FI

and have encouraged them to identify their own goals and targets through their respective Financial Inclusion Plans.

Robust Institutional Mechanism

11. Our strength lies in the fact that we have created a robust institutional mechanism to support the roll out of banking services across the country. This was essential considering the enormity of the task in terms of the number of excluded people and the geographical size of the country.

- India is one country where the FSDC has a specific mandate for financial inclusion and financial literacy. There is a separate Technical Group on Financial Inclusion and Financial Literacy under the aegis of FSDC with representation from all the financial sector regulators.
- In order to spearhead efforts towards greater financial inclusion, the RBI has constituted a Financial Inclusion Advisory Committee (FIAC) under the Chairmanship of a Deputy Governor from the RBI. The FIAC has few Directors from the Central Board of the RBI and experts drawn from NGO sector/other civil society representatives, *etc.* as members. The collective expertise and experience of the members is expected to be leveraged to explore issues such as developing viable and sustainable banking services delivery models focusing on accessible and affordable financial services, developing products and processes for rural as well as urban unbanked consumers.
- At the state level, we have State Level Bankers Committees (SLBC) in all the states. Going further down, we have Lead District Managers in all the 659 districts, with recent inclusion of the metropolitan areas into the Lead Banks Scheme.
- About 700 financial literacy centres have been set up by banks. There are Rural Self-Employment Training Institutes (R-SETI), working towards capacity building for taking up self employment ventures.

RBI's Policy Initiatives to foster Financial Inclusion

12. Let me now turn to some of the supporting policy initiatives that the RBI has taken to further the Financial Inclusion in the country.

(a) Reach

(i) Branch expansion in rural areas

Branch authorisation has been relaxed to the extent that banks do not require prior permission to open branches in centres with population less than 1 lakh, which is subject to reporting. To further step up the opening of branches in rural areas, banks have been mandated to open at least 25 per cent of their new branches in unbanked rural centres.

In the Annual Policy Statement for 2013-14, banks have been advised to consider frontloading (prioritising) the opening of branches in unbanked rural centres over a three year cycle co-terminus with their FIPs. This is expected to facilitate the branch expansion in unbanked rural centres.

(ii) Agent Banking – Business Correspondent/ Business Facilitator Model

In January 2006, the Reserve Bank permitted banks to utilise the services of intermediaries in providing banking services through the use of business facilitators and business correspondents. The BC model allows banks to do 'cash in – cash out' transactions at a location much closer to the rural population, thus addressing the last mile problem.

(iii) Combination of Branch and BC Structure to deliver Financial Inclusion

The idea is to have a combination of physical branch network and BCs for extending financial inclusion, especially in geographically dispersed areas. To ensure increased banking penetration and control over operations of BCs, banks have been advised to establish low cost branches in the form of intermediate brick and mortar structures in rural centres between the present base branch and BC locations, so as to provide support to a cluster of BCs (about 8-10 BCs) at a reasonable distance of about 3-4 kilometers.

(b) Access

Relaxed KYC norms

- Know Your Customer (KYC) requirements have been simplified to such an extent that small accounts can be opened with self certification in the presence of bank officials.
- RBI has allowed 'Aadhaar' to be used as one of the eligible documents for meeting the KYC requirement for opening a bank account.

Roadmap for Banking Services in unbanked Villages

- In the first phase, banks were advised to draw up a roadmap for providing banking services in every village having a population of over 2,000 by March 2010. Banks have successfully met this target and have covered 74,398 unbanked villages.
- In the second phase, Roadmap has been prepared for covering remaining unbanked villages *i.e.* with population less than 2000 in a time bound manner. About 4,90,000 unbanked villages with less than 2000 population across the country have been identified and allotted to various banks. The idea behind allocating villages to banks was to ensure availability of at least one banking outlet in each village.

(c) Products

Bouquet of Financial services

In order to ensure that all the financial needs of the customers are met, we have advised banks to offer a minimum of four basic products, *viz.*,

- A savings cum overdraft account
- A pure savings account, ideally a recurring or variable recurring deposit
- A remittance product to facilitate EBT and other remittances, and
- Entrepreneurial credit products like a General Purpose Credit Card (GCC) or a Kisan Credit Card (KCC)

(d) Transactions

Direct Benefit Transfer

The recent introduction of direct benefit transfer, leveraging the Aadhaar platform, will help facilitate delivery of social welfare benefits by direct credit to the bank accounts of beneficiaries. The government, in future, has plans to route all social security payments through the banking network, using the Aadhaar based platform as a unique identifier of beneficiaries. In order to ensure smooth roll out of the Government's Direct Benefit Transfer (DBT) initiative, banks have been advised to:

- Open accounts of all eligible individuals in camp mode with the support of local Government authorities.
- Seed the existing and new accounts with Aadhaar numbers.
- Put in place an effective mechanism to monitor and review the progress in implementation of DBT.

Financial Inclusion Plan of banks

14. Financial Inclusion Plan 2010-13

We have encouraged banks to adopt a structured and planned approach to financial inclusion with commitment at the highest levels, through preparation of Board approved Financial Inclusion Plans (FIPs). The first phase of FIPs was implemented over the period 2010-2013. The Reserve Bank has sought to use the

FIPs as the basis for FI initiatives at the bank level. RBI has put in place a structured, comprehensive monitoring mechanism for evaluating banks' performance against their FIP plans. Annual review meetings are being held with CMDs of banks to ensure top management support and commitment to the FI process.

What has been achieved so far?

15. A snapshot of the progress made by banks under the FIPs (April 10 – March 13) for key parameters, during the three year period is as under:

- Nearly 2, 68, 000 banking outlets have been set up in villages as on March 2013 as against 67,694 banking outlets in villages in March 2010.
- About 7400 rural branches opened during this period.
- Nearly 109 million Basic Savings Bank Deposit Accounts (BSBDAs) have been added, taking the total no. of BSBDAs to 182 million. Share of ICT based accounts have increased substantially – Percentage of ICT accounts to total BSBDAs has increased from 25 per cent in March 10 to 45 per cent in March 2013.
- With the addition of nearly 9.48 million farm sector households during this period, 33.8 million households have been provided with small entrepreneurial credit as at the end of March 2013.
- With the addition of nearly 2.25 million non farm sector households during this period, 3.6 million households have been provided with small entrepreneurial credit as at the end of March 2013.
- About 4904 lakh transactions have been carried out in ICT based accounts through BCs during the three year period.

16. It is important to analyse this progress against the some disconcerting trends that were noticed in the run up to the structured Financial Inclusion initiatives that the banks launched since 2010 onwards. First, the number of banked centres in the country between 1991 and 2007 had actually come down (from 35,236 to 34,471). Second, the number of rural branches during the same period had also declined significantly (from 35,206 to 30,409). Against this backdrop, the progress made during 2010-13 is certainly remarkable.

Financial Inclusion Plan 2013-16

17. In order to continue with the process of ensuring access to banking services to the excluded, banks have now been advised to draw up a fresh 3 year FIP for the period 2013-16. Banks have also been advised that the FIPs prepared by them are disaggregated and percolated down up to the branch level. The disaggregation of the plans is being done with a view to ensure involvement of bank staff across the hierarchy, in the FI efforts and also to ensure uniformity in the reporting structure under the FIP. The focus is also now more on the volume of transactions in new accounts opened as a part of the financial inclusion drive.

Challenges and Way Forward

18. The current policy objective of inclusive growth with financial stability cannot be achieved without ensuring universal financial inclusion. Our experience suggests that the banks alone will not be able to achieve this unless an entire support system partners them in this mission. Only the support of policymakers, regulators, governments, IT solution providers, media and the public at large can bring about a decisive metamorphosis in our journey towards universal financial inclusion.

19. Financial Inclusion of the unbanked masses is expected to unleash the hugely untapped potential of the sections of the society that constitute the bottom of the pyramid. However, in pursuing the FI mission, the normal banking model has been found wanting in terms of cost, scalability, convenience, reliability,

flexibility and continuity. To ensure that the banks give adequate attention to financial inclusion, they must view this as a viable business proposition rather than as a corporate social responsibility or a regulatory obligation. For the business to remain viable it would be important to focus on increasing usage of existing banking infrastructure which would happen only if the banks can offer an entire bouquet of products and services to the holders of the large number of basic bank accounts opened during the last three years as also to the new customers that the banks acquire.

20. Our past experience and FIP review meetings with the banks have highlighted that if the dream of universal and a meaningful financial inclusion has to be turned into reality, then going forward, we would need to focus on the following issues:

(a) Increasing Reach

- Ensuring coverage of all unbanked villages in next 3 years.
- Emphasis on increasing rural branches.
- Opening of bank accounts for all eligible individuals.

(b) Increasing transactions

- Leveraging on DBT
- Delivery of credit products through BCs
- Hassle free Emergency credit (In built OD)

(c) HR Structure

- Banks to review HR policy in view of FI requirements
- Examining appointing of a separate cadre of staff for cost optimisation

(d) Fine-tuning the BC Model

- Stabilising the BC delivery model
- Encouraging innovations in remittances model
- Review of Cash Management for BC operations

(e) Spreading Financial Literacy

- Implementing National Strategy for Financial Education
- Creating Dedicated Website- Inclusion in School Curriculum
- Organising Financial Literacy Camps

Conclusion

21. While the task before us is daunting, I am sure that a collaborative approach can definitely help in successfully overcoming this challenge. Though we expect the commercial banks to play a significant role in ensuring financial inclusion and promoting financial literacy, I want to emphasise that the banks alone would not be able to achieve this ambitious goal and that other stakeholder groups also need to contribute their mite towards this cause. For banks, the focus has to be on building a sustainable, scalable and cost-efficient business delivery model by leveraging upon technology.

22. I would like to conclude by saying that financial inclusion and inclusive growth are no longer just policy choices, but are policy imperatives, which would determine the long-term financial stability and sustainability of the economic and social order, going forward. We need to ensure that all of us are collectively willing to walk that extra mile to ensure that our fellow countrymen get easy access to the financial system and are able to leverage this access to improve their economic and social well-being. Please remember that the rich would not be able to sleep peacefully if the economic and social divide is allowed to grow any bigger. As I mentioned at the beginning, in view of their reach and coverage, electronic and print media has an important role in not only supporting our financial inclusion mission but in leading the initiative by spreading our message far and wide. Today's event is a glowing testimony to the support being extended by the media to the cause of Financial Inclusion and I

firmly believe that this support would act as a catalyst and further invigorate the efforts being made by the governmental and non-governmental agencies.

23. I once again thank CNBC TV 18 for inviting me to share my thoughts today and do hope that the conclave succeeds in throwing up several new practical ideas and strategies which can be implemented by banks and other financial sector participants to further the objective of Financial Inclusion in the days to come.

Thank you!