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# Understanding Financial Inclusion in India and Role of ICT in ICT

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***Abstract:***
*Inclusive growth is absolutely necessary to pull millions of Indians out of poverty. Financial inclusion is crucial driver for such growth by covering large sections of society providing them with financial services. High economic growth in the past decade has lead to huge economic inequality in India; various efforts have been made to achieve the objectives of the financial inclusion. One such effort is adoption of ICT in Indian banking sector. This paper is an attempt to understand how the financial inclusion is happening in India by discussing and analyzing various initiatives by the Government, Reserve Bank of India, Banks and the role played by ICT.*

***Key words****: Financial inclusion; ICT; Financial services; Inclusive Growth; Indian banks*

## 1. Introduction

India which was a socialist economy at the time of independence did away with the socialist policies after the economic liberalization in 1991 and by the turn of 21st century, India's GDP has grown at a very high rate peaking at 10.1 percent in 2010. This level of economic growth has led to huge economic inequality, to negate this inequality it was understood that inclusive growth is necessary. Inclusive growth can be possible only through financial inclusion. The term financial inclusion can be defined as deliver of financial services at affordable costs to sections of disadvantaged and low income groups. Although the term gained importance in early 2000's, the beginning of financial inclusion in India can be traced back to 1969 when Indira Gandhi, the then Prime Minister of India nationalized fourteen major commercial banks and in 1980 another six banks. This brought 91 percent of banking sector under government [1]. After the nationalization, Indian banking sector expanded in an unprecedented rate. Since 1969 the banking sector has grown at a good pace, over 102,343 branches have been opened compared to 8700 before 1969, thus providing more number of people with access to the financial system [2]. Still, Only 58.7 percent of the Indian population are availing banking services with the formal financial sector [2] and only 40 percent of population are engaged with the formal financial sector [3] .As the level of financial exclusion in India is alarming, to increase the financial inclusion various initiatives and policy measures in banking sector have been taken by the Government and Reserve Bank of India to accelerate the process. For a developing economy like India, financial inclusion helps to improve the social development initiatives by reducing the leakages in social welfare distribution programs.

## 2. Barriers to Financial Inclusion

The term "excluded section" refers to people who are not having access to the financial services. Excluded section generally consists of people working in an unorganized sector, landless labour, migrants, urban slum dwellers, marginal farmers, socially excluded groups. The major barriers for financial inclusions are due to lack of information and awareness people from excluded section find the financial services complex in nature. Since the commercial banks operate in profitable areas as a result only 37 percent of branches are there in rural areas whereas almost 70 percent of India is in rural areas [2]. People who live in under developed areas find it very difficult to reach the nearest bank due to transportation cost and wages lost in travelling to the bank. Another barrier for financial inclusion is insufficient documentation, inability to provide a legal identity such a residence proof, birth certificates, etc. often exclude women and migrants from accessing financial services.
Other barriers are limitations of physical infrastructure, high cost of maintaining setup.

## 3. ICT and Financial Inclusion

Developments in the field of Information and Communication Technology (ICT) have made inroads in almost all the sectors. The impact of technology adoption particularly in the banking sector has changed the face of the industry. Banking sector is the backbone of any economy and a healthy economy denotes a strong and resilient banking sector. ICT strongly supported the growth and inclusiveness of the banking sector, thus facilitating an inclusive economic growth. ICT not only improved the efficiency of the banking by strengthening the back end administrative processes and also front end operations thus bringing down the transaction costs for customers which has been the major focus of the ICT for financial inclusion. Today banks have centralized operations, more and more banks and branches are moving to core banking solutions, network based computing and are using ICT for customer relationship management.. The average cost per transaction through an ATM is INR 18 whereas the same for a bank branch is INR 45 [4]. ICT has not just helped to reduce the transaction costs but it is acting as a tool to facilitate financial inclusion overcoming the barriers such as limitations of physical infrastructure and high cost of maintaining setup. Various initiatives taken by the banks use ICT as an important tool for fulfilling them. The Business Correspondent (BC) model which is the most successful model adopted by the Banks for financial inclusion would not have been possible without ICT.

**4. Initiatives Taken By the Government of India, RBI and Banks to Facilitate Financial Inclusion**

The Government of India and the Reserve Bank of India have played an important role in establishing banks and financial infrastructure for providing financial access to the poor such as National Bank for Agriculture and Rural Development (NABARD) and Small Industries Development Bank of India (SIDBI). NABARD has designed and developed the SHG-Bank Linkage Programme (SBLP) through which it has provided INR 25.45 billion to banks covering their lending to SHGs and around 4.82 million SHGs received loans from banks with an outstanding amount of INR 306.27 billion while 7.54 million SHGs have been linked to the banking system as on March 2011[5]. Although the number of SHG's linked with banks have increased, but the size of the disbursed loans haven't shown the same trend and in fact the SBLP had underperformed in the year 2011-2012[5]. It also operates the INR 500 crore Women SHG's Development Fund proposed by the Union Cabinet 2011-2012 to empower women and fund their SHG's[5]. Other overall inclusion initiatives by the Government are Swarnjayanti Gram Swarozgar Yojana (SGSY), National Rural Livelihood Mission (NRLM) , The Mahatma Gandhi National Rural Employment Guarantee Scheme (MGNREGS) and Aadhaar. The measures taken by the RBI include No-Frills Accounts (NFA), relaxing Know Your Customer (KYC) norms, providing easy credit facilities through Kisan Credit Card (KCC) and General Credit Card (GCC), liberalization of Bank branch expansion. Through NFA with a view to achieving the objective of greater financial inclusion, RBI advised all the banks to provide basic banking account either with 'nil' or very low minimum balances as well as charges that would make such accounts accessible to vast sections of population. In doing so, the RBI has asked the banks to relax the KYC norms. Hence, KYC procedure for opening accounts was simplified for those accounts whose balances will not be exceeding INR 50,000 and their annual borrowing would not exceed INR 100,000[6]. A study by CMF-IFMR in their findings published that 72% of the accounts in Cuddalore, Tamil Nadu had zero or near zero balance even after a year. Similarly, another CMF-IFMR study reported that the 100% inclusion drive in Gulbarga district, Karnataka did not have any major impacts because as much as one-third of the households were without bank accounts even after the drive[5]. With the view of providing credit facilities in the rural areas, RBI advised all the Scheduled Caste Banks (SCB's) and Regional Rural banks (RRBs) to introduce GCC facility up to INR 25,000, for their constituents in rural and semi-urban areas [6]. Similarly, the RBI also introduced the KCC scheme to provide timely credit to the farmers for the agricultural purposes. 22.49 millions Farmers have been provided with Kisan Credit Cards and 950,000 clients have been provided with General purpose Credit Cards as on March 2011[5]. RBI has also advised the banks to use the services of NGOs/SHGs/MFIs by providing banking services as BC's. RBI in its October 2009 review took a further step in financial inclusion by freeing the norms for opening of branches in towns or villages with population less than 50,000.The Financial Inclusion Technology Fund (FITF) had been set up in 2007-08 as per the suggestion of the Rangarajan Committee report with a corpus of Rs. 500 crore each. The objectives of FITF has been to enhance investment in ICT aimed at promoting financial inclusion, stimulate the transfer of research and technology in financial inclusion, increase the technological absorption capacity of financial service providers/users and encourage an environment of innovation and cooperation among the stakeholders[6].

**5. Business Correspondent Model (BC) Model**

To achieve higher financial inclusion in the country, a committee on Financial Inclusion, with Dr. C. Rangarajan as Chairman, was constituted by the Government of India in June 2006 to increase the outreach of the banks for greater financial inclusion. The committee recommended the banks to use the services of intermediaries such as of Business Facilitators (BFs) and Business Correspondents (BCs) for providing financial and banking services to the people in rural and unbanked areas. To enable themselves in expanding their outreach and offer limited range of banking services at low cost at locations other than where there is a bank branch/ ATM, banks engage retail agents. These retail agents are Business Correspondents (BC) who represent the concerned bank and offer financial services. These BCA's are connected to the bank by CBS and the transactions are done in such a way that as on swiping the smart card on the smart card on the machine the account details of the customer are retrieved and then once the amount to be transacted is entered the transaction is authenticated by biometric system present in the machine, which scans the customers thumb print, since most of the customers are illiterate, there is a voice system present in the machine which announces the transaction details to the customer in the local language, hence this so designed to ensure that customer is not cheated . As of December 2012, there were over 1, 52,000 BCs engaged by Banks [2]. Also till December 2012, over 18.38 crore transactions valued at INR 16533 crore had been undertaken by BCs [2]. BC's have also brought down the transaction costs which have also been one of the major objective of financial inclusion. According to a Wharton School study, the average cost per transaction in India at a BC is the lowest at INR 4.50 per transaction as compared to an ATM (INR 18) and a bank branch (about INR 45) [4].Also, under the "Swabhimaan" campaign launched in February 2011, over 74,000 habitations having population in excess of 2000 using various models and technologies including branchless banking through Business Correspondents(BCs)[2]. Earlier we have seen that no frill accounts (NFA) approach of financial inclusion has proven to be ineffectual, but what actually is to be thought of is NFA when delivered through BC's have also shown very low activity. One reason for this is because current model of BC offers only liquidity management. While a transaction mechanism for daily cash management is indeed a core requirement for low income customers. However, the particular segment views this as more complex and hence customers prefer storing money with themselves as they see it as less complex and more convenient. The other reason is among the banks, the financial inclusion is often views as regulatory compulsion or social initiative rather than viable business proposition. As a result mass accounts opening and recruitment of BC's is being done and minimal focus is put on implementing an effective transactional mechanism. According to the Micro save survey, there is a belief among bankers at all levels from senior managers to branch staff that the business correspondent model is a poor man's service [7]. This attitude is turning the lack of belief in the business case into a self fulfilling prophecy, as evidenced by the paltry levels of activity in most BC initiatives. Dr. Duvvuri Subbarao, the then Governor of RBI said it is only the change in mindset of all concerned stakeholders that can make financial inclusion a reality' 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 [8]. Also, Dr. K.C. Chakrabarty, Deputy Governor of RBI in his address at 7th Banking Tech Summit 2012, Mumbai on 28 June 2012 said "Banks have to ensure that the BC model finds space in the business strategies of the banks and not in the footnotes of their annual reports and that the banks should make client acquisition under this model a business proposition; and not treat it as a CSR activity"[9].

**6. Mobile Banking**

The term mobile banking consists of activities that result in an entity's access to the range of banking products (related to savings or credit) by using a cell phone. This also includes payments (transfer of value, bill payments etc.) made using a cellular/mobile phone. The mobile banking provision for the unbanked population can be the quickest way to achieve the goal of financial inclusion in India. On customer's side, it can help them to easily avail the financial services at a low cost. On banks side, mobile banking will be cost effective (would save costs of providing physical access). Thus, mobile banking can successfully tackle barriers of financial inclusion which are high cost of providing services and low accessibility. The outreach of the banks would increase tremendously by providing services through mobile banking. Total mobile subscribers as on March, 2013 are 867.80 million[10] and according to the Analysis Mason report there will be more than 1.36 billion mobile subscribers[11]. Also, according to TRAI (Telecom Regulatory Authority of India) the rural India will cross 100 percent mobile penetration in 2020[12].There are various communication modes for deploying mobile banking services such as Interactive Voice Response (IVR), Short Messaging Service (SMS), Wireless Access Protocol (WAP), Stand-alone Mobile Application Clients (Mobile Apps), Unstructured Supplementary Service Data (USSD), Using SIM tool Kit (STK). The target groups for the financial inclusion are likely to be low income, semi literate with limited knowledge of technological applications. Hence, such target groups would prefer a mode for mobile banking which is user friendly (menu driven but without the need to download software etc.), has a low cost of operation (cost per transaction) and does not require any significant investment (requirement of a high-end phone instrument).

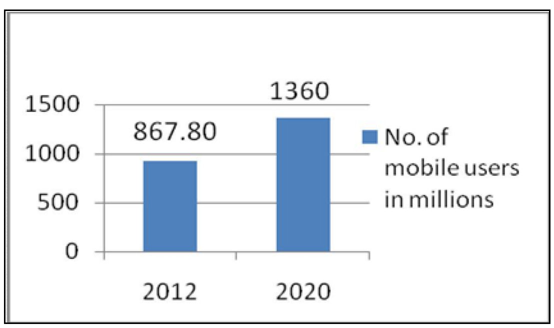


*Figure 1*
*Sources: TRAI; Analysis Mason*

The features of IVR, SMS and USSD make them eminently suitable communication modes for providing banking services for financial inclusion. Banks have deployed the IVR channel for IVR channel for services like balance enquiry, mini-statement, cheque-book request and complaint booking and not for the full-suite of mobile banking services, as the human interface in IVR exposes the system to the potential risk of misuse and the cost of operation is also high. However, SMS and USSD have been deployed for a wider range of services by most banks that have implemented mobile banking services. Some banks such as SBI and ICICI have launched USSD based services. However, there are various challenges with adoption of mobile banking are Regulatory challenges such as only those having banking account can use the provision of mobile banking. This will limit the full potential of mobile banking to extend micro credit and bring banking to the large number of unbanked customers. India has 18 official languages and state governments are directed to correspond in their official language for official purposes and as there is huge illiterate Indian population; pan Indian mobile banking will be quite cumbersome. Also, there are other security challenges such as SMS spoofing attack, where attacker sends the messages on network manipulating sender's number. Virus attack where software's like Trojan Horses and Zeus are used to steal mobile transaction authentication number or password.

**7. Conclusion**

Significant progress towards financial inclusion has been made through various initiatives taken by the Government, RBI, Banks and ICT has been the key driver in implementing these initiatives. Various models have been tested for financial inclusion, however BC model has emerged out to be the most effective model for the financial inclusion so far and has managed to reduce the transaction costs and tackle the barriers of financial inclusion. It is important that banks should start addressing the issue of financial illiteracy by organizing campaigns, addressing this issue would help in greatly reducing the financial exclusion. Banks rather than just offering liquidity management services should also offer other innovative products which would have customer value proposition. Banks should see financial inclusion as an opportunity rather than just a regulatory compulsion or a social initiative because today's poor is tomorrow's middle class. It is for the banks to convert what they see as an obligation into an exciting opportunity and aggressively pursue it. Banks should create out of box strategies and employ new technologies to enhance the performance of the existing approach. Another model which will immensely help in financial inclusion is mobile banking which is still in its nascent stage. With an expected rural penetration of 100 percent by 2020, mobile banking along with an innovated BC model will give magnanimous outreach to the banks and also help them in providing cost effective products and services. Hence, ICT has a greater role to play in financial inclusion.

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