CHAPTER II

FINANCIAL INCLUSION –AN OVERVIEW

2.1 Phases of Bank Evolution in India

According to RBI report “evolution of banking in India”\(^\text{12}\) the Indian banking sector has been evolving continuously. The initial phase (up to 1947) was a difficult period for the banking sector. A large number of banks sprang up as there were no entry norms for banks. The Swadeshi Movement during this phase saw the establishment of many Indian banks, most of which continue to operate even now. In this phase, banks failed for many reasons they are the two World Wars and the Great Depression, Most of the small banks were local in character and had low capital base, apart from the global factors, one of the major reason for failures of bank was fraudulent manipulation by directors and managers and inter-connected lending. Partly, in order to address the problem of bank failure, the Reserve Bank was set up in 1935.. However, the Reserve Bank had a limited control over banks and lack of an appropriate regulatory framework posed a problem of effective regulation of small banks. By the end of this phase, the country’s financial requirements were still catered to, in a large measure, by the unorganized sector. The focus of the banking sector was on urban areas and the requirements of agriculture and the rural sector were neglected. Although the co-operative credit movement had a very encouraging beginning, it did not spread as expected despite Government patronage.

The period after independence could be categorized broadly in three phases: (i) 1947 to 1967; (ii) 1967 to 1991-92; and (iii) 1991-92 and beyond.

The banking scenario that prevailed in the early independence phase faced three main issues. Bank failures had raised the concerns regarding the soundness and

\(^{12}\) Evolution of Banking in India (2008), Reserve bank report.
stability of the banking system. There was large concentration of resources from deposits mobilization in a few hands of business families or groups. Banks raised funds and on-lent them largely to their controlling entities. Agriculture was neglected insofar as bank credit was concerned. In order to address the issue of bank failures, the Banking Companies Act (renamed as Banking Regulation Act in March 1966) was enacted in 1949 empowering the Reserve Bank to regulate and supervise the banking sector. The Reserve Bank, therefore, was granted powers in the early 1960s for consolidation, compulsory amalgamation and liquidation of small banks. Although some banks had amalgamated before 1960s, the number of banks amalgamating rose sharply between 1960 and 1966. Another feature that emerges from the evolution of banking till the end of this phase was that despite the existence of small banks, a large segment of the population remained outside the banking system. In other words, the existence of small banks did not necessarily promote financial inclusion. On the eve of independence, the banking system was concentrated primarily in the urban and metropolitan areas. Efforts, therefore, were made to spread banking to rural and unbanked areas, especially through the State Bank of India and through the branch licensing policy. The number of bank branches rose significantly between 1951 and 1967, as a result of which the average population per branch fell from 1,36,000 in 1951 to 65,000 in 1969. However, the pattern of bank branches in rural and urban areas remained broadly the same.

Although the Indian banking system had made considerable progress in the 1950s and the 1960s, the benefits of this did not percolate down to the general public in terms of access to credit. This was primarily due to the nexus between banks and industrial houses that cornered bulk of bank credit, leaving very little for agriculture and small industries. Efforts, therefore, were made to increase the flow of credit to agriculture. However, the share of agriculture in total bank credit remained broadly at the same level between 1951 and 1967. In this period, various objectives such as enhancing the deposit rates, while keeping the cost of credit for productive activities at a reasonably low level led to a complex structure of interest rates and other micro controls.
The second phase after independence (1967 to 1991-92) was characterized by several social controls over the banking sector. The focus in this phase was, thus, to break the nexus and improve the flow of credit to agriculture. The main instruments used for this purpose were nationalisation of major banks in the country and priority sector lending. These initiatives had a positive impact in terms of spread of the bank-branch network across the country, which in turn, accelerated the process of resource mobilisation. As a result of rapid branch expansion witnessed from 1969, the average population per bank office, which was 65,000 at the time of nationalization, declined to 14,000 by end-December 1990. Large branch expansion also resulted in increase in deposits and credit of the banking system, especially in rural areas. The share of credit to agriculture in total bank credit increased from 2.2 per cent in 1967 to 15.8 per cent in June 1989. However, these achievements extracted a price in terms of health of banking institutions. Banks did not pay adequate attention to their profitability, asset quality and soundness. At the end of this phase, banks were saddled with large non-performing assets. Banks’ capital position turned weak and they lacked the profit motive. During this period, the deposit and lending rate structure became very complex. By the early 1980s, the banking sector had transformed from a largely private owned system to the one dominated by the public sector. In the mid-1980s, some efforts were made to liberalize and improve the profitability, health and soundness of the banking sector. This phase also saw some diversification in banking activities.

The most significant phase in the evolution of banking was the phase of financial sector reforms that began in 1991-92, which had two sub-phases (1991-92 to 1997-98; and 1998-99 and beyond). The main issues faced in the first sub-phase (1991-92 to 1997-98) was the weak health of the banking sector, low profitability, weak capital base and lack of adequate competition. The reforms in the initial phase, thus, focused on strengthening the commercial banking sector. However, banks in this phase developed risk aversion as a result of which credit expansions slowed down in general and to the agriculture in particular.
The focus in the second sub-phase (1998-99 and beyond) was on further strengthening of the prudential norms in line with the international best practices, improving credit delivery, strengthening corporate governance practices, promoting financial inclusion, strengthening the urban co-operative banking sector and improving the customer service. The impact of these measures was encouraging as banks were able to bring down their non-performing assets sharply. This was the most important achievement of this phase. As the asset quality began to improve, banks also started expanding their credit portfolio. Capital position of banks also improved significantly. Competition intensified during this phase as was reflected in the narrowing down of margins. Banks slightly improved their profitability among others, due to increased volumes and improvement in asset quality. Another major achievement in this phase was the sharp increase in the flow of credit to the agriculture and SME sectors. With a view to bringing a larger segment of excluded population within the banking fold, banks were advised to introduce a facility of ‘no frills’ account. About 13 million ‘no frills’ accounts were opened in a short span of two years. The confidence in the urban co-operative banking segment was eroded in the early 2000s following a run on a multi-state co-operative bank. This phase also witnessed some significant changes in the use of technology by banks. Increased use of technology combined with some other specific initiatives helped improve the customer service by banks.

Form this it is clear that the problem of financial exclusion is not a new topic. It was happening before independence also. Rural and agricultural sector were neglected. They were suffering from financial exclusion.

The banking scenario that prevailed in the early independence that is first phase (1947 to 1967) faced financial exclusion issues. There was large concentration of resources from deposits mobilization in a few hands of business families or groups. Banks raised funds and on-lent them largely to their controlling entities. Agriculture was neglected insofar as bank credit was concerned.

The second phase after independence (1967 to 1991-92) breaks the nexus and improve the flow of credit to agriculture. Rapid branch expansion witnessed and
the average population per bank office declined. Large branch expansion also resulted in increase in deposits and credit of the banking system, especially in rural areas. The share of credit to agriculture in total bank credit increased. However, these achievements extracted a price in terms of health of banking institutions. Banks did not pay adequate attention to their profitability, asset quality and soundness. At the end of this phase, banks were saddled with large non-performing assets. Even though there is a awareness about financial inclusion in each phase, even before independence, only in this phase steps were taken to fill the gap. Unfortunately banks health was affected by non performing assets.

Next phase divided in to two sub phases. In 1991-98 banks in this phase developed risk aversion as a result of which credit expansions slowed down in general and to the agriculture in particular. In this phase again financial exclusion expanded as credit expansion slowed down for agricultural and rural sector.

The second sub-phase (1998-99 and beyond) was major achievement in this phase was the sharp increase in the flow of credit to the agriculture and SME sectors. To bring a larger segment of excluded population to banks, banks introduced a facility of ‘no frills’ account. The use of technology is also increasing significantly in this phase as reflected in computerization of branches, increase in the number of ATMs and introduction of electronic modes of transfer of funds (real time gross settlement system and national electronic funds transfer). Financial inclusion is widely recognized as a crucial element in ensuring equitable growth.

Access to affordable financial services - especially credit and insurance - enlarges livelihood opportunities and empowers the poor to take charge of their lives. At close to a quarter of the population, the official headcount figures in India are already worrying, yet, the actual proportion of population which is not growing with the mainstream economy is even larger.

Anurag.B.Singh raises the question that comes to mind is why can't financial inclusion happen on its own? Why do we need to make a policy to increase
the same? Like any other product or service, why can't it find a market of its own? The reasons given by her are

### 2.2 Financial Exclusion

It has been found that financial services are used only by a section of the population. There is demand for these services but it has not been provided. The excluded regions are rural, poor regions and also those living in harsh climatic conditions where it is difficult to provide these financial services. The excluded population then has to rely on informal sector (moneylenders etc) for availing finance that is usually at exorbitant rates. This leads to a vicious cycle. First, high cost of finance implies that first poor person has to earn much more than someone who has access to lower cost finance. Second, the major portion of the earnings is

As per European Commission report\(^{13}\), the World Bank (1995) considered four key areas of exclusion: Transaction banking; Savings; Credit; Insurance as the major areas that all in society should have access.

### 1. Banking exclusion – Transactions

The access to banking (transaction banking services in particular) is seen as a universal need in most developed and cashless societies. The lack of access or use of this financial provision has such bad effects that social inclusion is effectively damaged because: It is the most popular/generalized financial provision, lack stigmatizes; It is a key to access other financial services (credit/savings), lack disturbs market access and gives opportunity to unfair provisions to grow and may consequently increase risk of poverty; It becomes more difficult and expensive for people who can only pay in cash, lack increases risk of being stolen and risk of poverty; It leads to time consuming and somehow annoying procedures, lack reinforce exclusion.

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The types of transactions that can be linked to an account are:

- Receiving regular (electronic) payment of funds such as wages, pensions or social assistance
- Converting cheques or vouchers into cash
- Storing money safely until it needs to be withdrawn
- Paying for goods and services other than in cash
- Paying bills electronically

2. **Savings exclusion**

The problem related to savings is completely different. The access to a simple deposit account does not seem globally to bring many problems. In addition, a lack of access or use may bring inconvenience in day to day life, but cannot be related to social exclusion. In addition, we have to consider that the lack of deposit is more often a consequence than a cause of social problems, as in the following cases:

- Lack of money to save, (low income, low pension,..)
- Lack of habit to save money in bank;
- Unwilling to deal with banks because of negative past experience or prejudice.

3. **Credit exclusion**

Credit is a main financial tool to enable access to goods or expenditures that oversize the monthly budget. It may play a significant role to smooth consumption and to protect against income shocks. Because lack of access to appropriate credit may lead to reimbursement difficulties, it may increase household budget disequilibrium for long period of time and, finally, it may lead to over-indebtedness. Indeed, over-indebtedness may lead to financial and social exclusion.
Exclusion from affordable loans leaves people who need to borrow money with no option but to use high-interest credit.

A number of other dimensions of financial exclusion have been identified (Kempson and Whyley)\textsuperscript{14}, (1999) are

4. **Access exclusion**

The restriction of access through the processes of risk assessment;

5. **Condition exclusion**

Where the conditions attached to financial products make them inappropriate for the needs of some people;

6. **Price exclusion**

Where some people can only gain access to financial products at prices they cannot afford;

7. **Marketing exclusion**

Whereby some people are effectively excluded by targeting marketing and sales;

8. **Self-exclusion**

People may decide that there is little point applying for a financial product because they believe they would be refused. Sometimes this is a result of having been refused personally in the past, sometimes because they know someone else who has been refused.

2.3 The Symptoms of Financial Exclusion

Factors affecting access to financial services do differs

- **Geographic**: deficient access to branches and outlets. This is due to population density, underdeveloped rural areas (e.g., physical infrastructure), security, lack of demand

- **Socio-economic**: deficient access for some population segments because of high minimum deposits, administrative burden and fees, segmentation market frictions, information asymmetries and transaction costs reduce access, especially for the small and risky clients

- **Transaction costs**: Fixed costs in financial intermediation lead to decreasing unit costs as transaction volume increases

- **Risks as limit to access**: Adverse selection problem, Increases with informational opacity and is mitigated by screening techniques. Moral hazard problem, Increases with leverage and is mitigated by collateral and monitoring.

- **Gender issues**: Access to credit is often limited for women who do not have, or cannot hold title to assets such as land and property or must seek male guarantees to borrow.

- **Age factor**: Financial service providers usually target the middle of the economically active population, often overlooking the design of appropriate products for older or younger potential customers.

- **Legal identity**: Lack of legal identities like identity cards, birth certificates or written records often exclude women, ethnic minorities, economic and political refugees and migrant workers from accessing financial services
• **Limited literacy**: Limited literacy, particularly financial literacy, i.e., basic mathematics, business finance skills as well as lack of understanding often constrain demand for financial services.

• **Place of living**: Although effective distance is as much about transportation infrastructure as physical distance, factors like density of population, rural and remote areas, mobility of the population (i.e., highly mobile people with no fixed or formal address), insurgency in a location, etc., also affect access to financial services.

• **Psychological and cultural barriers**: The feeling that banks are not interested to look into their cause has led to self-exclusion for many of the low income groups. However, cultural and religious barriers to banking have also been observed in some of the countries.

• **Social security payments**: In those countries where the social security payment system is not linked to the banking system, banking exclusion has been higher.

• Bank charges: In most of the countries, transaction is free as long as the account has sufficient funds to cover the cost of transactions made. However, there are a range of other charges that have a disproportionate effect on people with low income.

• **Terms and conditions**: Terms and conditions attached to products such as minimum balance requirements and conditions relating to the use of accounts often dissuade people from using such products/services.

• **Level of income**: Financial status of people is always important in gaining access to financial services. Extremely poor people find it difficult to access financial services even when the services are tailored for them. Perception barriers and income discrimination among potential members in group-lending programmes may exclude the poorer members of the community.
• **Type of occupation:** Many banks have not developed the capacity to evaluate loan applications of small borrowers and unorganized enterprises and hence tend to deny such loan requests.

• **Attractiveness of the product:** Both the financial services/products (savings accounts, credit products, payment services and insurance) and how their availability is marketed are crucial in financial inclusion.

2.4 **Five Areas of Financial Inclusion**

1. **Banking**

   There are five areas of financial inclusion\(^\text{15}\) in that banking has attracted the most attention. There are a number of reasons for this. Banking is the most prominent financial service, and a basic stepping stone towards the others. Without a bank account it is more difficult to access credit, savings, gain employment and make payments. Socially, it also seems the most fundamental way that citizens recognize the financial standing of each other. That is, there is stigma attached to those who lack a bank account and other financial goods and services, and so it has a broader impact on social inclusion. Finally, and significantly, banking seems more susceptible to government intervention, and so policy is more likely to be effective as compared to areas such as insurance.

   Not having a bank account is the most obvious way that people are financially excluded. Lacking a bank account is bad for people because they are unable to achieve higher levels of economic well-being but also because it is more difficult for them to gain employment. Regular and stable employment typically requires employees to have a bank account, and the payments system is based on current account transactions. It is increasingly uncommon for organizations to pay

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employees in cheques, much less cash, and many governments require claimants to have an account in order to access benefits. And even where employers do pay by cheques, those who are unbanked still face the difficulty of cashing or depositing their income.

Furthermore, having a bank account may be seen as a basic requirement for citizens in a modern economy. Those without an account suffer from social stigma, not only in terms of having to use high-cost informal services to access cash and credit, but also in terms of how the majority of bank-holding citizens view them. For this reason, interventions in banking are not only the easiest policy area in which a government can intervene, but also one that is most easily justified in terms of social justice and citizen participation. Even if particular individuals are very costly for a bank to offer banking services to – say because they make few transactions and don’t subscribe to other financial products – it is harder for banks to exclude such individuals from basic banking because of its central importance in access to financial goods and services more generally.

2. Credit

Access to affordable credit is now widely recognized as a key element of financial inclusion, and research and now policy is increasingly developed in many countries for those who are already financially included; the issue of credit is closely tied to that of banking because many of these services are accessed via high street banks or mainstream mortgage lenders. However, there is a large non-commercial and also informal credit sector. For those more at risk of being financially excluded, all the difficulties raised above in terms of banking equally apply in the case of credit, including problems of access, language and identity requirements. Credit also raises the problems of risk and social justice.

The cost of credit is generally determined by a risk evaluation by the lender. Mainstream lenders take into account income, credit history, home ownership, age, and a variety of other factors including residence, especially in cases where a loan is for property or property improvements. Because poorer people
are likely to score worse on all these measures, they find it harder to access mainstream credit lenders. And when they do get credit, they are more likely to pay much greater interest and are perhaps more likely to default on their loan.

3. Insurance

As a recent review notes, insurance is the least developed area in terms of government policy, though the Government has now made access to insurance part of its financial inclusion strategy. Insurance is, in fact, perhaps the most difficult to understand in terms of financial inclusion. This is because of its relationship to risk and social justice. The logic of insurance is that those who are more likely to make a claim pay higher premiums, while those whose insured goods or services are less likely to be claimed against pay lower premiums. And since the poorer are more vulnerable to crime, that will necessarily require them to pay higher rates for car insurance and home contents insurance. But given that poorer people have less disposable income and arguably less goods to lose, it may also be less sensible for them to pay insurance premiums.

The only possible solution to this dilemma is somehow to change the calculation of risk for poorer groups. It seems unfair for poor people to pay more for a service when they have less capacity for doing so, but markets are not driven by fairness considerations. One solution is for the government to take on some of the risk and so to reduce premiums for poorer households while at the same time guaranteeing to insurance companies that adequate funds will be provided to run their business.

4. Savings

Savings are necessary for individual economic well-being but also for the strength of a national economy. Without adequate savings individuals are unable to provide for periods where they are unemployed or need cash for goods or to plan for the future more generally. For later in life, pensions have been developed as a way of ensuring adequate money after retirement. In order to save, households must have
some residual cash after paying for basic amenities, leisure and other costs. Although there are sometimes concerns about excessive levels of consumer spending, poorer people may be better off spending the majority of their cash flow rather than saving the small amount they might be able to save by reducing expenses. At the same time, lacking savings makes it more difficult to take advantage of opportunities to improve individual well-being, say by taking courses and expanding labour market options. This is a difficult balance to strike, as individuals may be required to forego spending on valuable goods and activities in order to increase life chances that may or may not materialize and be taken up.

5. **Advice**

The final of the five areas of financial inclusion is advice. Advice can range from extremely general and informal discussions on basic financial questions to more technical and costly suggestions on mortgages, starting a business or buying stocks and shares. It is not possible to make a good decision about bank accounts, credit, insurance or savings without good advice.

2.5 **Financial Inclusion in India**

In order to know where to go regarding financial inclusion it is necessary to know where we are first in financial inclusion. The Global F-index database provides such indicators, measuring how people in 148 economies around the world save, borrow, make payments, and manage risk. These new indicators are constructed with survey data from interviews with more than 150,000 nationally representative and randomly selected adults age 15 and above. The survey was carried out over the 2011 calendar year by Gallup, Inc. as part of its Gallup World Poll. This note explores gender differences in financial behaviors among adults worldwide. All reported global and regional statistics are weighted by country-level adult population, and all reported gender gaps are statistically significant, even

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when controlling for education, age, income, rural or urban residence, and country-level characteristics Financial inclusion in India according to World bank ‘little data book financial inclusion. Low-income economies are those with a GNI per capita of $1,005 or less in 2010. Middle-income economies are those with a GNI per capita of more than $1,005 but less than $12,276. Lower-middle-income and upper-middle income economies are separated at a GNI per capita of $3,975. High-income economies are those with a GNI per capita of $12,276 or more. The data (2.1) show sharp disparities in the use of financial services between high-income and developing economies and across demographic groups.

**Table 2.1: Account at Formal Institution**

<table>
<thead>
<tr>
<th>Account at a Formal Financial Institution</th>
<th>India</th>
<th>South Asia</th>
<th>World</th>
<th>Low</th>
<th>Middle</th>
<th>LMI</th>
<th>UMI</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>All adults (%, age 15+)</td>
<td>35.2</td>
<td>33</td>
<td>50.5</td>
<td>23.7</td>
<td>43.3</td>
<td>28.4</td>
<td>57.2</td>
<td>89.4</td>
</tr>
<tr>
<td>Male adults (%, age 15+)</td>
<td>43.7</td>
<td>40.7</td>
<td>54.7</td>
<td>27</td>
<td>48.1</td>
<td>33.9</td>
<td>61.4</td>
<td>91.7</td>
</tr>
<tr>
<td>Female adults (%, age 15+)</td>
<td>26.5</td>
<td>25</td>
<td>46.3</td>
<td>20.5</td>
<td>38.4</td>
<td>22.9</td>
<td>53.1</td>
<td>87.3</td>
</tr>
<tr>
<td>Young adults (%, ages 15–24)</td>
<td>27.3</td>
<td>24.7</td>
<td>37.9</td>
<td>15.6</td>
<td>34.9</td>
<td>21.5</td>
<td>51.7</td>
<td>76.8</td>
</tr>
<tr>
<td>Older adults (%, age 25+)</td>
<td>38.6</td>
<td>36.6</td>
<td>54.3</td>
<td>28.2</td>
<td>45.7</td>
<td>31.2</td>
<td>58.2</td>
<td>92.2</td>
</tr>
<tr>
<td>Adults with a primary education or less (%, age 15+)</td>
<td>30.5</td>
<td>27.8</td>
<td>40.4</td>
<td>16.2</td>
<td>34.4</td>
<td>20.8</td>
<td>47.5</td>
<td>72.9</td>
</tr>
<tr>
<td>Adults with a secondary education or more (%, age 15+)</td>
<td>59.5</td>
<td>54.2</td>
<td>63.4</td>
<td>35.4</td>
<td>58.7</td>
<td>45.4</td>
<td>71.4</td>
<td>92.3</td>
</tr>
<tr>
<td>Adults in income quintiles I (lowest) and II (%, age 15+)</td>
<td>27.1</td>
<td>25.3</td>
<td>40.7</td>
<td>16.3</td>
<td>31.4</td>
<td>19.7</td>
<td>42.4</td>
<td>85.8</td>
</tr>
<tr>
<td>Adults in income quintiles III, IV, and V (highest) (%, age 15+)</td>
<td>44.4</td>
<td>41</td>
<td>58.3</td>
<td>29.4</td>
<td>52.5</td>
<td>36.3</td>
<td>67.6</td>
<td>92.1</td>
</tr>
<tr>
<td>Adults living in a rural area (%, age 15+)</td>
<td>33.1</td>
<td>30.8</td>
<td>45.8</td>
<td>22</td>
<td>39</td>
<td>25.3</td>
<td>51.7</td>
<td>87</td>
</tr>
<tr>
<td>Adults living in an urban area (%, age 15+)</td>
<td>41</td>
<td>39.2</td>
<td>58.4</td>
<td>35.8</td>
<td>53.8</td>
<td>36</td>
<td>70.3</td>
<td>89</td>
</tr>
</tbody>
</table>

Source: World Bank
While about half of all adults around the world have an account with a formal financial institution, the share in high-income economies (89 percent) is more than twice that in developing economies (41 percent). Globally, more than 2.5 billion adults have no formal account, most of them in developing economies. The gaps in account use between demographic groups are particularly large in developing economies: While 46 percent of men have an account, only 37 percent of women do. And those in the highest income quintile are on average more than twice as likely to have a formal account as those in the lowest quintile. This graph compares account at a formal financial institution in India (series1) with south Asian countries (series2) data and World (series3) data. In India there are vast differences among male and female adults in having a bank account at a formal institution. 43.7 percent male have a bank account but only 26.5% female have account in a formal financial institution. In south Asian countries also there is striking differences among male and female banking practices. In world average also disparity is there but it is better. According to figure 2.1, in high income countries there are not many distinctions among gender. Older adults have more accounts when it is compared with young adults in all income countries. There is variation in account holding among rural and urban adults. This variation is less in high income countries and more in low income countries.

**Figure 2.1 Account at a Formal Institution**

![Graph showing account at a formal institution](image-url)
Having a bank account is foremost need for financial inclusion. Only having bank account is not enough to consider anyone banked, there should be access to bank account. Table 2.2 portrays the level of access to bank account in India.

### Table 2.2: Access to Formal Accounts

<table>
<thead>
<tr>
<th>Access to Formal Accounts (%, age 15+)</th>
<th>India</th>
<th>South Asia</th>
<th>World</th>
<th>Low</th>
<th>Middle</th>
<th>LMI</th>
<th>UMI</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>Zero deposits/withdrawals in a typical month</td>
<td>7</td>
<td>6.6</td>
<td>7.7</td>
<td>5.4</td>
<td>9.3</td>
<td>6.8</td>
<td>11.8</td>
<td>2.1</td>
</tr>
<tr>
<td>zero deposits in a typical month</td>
<td>12.6</td>
<td>11.7</td>
<td>12.8</td>
<td>8.3</td>
<td>14.9</td>
<td>11.6</td>
<td>18.1</td>
<td>6.4</td>
</tr>
<tr>
<td>1–2 deposits in a typical month (% with an account)</td>
<td>72.3</td>
<td>70.5</td>
<td>65.4</td>
<td>64.7</td>
<td>67.8</td>
<td>70.9</td>
<td>64.9</td>
<td>56.1</td>
</tr>
<tr>
<td>3+ deposits in a typical month (% with an account)</td>
<td>11.4</td>
<td>12.9</td>
<td>16</td>
<td>23.1</td>
<td>10.7</td>
<td>11.8</td>
<td>9.6</td>
<td>34</td>
</tr>
<tr>
<td>0 withdrawals in a typical month (% with an account)</td>
<td>14.9</td>
<td>15.9</td>
<td>13.9</td>
<td>21.2</td>
<td>15.7</td>
<td>13.7</td>
<td>17.6</td>
<td>3.9</td>
</tr>
<tr>
<td>1–2 withdrawals in a typical month (% with an account)</td>
<td>68.5</td>
<td>66.4</td>
<td>51.7</td>
<td>59.1</td>
<td>59.4</td>
<td>64.4</td>
<td>54.7</td>
<td>18.8</td>
</tr>
<tr>
<td>3+ withdrawals in a typical month (% with an account)</td>
<td>12.2</td>
<td>11.9</td>
<td>27.4</td>
<td>16.1</td>
<td>17.2</td>
<td>15.1</td>
<td>19.2</td>
<td>71.7</td>
</tr>
<tr>
<td>ATM is the main mode of deposit (% with an account)</td>
<td>1.6</td>
<td>2</td>
<td>13.6</td>
<td>4.3</td>
<td>11.3</td>
<td>4.5</td>
<td>17.7</td>
<td>26.2</td>
</tr>
<tr>
<td>Bank teller is the main mode of deposit (% with an account)</td>
<td>89.3</td>
<td>85.3</td>
<td>69.9</td>
<td>78.8</td>
<td>73.1</td>
<td>80.2</td>
<td>66.4</td>
<td>53.7</td>
</tr>
<tr>
<td>Bank agent is the main mode of deposit (% with an account)</td>
<td>3.1</td>
<td>5.3</td>
<td>3.1</td>
<td>9.1</td>
<td>2.6</td>
<td>4</td>
<td>1.2</td>
<td>3</td>
</tr>
<tr>
<td>ATM is the main mode of withdrawal (% with an account)</td>
<td>18.4</td>
<td>18</td>
<td>43.3</td>
<td>23</td>
<td>38.8</td>
<td>31</td>
<td>46.1</td>
<td>68.7</td>
</tr>
<tr>
<td>Bank teller is the main mode of withdrawal (% with an account)</td>
<td>69.7</td>
<td>68.6</td>
<td>47.7</td>
<td>62.9</td>
<td>52.4</td>
<td>56.8</td>
<td>48.2</td>
<td>23.3</td>
</tr>
<tr>
<td>Bank agent is the main mode of withdrawal (% with an account)</td>
<td>3.2</td>
<td>4</td>
<td>1.9</td>
<td>5.4</td>
<td>1.8</td>
<td>3</td>
<td>0.7</td>
<td>0.8</td>
</tr>
<tr>
<td>Has debit card</td>
<td>8.4</td>
<td>7.2</td>
<td>30.4</td>
<td>7.4</td>
<td>24.8</td>
<td>10.1</td>
<td>38.7</td>
<td>61.4</td>
</tr>
</tbody>
</table>

Source: World Bank
Access to formal account is another important indicator of financial inclusion. Number of deposits and withdrawals in a month is the comprehensible indicator of access to formal account. In India 72.3% of adults have 1-2 deposits per month. 0 deposits in a month is 12.6% in India which is only 6.4% in high income countries. 3 deposits in a month is towering in high income countries when compared to low, middle income countries. In withdrawals also similar situation prevails. Following graph shows the deposit and withdrawal pattern in India(series1), South Asia(series2), and the world(series3) as whole.

Figure 2.2 Access to Formal Accounts

Tellers are responsible for accurately processing routine transactions at a bank. These transactions include cashing checks, depositing money, and collecting loan payments. An automated or automatic teller machine is a computerized telecommunications device that enables the clients of a financial institution to perform financial transactions without the need for a cashier, human clerk or bank teller.

A banking agent is a retail or postal outlet contracted by a financial institution or a mobile network operator to process clients’ transactions. Rather than a branch teller, it is the owner or an employee of the retail outlet who conducts the transaction and lets clients deposit, withdraw, and transfer funds, pay their bills,
inquire about an account balance, or receive government benefits or a direct deposit from their employer. Banking agents can be pharmacies, supermarkets, convenience stores, lottery outlets, post offices, and many more.

Figure 2.3 Mode of Deposit and Withdrawal

According to table 2.3, in India 1.6% people only use ATM as the mode of deposit while in high income countries 26.2% and in world 13.6%. ATM is not popular for deposits and is mostly used for withdrawals. Not only in India all over World Bank teller is the major source of deposits. ATM as the main mode withdrawal is getting popular in India even though it is far away from high income countries. Only 18.4% of people use ATM as the main mode of withdrawal it is fewer when compared with high income economies (43.3%). But India has more ATM usage while comparing with South Asia average.
Table 2.3: Use of Formal Accounts

<table>
<thead>
<tr>
<th>Use of Formal Accounts (%)</th>
<th>Country</th>
<th>South Asia</th>
<th>World</th>
<th>Low</th>
<th>Middle</th>
<th>LMI</th>
<th>UMI</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>Use an account for business purposes</td>
<td>4.1</td>
<td>4.04</td>
<td>7.9</td>
<td>4.6</td>
<td>4</td>
<td>0.1</td>
<td>4</td>
<td>24.4</td>
</tr>
<tr>
<td>Use an account to receive wages</td>
<td>8.3</td>
<td>7.48</td>
<td>20.9</td>
<td>5.9</td>
<td>15.1</td>
<td>0.5</td>
<td>21.3</td>
<td>49.5</td>
</tr>
<tr>
<td>Use an account to receive government payments</td>
<td>4</td>
<td>3.53</td>
<td>12.9</td>
<td>2.5</td>
<td>6.5</td>
<td>0.9</td>
<td>9</td>
<td>42</td>
</tr>
<tr>
<td>Use an account to receive remittances</td>
<td>1.9</td>
<td>2.03</td>
<td>7.2</td>
<td>4.7</td>
<td>5.9</td>
<td>0.7</td>
<td>8</td>
<td>13.2</td>
</tr>
<tr>
<td>Use an account to send remittances</td>
<td>1.8</td>
<td>1.63</td>
<td>7</td>
<td>2.8</td>
<td>4.6</td>
<td>0</td>
<td>6.2</td>
<td>18.1</td>
</tr>
</tbody>
</table>

Source: World Bank

Emphasis on usage is most important for financial inclusion. Diverse portfolios make the poor less vulnerable to the unexpected events that emerge within their environment. The socio-economic goals, which are the motivation for the Financial Inclusion drive, will not be realized if the banked poor are not encouraged to avail themselves of the opportunities that access presents. Increased usage can also lead to other vitally important outcomes—increased savings balances over time, and increased access to other vital financial services including insurance and loans. All over the World, Bank account used mostly for receiving wages and for receiving government payments. But there is drastic difference in the percentage of use. Using bank account for sending and receiving payments also there is striking differences among different income group countries.
Mobile technology is transforming the global banking and payment industry by providing added convenience to existing bank customers in developed markets, and by offering new services to the unbanked customers in emerging markets. Mobile banking is gaining popularity with increasing number of people using this platform to buy tickets, pay bills, shop online, and transfer funds. Checking account information, balance available, credit/debit card information, cheque status, setting alerts, payment reminders, locating ATMs and bank branches, accessing mini statement, accessing loan and equity statements, insurance policy management, placing orders for cheque books etc via mobile phones are some of the services offered in mobile banking.

Table 2.4: Payments System

<table>
<thead>
<tr>
<th>Mobile Payments (%, age 15+)</th>
<th>Country</th>
<th>South Asia</th>
<th>World</th>
<th>Low</th>
<th>Middle</th>
<th>LMI</th>
<th>UMI</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>Use a mobile phone to pay bills</td>
<td>2.2</td>
<td>2.02</td>
<td>2</td>
<td>2.6</td>
<td>1.8</td>
<td>0.1</td>
<td>1.7</td>
<td>..</td>
</tr>
<tr>
<td>Use a mobile phone to send money</td>
<td>0.6</td>
<td>0.82</td>
<td>2.2</td>
<td>7.1</td>
<td>1.6</td>
<td>0.4</td>
<td>0.9</td>
<td>..</td>
</tr>
<tr>
<td>Use a mobile phone to receive money</td>
<td>2</td>
<td>1.93</td>
<td>3</td>
<td>9.1</td>
<td>2.4</td>
<td>0.8</td>
<td>1.1</td>
<td>..</td>
</tr>
</tbody>
</table>

.. indicates that data are not available

compiled from world bank data
The table 2.4 portrays use of mobile banking for paying bills and to send and receive money. Wide-scale savings mobilization is fundamental to building inclusive financial systems. It is now widely understood that savings has great potential impact. This insight is grounded in evidence that the poor do save in cash and in kind—whether as a way to build assets, manage household cash flow, or effectively cope with risk.

Table 2.5: Saving Pattern Across Countries

<table>
<thead>
<tr>
<th>Savings (%, age 15+)</th>
<th>India</th>
<th>South Asia</th>
<th>World</th>
<th>Low</th>
<th>Middle</th>
<th>LMI</th>
<th>UMI</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>Saved any money in the past year</td>
<td>22.4</td>
<td>21.3</td>
<td>35.9</td>
<td>29.9</td>
<td>30.7</td>
<td>27.6</td>
<td>33.7</td>
<td>58.3</td>
</tr>
<tr>
<td>Saved at a formal financial institution in the past year</td>
<td>11.6</td>
<td>11.1</td>
<td>22.4</td>
<td>11.5</td>
<td>17.8</td>
<td>11.1</td>
<td>24.2</td>
<td>44.6</td>
</tr>
<tr>
<td>Saved using a savings club in the past year</td>
<td>3.2</td>
<td>3.3</td>
<td>5.3</td>
<td>8.2</td>
<td>4.9</td>
<td>0.2</td>
<td>2.8</td>
<td>5.4</td>
</tr>
<tr>
<td>Saved for future expenses in the past year</td>
<td>16.7</td>
<td>15.5</td>
<td>24</td>
<td>20.3</td>
<td>21</td>
<td>19.9</td>
<td>22</td>
<td>37.4</td>
</tr>
<tr>
<td>Saved for emergencies in the past year</td>
<td>18</td>
<td>17.2</td>
<td>27.2</td>
<td>22.8</td>
<td>23.3</td>
<td>22.1</td>
<td>24.5</td>
<td>44.1</td>
</tr>
</tbody>
</table>

Source: world Bank

Data is not available for high income countries. In India when it is compared with upper middle income countries it has better percentage of mobile banking. Still long way to go regarding mobile banking. If mobile banking become popular and financial education is provided automatically usage of bank accounts will increase. Saving, credit and insurance are the indicators of usage of bank accounts.

Mostly it is believed saving practices are high in India. According to World Bank data saving practices are high in high income countries and upper middle income countries. The table 2.5 reveals the saving practices in India (series1), South Asia (series2), and the world (series3). Closing this savings gap is central to any strategy of financial inclusion and equitable economic development.
However saving practices to meet emergencies is comparatively high than saving for future expenses to all income countries including India. Finding of RBI's Research Project Study in Kerala Study concludes that meaningful financial inclusion of the poor by the commercial banks also depends on their ability to meet the credit gaps of the poor households.

Bank is the most appropriate channel for credit delivery. Credit intermediation has traditionally been the stronghold of banks, driven by policy mandates and regulatory backing. Over the years, banks have also used intermediaries for channeling credit to the end customer and a few such credit intermediation channels have established themselves as sustainable routes – these include the NABARD promoted Self Help Group (SHG)-bank linkage model, as well as the Joint Liability Group-based Micro Finance Institution (MFI) model.

So far the unbanked population has been vulnerably dependent of informal channels of credit like family, friends and moneylenders. Availability of adequate and transparent credit from formal banking channels shall allow the entrepreneurial spirit of the masses to increase outputs and prosperity in the countryside. Below table elucidates Loan behavior of people belong to low, high and middle income countries. India people’s Loan from a formal financial institution in the past year is 7.7% which is less comparatively with south Asian countries average, low income countries average, high income countries average and world
average. Surprisingly low income countries borrowing from formal financial institution is more than all sections except high income countries.

Table 2.6: Credit Pattern Across Economies

<table>
<thead>
<tr>
<th>Credit (%, age 15+)</th>
<th>India</th>
<th>South asian</th>
<th>World</th>
<th>Low</th>
<th>Middle</th>
<th>LMI</th>
<th>UMI</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loan from a formal financial institution in the past year</td>
<td>7.7</td>
<td>8.77</td>
<td>9</td>
<td>11.4</td>
<td>7.6</td>
<td>0.3</td>
<td>7.8</td>
<td>13.8</td>
</tr>
<tr>
<td>Loan from family or friends in the past year</td>
<td>19.7</td>
<td>19.5</td>
<td>22.8</td>
<td>30.2</td>
<td>24.7</td>
<td>26.6</td>
<td>22.8</td>
<td>12.3</td>
</tr>
<tr>
<td>Loan from an informal private lender in the past year</td>
<td>6.6</td>
<td>6.45</td>
<td>3.4</td>
<td>7</td>
<td>3.3</td>
<td>0.3</td>
<td>1.5</td>
<td>2.3</td>
</tr>
<tr>
<td>Outstanding loan to purchase a home</td>
<td>2.3</td>
<td>2.42</td>
<td>7</td>
<td>2.4</td>
<td>3.2</td>
<td>0.2</td>
<td>4</td>
<td>23.8</td>
</tr>
<tr>
<td>Outstanding loan for home construction</td>
<td>3.7</td>
<td>4.44</td>
<td>5</td>
<td>6.3</td>
<td>4.8</td>
<td>0.7</td>
<td>4.9</td>
<td>..</td>
</tr>
<tr>
<td>Outstanding loan to pay school fees</td>
<td>5.5</td>
<td>4.96</td>
<td>5.4</td>
<td>6.9</td>
<td>5.3</td>
<td>0.8</td>
<td>3.8</td>
<td>..</td>
</tr>
<tr>
<td>Outstanding loan for health or emergencies</td>
<td>14.2</td>
<td>14.1</td>
<td>11</td>
<td>16.1</td>
<td>10.6</td>
<td>14.8</td>
<td>6.6</td>
<td>..</td>
</tr>
<tr>
<td>Outstanding loan for funerals or weddings</td>
<td>3.4</td>
<td>3.93</td>
<td>2.8</td>
<td>5.4</td>
<td>2.5</td>
<td>0.9</td>
<td>1.2</td>
<td>..</td>
</tr>
</tbody>
</table>

...indicates that data are not available
Source: world Bank

Loan from family and friends was more than loan from an informal private lender in all income income group countries. In India outstanding loan for health or emergencies were high than loan for other purposes like home loan, education loan, and personal loan. Not only in India, all countries except income countries prevailing in same situation.
Figure 2.6 Credit Pattern Across Economies

The above graph provides a clear picture about credit behaviour. Below table talks about amount paid for health insurance, upper middle income countries paid more for health insurance when it is compared with middle income and low income countries.

Table 2.7: Insurance Across Economies

<table>
<thead>
<tr>
<th>Insurance (%)</th>
<th>India</th>
<th>South Asia</th>
<th>World</th>
<th>Low</th>
<th>Middle</th>
<th>LMI</th>
<th>UMI</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>Personally paid for health insurance</td>
<td>6.8</td>
<td>5.55</td>
<td>17.1</td>
<td>2.2</td>
<td>18.6</td>
<td>5.1</td>
<td>31.3</td>
<td>..</td>
</tr>
</tbody>
</table>

...indicates that data are not available

Source: world Bank

The Table 2.7 provides a clear picture about India’s financial inclusion attainment. The quality of this report and support offered to understand the financial inclusion is one of the major motivations behind the study
2.6 Measures to Enhance Financial Inclusion

The Reserve Bank of India (RBI) set up the Khan Commission in 2004 to look into financial inclusion and the recommendations of the commission were incorporated into the mid-term review of the policy (2005–06). In the report RBI exhorted the banks with a view to achieving greater financial inclusion to make available a basic "no-frills" banking account. In India, financial inclusion first featured in 2005, when it was introduced by K.C. Chakraborty, the chairman of Indian Bank. Mangalam became the first village in India where all households were provided banking facilities. Norms were relaxed for people intending to open accounts with annual deposits of less than Rs. 50,000. General credit cards (GCCs) were issued to the poor and the disadvantaged with a view to help them access easy credit. In January 2006, the Reserve Bank permitted commercial banks to make use of the services of non-governmental organizations (NGOs/SHGs), micro-finance institutions, and other civil society organizations as intermediaries for providing financial and banking services. These intermediaries could be used as business facilitators or business correspondents by commercial banks. The bank asked the commercial banks in different regions to start a 100% financial inclusion campaign on a pilot basis. As a result of the campaign, states or union territories like Puducherry, Himachal Pradesh and Kerala announced 100% financial inclusion in all their districts. Reserve Bank of India’s vision for 2020 is to open nearly 600 million new customers' accounts and service them through a variety of channels by leveraging on IT. However, illiteracy and the low income savings and lack of bank branches in rural areas continue to be a roadblock to financial inclusion in many states and there is inadequate legal and financial structure.

In India, RBI has initiated several measures to achieve greater financial inclusion, such as facilitating no-frills accounts and GCCs for small deposits and credit. Some of these steps are:

- Opening of no-frills accounts: Basic banking no-frills account is with nil or very low minimum balance as well as charges that make
such accounts accessible to vast sections of the population. Banks have been advised to provide small overdrafts in such accounts.

- Relaxation on know-your-customer (KYC) norms: KYC requirements for opening bank accounts were relaxed for small accounts in August 2005, thereby simplifying procedures by stipulating that introduction by an account holder who has been subjected to the full KYC drill would suffice for opening such accounts. The banks were also permitted to take any evidence as to the identity and address of the customer to their satisfaction. It has now been further relaxed to include the letters issued by the Unique Identification Authority of India containing details of name, address and Aadhaar number.

- Engaging business correspondents (BCs): In January 2006, RBI permitted banks to engage business facilitators (BFs) and BCs as intermediaries for providing financial and banking services. The BC model allows banks to provide doorstep delivery of services, especially cash in-cash out transactions, thus addressing the last-mile problem. The list of eligible individuals and entities that can be engaged as BCs is being widened from time to time. With effect from September 2010, for-profit companies have also been allowed to be engaged as BCs.

- Swabhimaan Campaign: Under “Swabhimaan” - the Financial Inclusion Campaign launched in February 2011, Banks had provided banking facilities by March, 2012 to over 74,000 habitations having population in excess of 2000 using various models and technologies including branchless banking through Business Correspondents Agents (BCAs). Over 3.16 crore accounts were opened and more than 62,000 BCAs were engaged during the campaign. Further, in terms of Finance Minister’s Budget Speech 2012-13, it has been decided to extend the “Swabhimaan”
campaign to habitations with population of more than 1000 in North Eastern and hilly States and to habitations which have crossed population of 1600 as per census 2001. Accordingly, about 45,000 such habitations had been identified to be covered under the extended “Swabhimaan” campaign.

- Setting up of Ultra Small Branches (USBs): Considering the need for close supervision and mentoring of the Business Correspondent Agents (BCAs) by the respective banks and to ensure that a range of banking services are available to the residents of such villages, Ultra Small Branches (USBs) are being set up in all villages covered through BCAs under Financial Inclusion.

- A USB would comprise of a small area of 100-200 sq. feet where the officer designated by the bank would be available with a lap-top on pre-determined days. While the cash services would be offered by the BCAs, the bank officer would offer other services, undertake field verification and follow up the banking transactions. The periodicity and duration of visits can be progressively enhanced depending upon business potential in the area. A total of over 43,000 USBs have been set up in the country by December, 2012.

- Use of technology: Recognizing that technology has the potential to address the issues of outreach and credit delivery in rural and remote areas in a viable manner, banks have been advised to make effective use of information and communications technology (ICT), to provide doorstep banking services through the BC model where the accounts can be operated by even illiterate customers by using biometrics, thus ensuring the security of transactions and enhancing confidence in the banking system.

- Adoption of EBT: Banks have been advised to implement EBT by leveraging ICT-based banking through BCs to transfer social
benefits electronically to the bank account of the beneficiary and deliver government benefits to the doorstep of the beneficiary, thus reducing dependence on cash and lowering transaction costs.

- GCC: With a view to helping the poor and the disadvantaged with access to easy credit, banks have been asked to consider introduction of a general purpose credit card facility up to 25,000 at their rural and semi-urban branches. The objective of the scheme is to provide hassle-free credit to banks’ customers based on the assessment of cash flow without insistence on security, purpose or end use of the credit. This is in the nature of revolving credit entitling the holder to withdraw up to the limit sanctioned.

- Simplified branch authorization: To address the issue of uneven spread of bank branches, in December 2009, domestic scheduled commercial banks were permitted to freely open branches in tier III to tier VI centers with a population of less than 50,000 under general permission, subject to reporting. In the north-eastern states and Sikkim, domestic scheduled commercial banks can now open branches in rural, semi-urban and urban centers without the need to take permission from RBI in each case, subject to reporting.

- Opening of branches in unbanked rural centers: To further step up the opening of branches in rural areas so as to improve banking penetration and financial inclusion rapidly, the need for the opening of more bricks and mortar branches, besides the use of BCs, was felt. Accordingly, banks have been mandated in the April monetary policy statement to allocate at least 25% of the total number of branches to be opened during a year to unbanked rural centers.

- Aadhaar Enabled Payment Systems (AEPS) : The AEPS architecture designed by Unique Identification Authority of India (UIDAI) in collaboration with the NPCI is a platform which banks
can leverage upon for expanding their financial inclusion initiatives. The basic premise of AEPS is that one BC Customer Service Point (CSP) will have the ability to service customers of many banks based on the unique bio-metric identification data stored in the Aadhaar database. The AEPS platform 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. The beneficiaries withdraw the amounts through micro-ATMs which authenticate their Aadhaar number.