The need for Financial Inclusion with an Indian perspective

March 3, 2008

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Financial Inclusion has become the buzzword in academic research, public policy meeting and seminars. This report is a primer on the subject focusing on India.

Background

The earlier theories of development concentrated on labor, capital, institutions etc as the factors for growth and development. The leading works hardly include finance as a factor for growth. Fed Governor, Frederick Mishkin in his JMCB-FDIC Lecture presented at the FDIC, Washington, D.C. on September 22, 2005 said:

> *The importance of finance to economic growth has also frequently been ignored by economists. For example, the leading undergraduate textbook on economic growth, Weill (2005) does not /discuss the link between finance and growth at all.*

The main reason was that initial finance theories like Modgillani Miller theorems and Efficient Market Hypothesis (developed by Eugene Fama and Kenneth French) were based on the assumption that markets are perfect and there are no frictions. But if these theories were correct then there was very little reason for financial markets to exist. However, later development showed that there were imperfections in the financial market and how various financial entities led to reduction of these imperfections. Fed Governor, Ben Bernanke in his speech (15 June 2007) said:

> *The blossoming of work on asymmetric information and principal-agent theory, led by Nobel laureates Joseph Stiglitz and George Akerlof and with contributions from many other researchers, gave economists the tools to think about the central role of financial markets in the real economy. For example, the classic 1976 paper by Michael Jensen and William Meckling showed that, in a world of imperfect information and principal-agent problems, the capital structure of the firm could be used as a tool by shareholders to better align the incentives of managers with the shareholders' interests. Thus was born a powerful and fruitful rejoinder to the Modigliani-Miller neutrality result and, more broadly, a perspective on capital structure that has had enduring influence.*

Since then there has been numerous research analyzing how financial systems help in developing economies. The research has not just looked at how finance helps economic activity but also social aspects like poverty, hunger etc. Like any research on a particular topic, the findings have been diverse and the consensus is that finance helps but the magnitude of impact differs.

Meaning of Financial Inclusion

What is Financial Inclusion? Rangarajan's committee on financial inclusion defines it as:

> *"Financial inclusion may be defined as the process of ensuring access to financial services and timely and adequate credit where needed by vulnerable groups such as weaker sections and low income groups at an affordable cost."*

The financial services include the entire gamut - savings, loans, insurance, credit, payments etc. The financial system has to provide its function of transferring resources from surplus to deficit units but both deficit and surplus units are those with low incomes, poor background etc. By providing these services, the aim is to help them come out of poverty. So far, the focus has only been on delivering credit (it is called as microfinance but is microcredit) and has been quite successful. Similar success has to be seen in other aspects of finance as well (discussed below)

Rationale for Financial Inclusion

Finance has come a long way since the time when it wasn't recognized as a factor for growth and development. It is now attributed as the brain of an economic system and most economies strive to make their financial systems more efficient. It also keeps policymakers on their toes as any problem in this sector could freeze the entire economy and even lead to a contagion.

The earlier research focused on how finance helps an economy. Now, research shows that financial inclusion is as important. The new avenue for research in finance is - making financial inclusion workable. Patrick Honohan (of Trinity College, Dublin) in his research developed an index to measure access to finance in 160 countries. If the index is put on a world map it can be clearly seen that those economies having higher indices are usually those, which we term as developed/advanced economies. It is not implied that financial inclusion alone has led to the development but is an important factor.

The policymakers have set up their task force/committees to understand how can financial inclusion be achieved including advanced economies like United Kingdom. India also set up a committee under the chairmanship of Mr. C.Rangarajan to suggest measures to increase financial inclusion (hence called the Rangarajan Committee on Financial Inclusion). The World Bank had organized a conference in March 2007 and has released a report titled "Finance for All" in November 2007.

The first 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 are:

- **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. These 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 paid to the moneylender and the person can never come out of the poverty.
- **High cost:** It has also been seen that poor living in urban areas don't utilize the financial services as they find financial services are costly and thus are unaffordable. Hence, even if financial services are available, the high costs deter the poor from accessing them. For example, to open a checking account in Cameroon, the minimum deposit requirement is over 700 dollars, an amount higher than the average GDP per capita of that country, while no minimum amounts are required in South Africa or Swaziland. Annual fees to maintain a checking account exceed 25 percent of GDP per capita in Sierra Leone, while there are no such fees in the Philippines. In Bangladesh, Pakistan, Philippines, to get a small business loan processed requires more than a month, while the wait is only a day in Denmark. The fees for transferring 250 dollars internationally are 50 dollars in the Dominican Republic, but only 30 cents in Belgium.
- **Non-price barriers:** Access to formal financial services also requires documents of proof regarding a persons' identity, income etc. The poor people do not have these documents and thus are excluded from these services. They may also subscribe to the services initially but may not use them as actively as others because of high distance between the bank and residence, poor infrastructure etc.
- **Behavioral aspects:** Research in behavioral economics has shown that many people are not comfortable using formal financial services. The reasons are difficulty in understanding language, various documents and conditions that come with financial services etc.

The above reasons show that it is not enough to assume that financial inclusion will happen on its own. Therefore, the onus has come on to the policymakers to provide the same. Dr. Vijay Kelkar, Chairman, Finance Commission in NP Sen Memorial Lecture at Hyderabad (dated 13/1/08) said financial inclusion is a quasi public good:

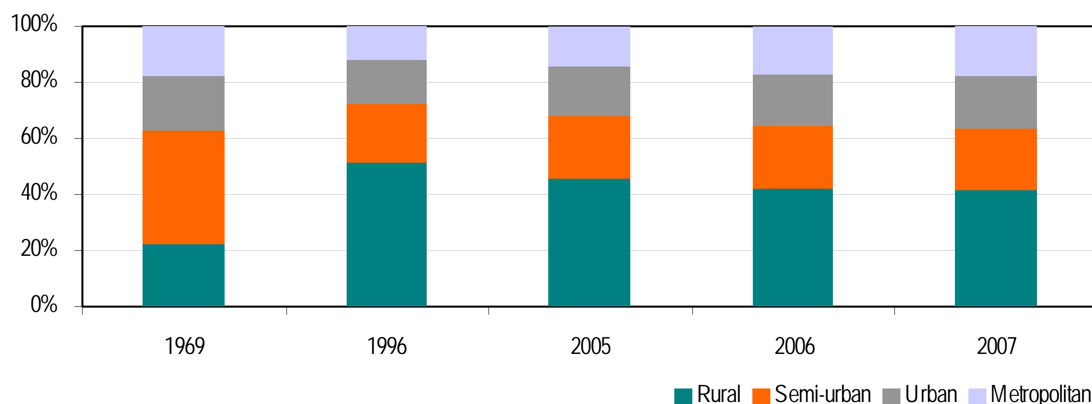
> *Increasingly, in developing countries access to finance is positioned as a public good, which is as important and basic as access to safe water or primary education. The pertinent question to ask here is whether 'Financial Inclusion' can be construed a public good? A good is considered a 'public good' if it meets the conditions of non-rivalness in consumption and non- excludability. The degree of 'publicness' in 'financial inclusion' maybe different from the stand point of a typical public good like say 'defense', but there is little doubt that financial inclusion meets the above two criteria to a large measure and to that extent is a "quasi public good".*
>
> *There are a number of positive externalities of financial inclusion. One of the important effects is one is able to reap the advantages of network externality of financial inclusion as the value of the entire national financial system increases. Yet another reason why Financial inclusion is a quasipublic good is that the consequent fuller participation by all in the financial system makes monetary policy more effective and thus enhances the prospects of non-inflationary growth.*

Financial Inclusion in India – in Statistics

Financial inclusion in developing economies is different than that of developed economies. In latter where inclusion is a minority, in former it could be a majority. Elaine Kempson in his research (2006) showed that in Sweden lower than two per cent of adults did not have an account in 2000 and in Germany, the figure was around three per cent. Another research by (Buckland et al (2005) showed that less than four per cent of adults in Canada and five per cent in Belgium, lacked a bank account. Therefore, it is also mentioned in academia that a better way to analyze financial inclusion in developing economies is to actually see financial exclusion.

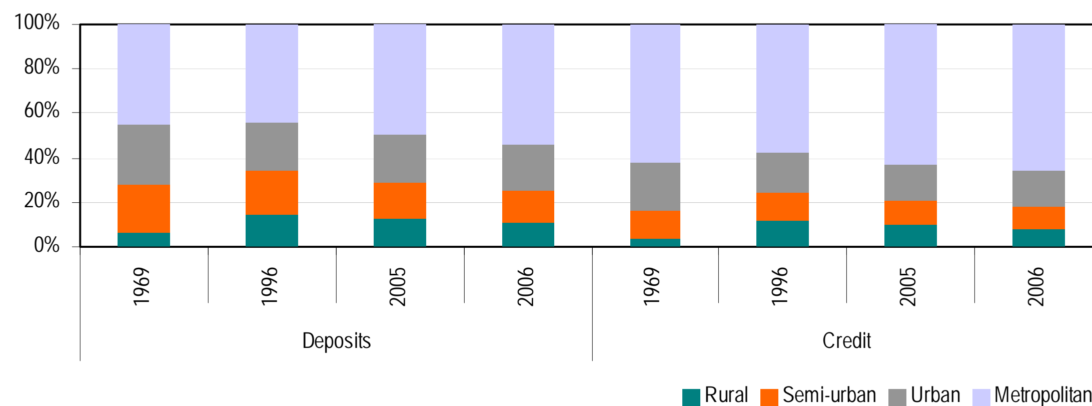
- **All India level:** Figure 1 shows that rural and Semi-urban offices constitute a majority of the Commercial Bank offices in India. Rural bank offices as a % of total have increased from 22% in 1969 to 41% in 2007. This is mainly because of the inclusive focus of the policymakers mentioned above. However, that is just one part of the story. If we look at figure 2, it can be seen that bulk of the deposits received and credit allocated is to the urban and metropolitan areas. Infact, the share of rural and semi-urban in deposits and credit has been declining. Table 1 provides further clarity providing a break-up of the deposit accounts. Both the deposit and credit accounts are lower in rural households than urban households. Hence despite the rural-push, the rural population has not come forward and avail even basic banking services (a fact mentioned in the section above - Rationale for Financial Inclusion).

Figure 1: Distribution of Bank offices in India



Source: Rakesh Mohan, RBI, IDBI Gilts Ltd.

Figure 2: Sources of Despoits and Credit in India (in %)



Source: Rakesh Mohan, RBI, IDBI Gilts Ltd.

Table 1: Number of Deposit and Credit Accounts in Scheduled Commercial Banks (% of Number of Households)

		1981	1991	1996	2001	2004	2005
Current Accounts	Rural	3.6	5.5	4.7	4.9	4.4	4.6
	Urban	15	23.4	24.1	19.2	17.5	18.3
Savings Accounts	Rural	59.6	137	129.8	123.3	126.8	131.5
	Urban	135.5	243.7	249.7	197.4	206.5	213.1
Term Deposits Accounts	Rural	22.9	41.8	45.5	52	48.3	45.7
	Urban	74.6	96.9	105	105.6	113.4	104
Credit Accounts	Rural	18	44.3	36	26.5	28.7	32.2
	Urban	15.1	29.9	27.1	28.4	42.5	50.2

Source: Rakesh Mohan, RBI, IDBI Gilts Ltd.

- **Regionwise:** Another way to analyse the financial inclusion is to see the region-wise distribution of the bank offices, credit and deposit ratios. Table 2 shows the population per office has increased in the rural areas of all the regions indicating lower financial deepening in rural areas. In urban areas the population per bank office has declined in all the regions except Western region.

  Despite the increase in financial deepening in the urban regions, the savings account per hundred persons has declined in all regions. Contrastingly, in the rural regions, savings account per hundred persons has increased in North-East, Central and Southern Regions, indicating banks in these rural regions have led to more financial inclusion than their counterparts in other rural regions and all urban regions. In Credit accounts per 100 persons, the situation is no different with the figure falling in all regions except Southern and Western regions in Urban India.

Table 2: Financial Inclusion region-wise

	1991	2005	1991	2005	1991	2005
	Total		Rural		Urban	
Population per Office						
Northern	11,002	12,257	10,771	13,043	11,571	10,941
North-East	16,870	26,227	16,335	22,158	21,169	20,318
Eastern	16,441	19,913	16,402	21,208	16,614	15,759
Central	15,786	19,518	15,153	20,264	18,745	17,297
Western	12,771	14,618	12,579	15,526	13,108	13,472
Southern	11,932	12,328	11,276	12,372	13,811	12,243
All-India	13,711	15,680	13,462	16,650	14,484	13,619
Deposits: Number of Savings Accounts per 100 persons						
Northern	40	38.3	30.1	29.7	62.6	55.4
North-East	17.8	17.6	16.1	16.4	28.4	24.2
Eastern	21.8	20.5	17.7	16.9	40	36.1
Central	23.8	24.5	21	22.1	34.7	32.9
Western	35.5	32.5	24.7	23.8	53.8	45.2
Southern	37	37.6	34.6	35.5	42.7	41.8
All-India	29.9	29.2	24.5	24.4	45.6	41.6
Credit: Number of Credit Accounts per 100 persons						
Northern	6.4	5.7	6.6	5.1	5.9	6.7
North-East	4.4	3.3	4.4	3.2	4.4	3.9
Eastern	6.6	4.2	7.2	4.2	4.3	4.3
Central	5.5	4.3	5.8	4.2	4.4	4.5
Western	5.7	7.5	6.2	4.2	4.8	12.2
Southern	11.8	14.2	13.6	12.7	7.6	17.4
All-India	7.3	7	7.9	6	5.5	9.8

Source: Rakesh Mohan, RBI, IDBI Gilts Ltd.

Financial Inclusion in India- Policy Perspective

Financial Inclusion has become a buzzword now but in India it has been practiced for quite sometime now. RBI has made efforts to make commercial banks open branches in rural areas. Priority sector lending was instituted to provide loans to small and medium enterprises and agricultural sector. Further special banks were set up for rural areas like Rural Cooperative Banks, Regional Rural Banks. The government also set up national level institutions like NABARD, SIDBI to empower credit to rural areas and small and medium enterprises. Appendix 1 presents the banking structure in India and one can see the emphasis on having banks in the rural sector.

Despite the rural policy-push, above statistics suggest majority of the population continues to be financially excluded. The efforts were further intensified by RBI and its Annual Policy (2005-06) mentioned:

- *RBI will implement policies to encourage banks which provide extensive services while disincentivising those which are not responsive to the banking needs of the community, including the underprivileged.*
- *The nature, scope and cost of services will be monitored to assess whether there is any denial, implicit or explicit, of basic banking services to the common person.*
- *Banks are urged to review their existing practices to align them with the objective of financial inclusion.*

This RBI focus led to a few key developments:

- **No-Frill accounts:** In November 2005, RBI asked banks to offer no-frills savings account which enables excluded people to open a savings account. Normally, the savings account requires people to maintain a minimum balance and most banks now even offer various facilities with the same. No-frills account requires no (or negligible) balance and is without any other facilities leading to lower costs both for the bank and the individual. The number of no-frills account has increased mainly in public sector banks from about 0.4 million to 6 million between March 2006 and March 2007. The number of No-frill accounts in private sector banks also increased from 0.2 million to 1 million in the same period. No significant increases were there in foreign banks. This is understandably so as majority of rural and sub-urban bank offices are in public sector banks.
- **Usage of Regional language:** The Banks were required to provide all the material related to opening accounts, disclosures etc in the regional languages.
- **Simple KYC Norms:** In order to ensure that persons belonging to low income group both in urban and rural areas do not face difficulty in opening the bank accounts due to the procedural hassles, the KYC procedure for opening accounts has been simplified for those persons who intend to keep balances not exceeding rupees fifty thousand (Rs. 50,000/-) in all their accounts taken together and the total credit in all the accounts taken together is not expected to exceed rupees one lakh (Rs.1,00,000/-) in a year.
- **Easier Credit facilities:** Banks have been asked to consider introducing General purpose Credit Card (GCC) facility up to Rs. 25,000/- at their rural and semi urban branches. GCC is in the nature of revolving credit entitling the holder to withdraw upto the limit sanctioned. The limit for the purpose can be set Based on assessment of household cash flows, the limits are sanctioned without insistence on security or purpose. The Interest rate on the facility is completely deregulated. A simplified mechanism for one-time settlement of overdue loans up to Rs.25,000/- has been suggested for adoption. Banks have been specifically advised that borrowers with loans settled under the one time settlement scheme will be eligible to re-access the formal financial system for fresh credit.
- **Other rural intermediaries:** Banks were permitted in January 2006, to use other rural organisations like Non-governmental organizations, self-help groups, micro-finance institutions etc for furthering the cause of financial inclusion.
- **Using Information Technology:** A few Pilot projects have been initiated to test how technology can be used to increase financial inclusion. Usha Thorat in her speech (June 19, 2007) pointed to a few measures:
    - Smart cards for opening bank accounts with biometric identification.
    - Link to mobile or hand held connectivity devices ensure that the transactions are recorded in the bank's books on real time basis.
    - Some State Governments are routing social security payments as also payments under the National Rural Employment Guarantee Scheme through such smart cards. The same delivery channel can be used to provide other financial services like low cost remittances and insurance.
    - The use of IT also enables banks to handle the enormous increase in the volume of transactions for millions of households for processing, credit scoring, credit record and follow up.

- **Financial Education:** RBI has taken number of measures to increase financial literacy in the country. It has set up a multilingual website in 13 languages explaining about banking, money etc. It has started putting up comic strips to explain various difficult subjects like importance of saving, RBI's functions etc. These comics explain myriad and complex concepts in an entertaining manner. The website states:

  The Reserve Bank of India has undertaken a project titled "Project Financial Literacy". The Objective of the project is to disseminate information regarding the central bank and general banking concepts to various target groups, including, school and college going children, women, rural and urban poor, defence personnel and senior citizens.

  The project has been designed to be implemented in two modules, one module in which Money Kumar will familiarise you with the role and functions of the Reserve Bank of India; and through the other module, Raju will introduce you to banking concepts.

Committee on Financial Inclusion (CFI)

Government of India constituted a Committee to enhance financial inclusion in India on 22 June 2006. The Committee presented its report in January 2008. The report has analyzed financial inclusion in detail and confirms the statistics presented above (Appendix 2).

CFI has initiated a mission called National Rural Financial Inclusion plan. It has set targets to increase FI in the country across regions and across institutions (banks, rural regional banks etc). It has suggested measures to address both, supply and demand constraints in increasing financial inclusion. The measures to address supply constraints aim to provide finance (via banks, micro-finance etc). Demand constraints imply that despite the supply people do not come forward because of number of factors (highlighted above). The report says:

> *It is widely recognized in economic literature that there are at least five different types of capital - physical (roads, buildings, plant and machinery, infrastructure), natural (land, water, forests, livestock, weather), human (nutrition, health, education, skills, competencies), social (kinship groups, associations, trust, norms, institutions) and financial. One of the causes as well as consequences of poverty and backwardness is inadequate access to all these forms of capital. Thus to look at financial inclusion in an isolated way is problematic.*

The report suggests measures to address demand constraints in all the other forms of capital as well. To address human capital it stresses on health and education; for natural capital - enhance access to land which could provide collateral; for physical capital- improve infrastructure; social capital- develop institutions like gram panchayats etc.

The interim report was presented before the Budget (2007-08). The Finance Minister

in the Budget decided to implement, immediately, two recommendations. The first was to establish a Financial Inclusion Fund with NABARD for meeting the cost of developmental and promotional interventions. The second was to establish a Financial Inclusion Technology Fund to meet the costs of technology adoption. The overall corpus for each fund was Rs.500 crore, with initial funding to be contributed by the Central Government, RBI and NABARD.

In the 2008-09-budget statement, the Finance Minister proposed two more measures: one to add at least 250 rural household accounts every year at each of their rural and semi-urban branches of commercial banks (including regional rural banks) and two, to allow individuals such as retired bank officers, ex-servicemen etc to be appointed as business facilitator or business correspondent or credit counsellor. The Finance Minister also proposed to expanding the reach of NABARD, SIDBI and NHB.

Some thoughts for policymakers

- **Applying behavioral economics:** The above-mentioned policies to address financial exclusion require huge effort and resources, thereby taking a longer time to address these imbalances. It has been pointed in our earlier research note (Subprime crisis for policymakers: Six Lessons and one request, dated 8/2/2008) that much of policymaking depends on classical economics. It assumes human beings as rational and so would respond to a policy like a rational person. However, this has not been the case and humans are shown to be irrational at most times. Dan Ariely (MIT Professor) in his recent book even says human behavior is 'predictably irrational'. The behavioral economic experts have shown how simple changes can lead to more financial inclusion.

  i) **Using Defaults:** Unlike what classical economics assumes, people seldom know what lies in their best interests and often end up making non-optimal decisions. The various experiments used to understand this behavior point that people do not select the best choice given the options. Hence, it is better to include a default amidst various options, with default being the choice that leads to a better choice. The default means if the consumer is unable to choose, the default option will be applicable.

This mechanism has been used to increase savings in many organizations. Earlier, employees had to opt in for the pension plan and most preferred not to opt for the pension plan. The choice was rephrased with help from Behavioral research. Unlike previously, employees had to select whether they wanted to opt for the pension plan, this time the employees were enrolled automatically in pension plans. So, if they didn't want to take the plan, they had to opt out of the plan. The default option had changed and the onus was now on the employee to opt out of the saving plans and most knowing the benefits, preferred to stay with the scheme. This led to increase in the pension savings in many organizations.

A similar mechanism could be deployed to increase usage of bank accounts in India. It is suggested that instead of giving cash transfers to the public, government should instead credit the bank accounts of the poor electronically. This will make people use their bank accounts. Now, this may work in developed economies but is going to be difficult to implement in developing economies like India. Nevertheless, it could be pilot-tested in a few urban regions.

It is to note that authorities in India have started testing this concept. It has been noted above that some State Governments have started routing social security and National Rural Employment Guarantee Scheme through the smart cards. The smart cards are then linked to the bank accounts. However, we do not know whether government has provided the electronic transfer as a default option or asking the person to opt for the card. Using the former should increase the application of the technology.

ii) **Simplify procedures:** It has been also seen in experiments that people are reluctant to go to banks as they are not clear of the directions, processes etc. BE experts suggest that measures like giving people a map showing the direction of the bank, asking for a time for appointment with the banker etc would lead more people to come to the bank. Another important finding is that poor people avoid banks because of complicated forms, procedures etc. Simpler structures will lead to higher footfalls to the banks. Instead of just calling it a saving account separate account could be opened called education account, vehicle account etc to enable a person to know the purpose of the saving.

These suggestions have come from research in developed economies. The emerging markets need to set up their own behavioral economics research centers. These centers will need to conduct surveys, conduct experiments etc to understand the behavioral nuances keeping people away from subscribing to various financial services.

- **Addressing Social issues:** This is a problem, which has not got as much mention in literature as much as it deserves. How do we address the various social issues in the rural/poor areas? The rural may not be approaching banks for fear of being looted on the way. Or they would want to keep a low profile and might not approach banks as that would send signal to the community that they have some money to spare. In the rural areas crimes are common and one has to be careful with the monies. So, may be financial inclusion will pick up if we address law and order. Another problem is that research has shown that women are better savers than men and financial inclusion is more likely to succeed with them in the fold. However, in rural areas women are not allowed to move around and their movement is limited to areas around the house. How do we get more women to participate in the movement?

  India has a diverse demographic profile which needs to be made a part of the financial inclusion policies, otherwise it could be a hindrance. This makes it even more important for policymakers to have their own behavioral research centers in emerging markets. The situation is very different from that in developed economies (where financial exclusion is a minority) and may require some adjustments to make the solution more workable. The Financial Inclusion report also shows how a few developing economies like Bangladesh, South Africa, Bolivia etc have achieved financial inclusion. The policymakers in these economies would have also faced similar kinds of problems. The research literature covers the various initiatives that have been successful in these regions. The research should also document how the social issues (if any) were addressed in these economies.

- **A broader approach than microcredit is needed:** The focus of policies have been so far on two things- one, to help people open more bank accounts and two, provide credit. The first makes people belong to the formal financial system and also gives them an identity. The second helps them get some financial capital and enables them to carry on some business activities to manage their livelihoods. However, this is too narrow a view. The poor people also need to invest their savings into financial products that get them higher returns than returns on savings account and fixed deposits. They also need other financial facilities like insurance, pension plans etc to manage risks and old-age. A World Bank Policy paper on finance said:

One of the criticisms against the microcredit movement has been the focus on credit. Most MFIs do not offer savings services beyond the compulsory savings linked to credit. However, the fact that the poor are capable of weekly repayments shows that the poor are capable of savings, even if it is only in small amounts. One of the reasons why the poor might not save in financial form might be the lack of appropriate products.

Rangarajan report has mentioned the importance of looking at financial inclusion in a holistic manner and has mentioned the need to look into insurance and remittance needs of the poor. Meanwhile, few efforts have been made in the financial sector to provide financial products to the poor. UTI Mutual Fund tied up with SEWA to provide pension plans to the latter's members.

The Mutual Funds have also been offering schemes that allow people to invest with just Rs 50/-. The schemes are called micro-SIP (Systematic Investment Plan) where a person would be required to invest regularly and minimum withdrawals are allowed. This will lead people to save regularly and withdraw judiciously. However, to get people to invest in these funds is also risky and the poor person is always interested in two questions: One, how much returns are guaranteed from this scheme? Two, is my money safe? If the funds can't give assured returns the poor has another option in form of a Fixed deposit and if the second condition isn't satisfied, he will not deploy his money. Hence, to make a holistic financial inclusion, removing demand constraints (financial literacy etc) will play a very important role.

- **Financial inclusion has to be in sync with Real-sector inclusion:** Though this point has been noted above, it needs separate mention. Financial inclusion alone will not be enough. The reforms in financial sector have taken center-stage in Indian polity with substantial media coverage to the same. It is true that access to finance is important but so is the access to real assets. The efforts have to be made to enable people to create real assets (plant, machinery, etc) with the access to various financial services.

It is widely felt Indian economy has changed but policies pertaining to financial sector are still very restrictive (some even term it as draconian). However, it is just one side of the argument. The reforms in financial sector have been much more progressive than the reforms in real sector.

Table 3 points to the rankings of the BRIC economies as per the Doing Business Report published by World Bank. The report shows how easy it is to do business in a country across various stages of business. The report covers 178 countries in its latest report. The table shows that India has a much lower ranking in getting credit than other countries but the ranking on other business parameters is still very low. India is ranked 36 in getting credit but overall ranking is 120. This implies it is much easier to get credit in India than other business processes like starting a business, licenses etc. Infact, latest report indicates that one area where India has been a major reformer is 'Getting credit'. Therefore, it is not fair to assume India will grow on the basis of reforms in the financial sector alone. The reforms in the real and financial sector need to go hand in hand.

Table 3: Doing Business Rankings in 178 countries

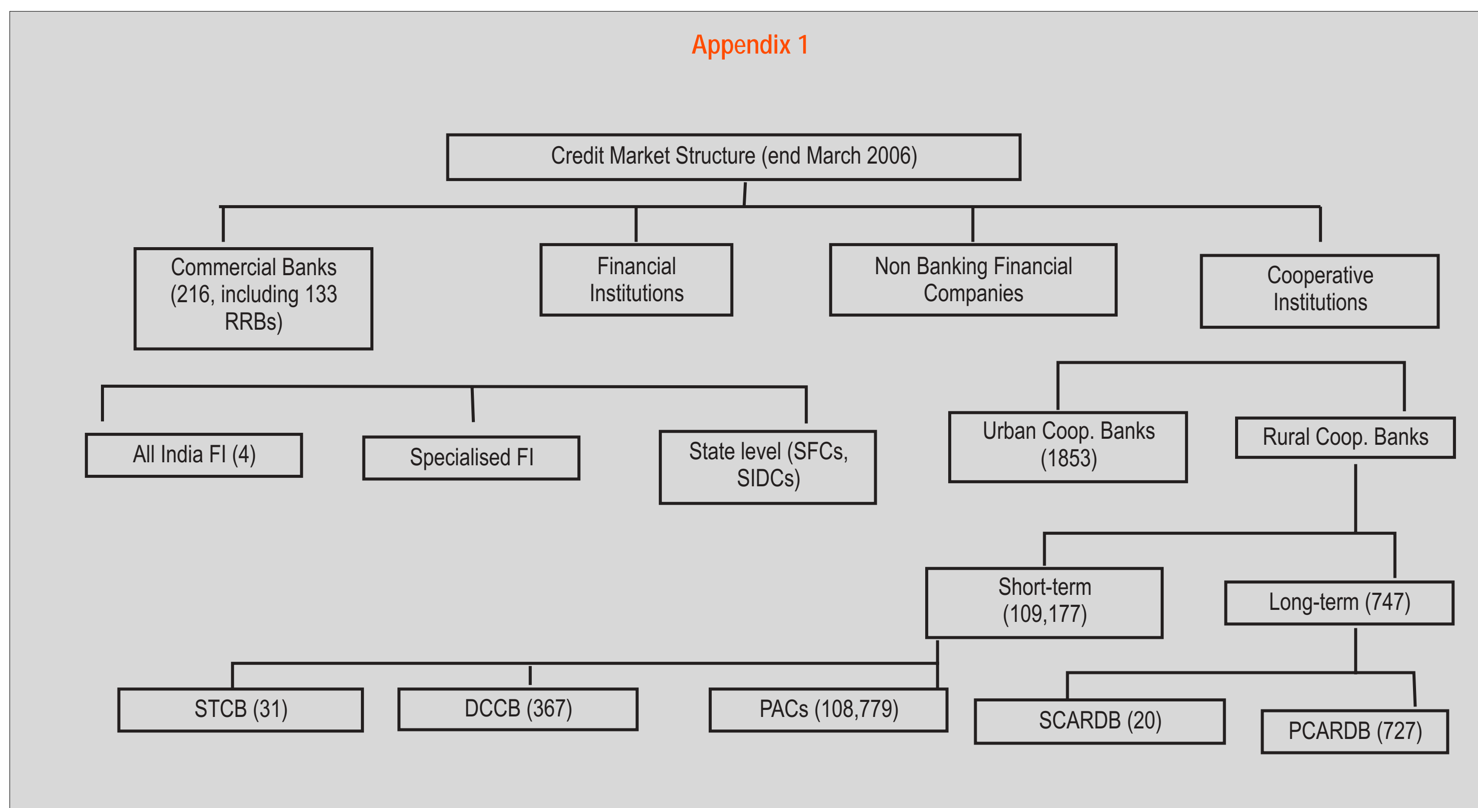
	India	China	Brazil	Russia
Starting a business	111	135	122	50
Dealing with licenses	134	175	107	177
Employing workers	85	86	119	101
Registering property	112	29	110	45
Getting credit	36	84	84	84
Protecting investors	33	83	64	83
Paying taxes	165	168	137	130
Trading across borders	79	42	93	155
Enforcing contracts	177	20	106	19
Closing a business	137	57	131	80
Doing Business Full Ranking	**120**	**83**	**122**	**106**

Source: World Bank, IDBI Gilts Ltd

Final Comments

The above research points to the importance of financial inclusion and highlights various policies that have been adopted in India to increase the same. There is another very important point to the entire exercise- the spirit of financial inclusion. A few commentators have also pointed to the similarity between sub-prime crisis and financial inclusion. The sub-prime market was originated to provide finance to people with weak credit histories (financial inclusion) enabling them to buy their homes (real-sector inclusion). In emerging markets as the population is largely financially excluded some analysts have commented that financial sector need to be careful.

The similarity is there but it was more to do with greed in US than the objective of financial inclusion. If the objective were inclusion (as is usually mentioned by the authorities), then we wouldn't have seen such far-reaching losses in the system. Financial Inclusion has far reaching consequences, which can help many people come out of abject poverty conditions. The financial markets must act responsibly and ensure that the spirit of financial inclusion is not breached in the future.



Appendix 2: Financial Inclusion Statistics in India

(a) General :

51.4% of farmer households are financially excluded from both formal / informal sources.

o Of the total farmer households, only 27% access formal sources of credit; one third of this group also borrow from non-formal sources.

o Overall, 73% of farmer households have no access to formal sources of credit.

(b) Region-wise :

o Exclusion is most acute in Central, Eastern and North-Eastern regions - having a concentration of 64% of all financially excluded farmer households in the country.

o Overall indebtedness to formal sources of finance alone is only 19.66% in these three regions.

(c) Occupational Groups:

o Marginal farmer households constitute 66% of total farm households. Only 45% of these households are indebted to either formal or non formal sources of finance.

o About 20% of indebted marginal farmer households have access to formal sources of credit.

o Among non-cultivator households nearly 80% do not access credit from any source.

(d) Social Groups :

o Only 36% of ST farmer households are indebted (SCs and Other Backward Classes - OBC - 51%) mostly to informal sources.

Analysis of the data provided by RBI thru' its Basic Statistical Returns reveal that critical exclusion (in terms of credit) is manifest in 256 districts, spread across 17 States and 1 UT, with a credit gap of 95% and above. This is in respect of commercial banks and RRBs.

As per CMIE (March 2006), there are 11.56 crore land holdings. 5.91 crore KCCs have been issued as at the end of March 2006, which translated into a credit coverage of more than 51% of land holdings by formal sources. Further data with NABARD on the doubling of agricultural credit indicates that agricultural loan disbursements during 2006-07 covered 3.97 crore accounts. Thus, there are different estimates of the extent of inclusion thru' formal sources, as the reference period of the data is not uniform. Consequently, this has had an impact on quantifying the extent of levels of exclusion.

Source: Committee on Financial Inclusion, IDBI Gilts Ltd

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