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Structured view of profitable financial inclusion models practiced by Indian banking industry

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Abstract
Financial inclusion offering all financial services to the rural poor is a mighty challenge and a complex task. As such, no single model can act as a panacea for this purpose. Banks and development agencies have to devise innovative methods and design models to suit the varying needs of rural poor. Group as well as community approach together with technological infrastructure, particularly Mobile Technology, would bring economies of scale for Banks. It needs no elaboration that the success of financial inclusion will finally depend on the whole hearted support of all concerned coupled with financial literacy/counseling of under-privileged. It is certain that financial inclusion will turn out to be a business opportunity in the long run.

Keywords: BC/BF, SHG, MFI, PACS, Post Offices, Hub-n-Sopke.

1. Introduction
1.1 Financial Inclusion
Financial Inclusion is the process of ensuring access to appropriate financial products and services needed by all sections of the society in general and vulnerable groups such as weaker sections and low income groups in particular at an affordable cost in a fair and transparent manner by mainstream institutional players.
In this connection, as per RBI guidelines
(i) A village is covered by banking service if either a bank branch is present or a BC is physically present or visiting that village.
(ii) Availability of Banking Services means availability of a Minimum of Four Products:
- A basic No-Frills banking account with Overdraft Facility.
- A Remittance Product for Electronic Benefit Transfer and other remittances.
- A Pure Savings Product ideally a recurring or a variable recurring deposit
- Entrepreneurial Credit such as General Credit Card, Kisan Credit Card.

2. Retrospective of Financial Inclusion
Provision of basic financial services is indispensable for tapping economic opportunities and development of any society. Unless all sections of the society are financially included, the growth will be lopsided which may lead to instability in the society. While Indian economy has been growing at the rate of over 8% for a decade or so, its fruit could not be enjoyed by majority of population. In a fast growing economy like ours, low level of financial inclusion is associated with high income disparities which are witnessed by the stint reality that still around 50% of people lack access to even basic financial services. Financial Inclusion as a concept is not new. Both the Government of India and Reserve Bank of India have been pursuing the goal of financial inclusion over several decades. To this end, the following Steps were taken in the Past:
- Co-operative Movement
- Nationalisation of Banks
- Lead Bank Scheme
- Opening of RRBs
- Service Area Approach
- Self Help Groups

3. Obstacles for Financial Inclusion
However, steps taken by Both the Government of India and Reserve Bank of India failed to produce the desired results mainly because of the following:
- Absence of Banking Technology.
- Absence of Reach and Coverage.
- Absence of Viable Delivery Mechanism.
- Not having a Business Model.

4. Extent of Financial Exclusion
As a consequence, the extent of financial exclusion in the country got staggered which can be corroborated from the following facts:
- Only 55% of the populations have deposit accounts and less than 10% have credit accounts with banks.
- India has the highest number of households (14.5 crore) excluded from Banking.
- There was only one bank branch per 14,000 people.
- 6 lack villages in India, rural branches of SCBs including RRBs number 33,495.
- Only 20% of the populations have any kind of life insurance and 10% of the populations have non-life insurance coverage.
- Just 18% have debit cards and less than 2% have credit cards.
- Again, financial exclusion varies across regions, social groups and asset holdings.

5. Structured Initiatives for F.I.
Financial Inclusion Plan for Banks: In our effort to achieve a sustained, planned and structured financial inclusion, in January 2010, all public and private sector banks were advised to put in place a Board approved three year Financial Inclusion Plan (FIP) and submit the same to the Reserve Bank by March 2010. These banks prepared and submitted their FIPs containing targets for March 2011, 2012 and 2013. These plans broadly include self-determined targets in respect of rural brick and mortar branches to be opened; business correspondents (BC) to be employed; coverage of unbanked villages with population above 2000 as also other unbanked villages with population below 2000 through branches/Bus/other modes; no-frill accounts opened including through BC-ICT; Kisan Credit Cards (KCC) and General Credit Cards (GCC); and other specific products designed by them to cater to the financially excluded segments. Banks were advised to integrate Board approved FIPs with their business plans and to include the criteria on financial inclusion as a parameter in the performance evaluation of their staff. The implementation of these plans is being closely monitored by the Reserve Bank.

(i) **Coverage of villages:** Banks have up to June 2011 opened banking outlets in 1.07lakh villages up from just 54,258 as on March 2010. Out of these, 22,870 villages have been covered through brick & mortar branches, 84,274 through BC outlets and 460 through other modes like mobile vans, etc.

(ii) **Opening of No-frills accounts:** Basic banking 'no-frills' account, with 'nil' or very low minimum balance requirement as well as no charges for not maintaining such minimum balance, make such accounts accessible to vast sections of the population were introduced as per RBI directive in 2005. As on June 2011, 7.91 crore No-frills accounts have been opened by banks with outstanding balance of Rs.5,944.73 crore. These figures, respectively, were 4.93 crore and Rs 4257.07 crore in March 2010.

(iii) **Small Overdrafts in No-frills accounts:** Banks have been advised to provide small ODs in such accounts. Up to June 2011, banks had provided 9.34 lakh ODs amounting to Rs.37.42 crore. The figures, respectively, were 1.31 lakh and Rs 8.34 crore in March 2010.

(iv) **General Credit Cards:** Banks have been asked to consider introduction of a General Purpose Credit Card (GCC) facility up to Rs. 25,000/- at their rural and semi-urban braches. The credit facility is in the nature of revolving credit entitling the holder to withdraw up to the limit sanctioned. Based on assessment of household cash flows, the limits are sanctioned without insistence on security or purpose. Interest rate on the facility is completely deregulated. As on June 2011, banks had provided credit aggregating Rs.2,356.25 crore in 10.70 lakh General Credit Card (GCC) accounts.

(v) **Kisan Credit Cards:** Kisan Credit Cards to small time farmers have been issued by banks. As on June 30, 2011, the total number of KCCs issued has been reported as 202.891akh with a total amount outstanding to the tune of1,36,122.32 crore.

6. Improving Policy and Regulatory framework
The usefulness as well as the risks of financial innovations, especially the credit derivatives, and the counter trading are part of debates of RBI. The RBI has been cautious in all these matters, partly reflecting its bank-dominated system, and its preference to concentrate on the flow of resources to government securities, and lending to the priority sector. No doubt, public policy tends to emphasize flow of resources to financial markets and to market-based instruments for several reasons. Since the performance of Indian banks, both in the private and public sectors, has been consistently high as well as improving, and returns to capital in equity markets reflected this, there was no compulsion to encourage banks to participate actively in financial innovations. Further, their positive contribution to overall efficiency and stability of output was acceptable in the Indian context.

RBI has undertaken a series of policy measures to boost Financial Innovation in order to provide banking to the unbanked and ensure economic growth. Some of the important ones are:

(i) **Relaxation on KYC norms:** Know Your Customer (KYC) requirements for opening bank accounts were earlier relaxed for small accounts in August 2005, simplifying procedure by stipulating that introduction by an account holder who has been subjected to full KYC drill would suffice for opening such accounts or the bank can take any evidence as to the identity and address of the customer to the satisfaction of the bank. During the year, it has been further relaxed to include job card issued by NREGA duly signed by an officer of the State Government or the letters issued by the Unique Identification Authority of India containing details of name, address and AADHAAR number.

(ii) **Simplified branch authorisation**: To address the issue of uneven spread of Bank branches, since December 2009, domestic scheduled commercial banks are permitted to freely open branches in Tier 3 to Tier 6 centres with 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 centres without the need to take permission from Reserve Bank in each case, subject to reporting.

(iii) **Pricing has been made free**: Banks have been given the freedom to price their advances as well as their Savings Bank Deposits.

(iv) **Liberalisation of Business Correspondents Model**: In January 2006, the Reserve Bank permitted banks to engage business facilitator and business correspondent (BC) as intermediaries for providing financial and banking services. The BC model allows banks to provide door step delivery of services especially 'cash in - cash out' transactions at a location much closer to the rural population, thus addressing the last mile problem. The list of eligible individuals/entities who can be engaged as BCs is being enlarged from time to time. For-profit companies have also been allowed to be engaged as BCs. You would be happy to know that as on March 31, 2011, domestic commercial banks have reported deploying 58,361 BCs, providing banking services in 76,081 villages.

(v) **Opening of branches in unbanked rural centres**: To further step up the opening of branches in rural areas so as to improve banking penetration and financial inclusion rapidly, the need for opening of more brick and mortar branches, besides the use of BCs, was felt. Accordingly, banks have been mandated in the Monetary Policy Statement - April 2011, to allocate at least 25 per cent of the total number of branches to be opened during a year in unbanked rural centres.

7. Achievements so far: While Banks have been acting as per guidelines prescribed by the Government and the RBI, the progress in this area is miniscule, that too, limited to opening of 'No Frills' accounts only, when assessed in the backdrop of the scope and need associated with this programme. The reasons for this slow progress need not far to seek which can be shortlisted, as under:

- Perceived more as an obligation than a business opportunity.
- Lack of appropriate Business Models for FI activity for Banks, Technology Providers and BCs.
- Inadequate Physical capacity of Banks including RRBs vis a vis the requirement.

It can thus be inferred that unless the Banking industry drives the activity on its own, Financial Inclusion may never be a real success. Establishing appropriate Business Models through the involvement of all stakeholders is, therefore, critical in making Financial Inclusion a reality. The Model must generate reasonable profits to make itself a self-sustaining one as otherwise it will always be perceived as an obligation on the part of Banks and will not be taken up with required zeal.

8. Pillars for Financial Inclusion Model:

When the needs of the poor are properly understood, it would be easier to design the appropriate model of financial inclusion by Banks. To this end, the following factors need consideration:

a) **Convenience -** in being able to transact where they live and work,

b) **Trust -** in putting their money with organizations that seem to care for them and who they feel will be there for them at the time of their needs,

c) **Affordability -** being able to transact in small amounts at reasonable cost.

9. Profitable Financial Inclusion Models

A. Self Help Group (SHG) Linkage Model:

Despite progress in banking networks and financial outreaches across the country, of late, it is noticed that there is relative decline in supply of credit in rural areas and this, in turn, has posed a serious challenge before the Indian formal financial system to achieve the financial inclusion in true spirit. SHG bank linkage model bunched by NABARD in 1992 can very well be considered for this purpose. It facilitates extending all the required financial services to unbanked areas. This model is widely accepted as the most successful micro finance model. On the issue of Si-iGs' role in inclusion, it is felt that SHGs are far better equipped to achieve the objectives of inclusion and as such, they should be suitably supported. This underscores the role of SHGs and their members in the inclusion dynamics and their number is too large to be ignored. RBI has thus permitted all Banks to appoint authorized functionaries of well-run SHGs which are linked to Banks as BCs. Banks ha-..e to seize this opportunity to increase their outreach for financial inclusion through the channels of SHGs. This would also help Banks to address the issue of viability of BCs as the volumes that could be reached, would be much highev. It is pertinent to mention that NABARD has also extended financial support to RRBs for capacity building and training of the authorized functionaries of SHGs to be appointed as BC/BF for financial inclusion.

B. Business Correspondent (BC)/ Business Facilitator (BF) Model

The predominant model adopted by the banks so far has been the branchless through Business Correspondents. Most of the banks that have employed BCs have appointed Section 25 Companies / Societies as BCs. Further, almost all the Section 25 Companies appointed as BCs have been floated by Technology Service Providers who have provided the Smart Card or Biometric solutions for the account opening. Many of the BCs have reported huge losses and have closed down operations. The model can be successful only if sufficient businesses are generated. As almost all BC transactions are cash based, they suffer from increased cost and operational risk besides logistics of handling large volumes of cash. Illiterate clients perceive BCs as Banks and their agents went about claiming to be Bank employees. As a result, there were a number of frauds leading to numerous disputes and litigation. There has also been a mismatch between revenue projected and cost incurred for BC operation resulting in non-viability of the model. Commissions paid by Banks to BC are not considered adequate for a viable business model. Banks utilize BCs only for opening of no-frills accounts, through which various payments solutions as NREGA, pension, etc. are routed. Banks have to provide a wide range of services such as suitable small savings, micro credit, micro insurance, small value remittances, etc. for the model to be viable. A few Loan products can also be thought of under the close surveillance of the Banks. In all, Banks have to develop models with customer centric approach to make BC model a viable one.

C. Micro Finance Institute (MFI)

The Microfinance Sector which had witnessed remarkable growth in the last few years, has decelerated now due to the recent developments, particularly in Andhra There are lots of changes taking place in the sector with MFIs trying to reposition themselves to achieve economy of scale. The client acquisition ratio of MFI has declined sharply due to the political interferences in the sector, the interest cap of Malegam Committee, hesitation of Banks in funding MFIs on account of uncertainties, non-profitability of operations, fall in recovery rates, etc. Over time, the stronger and fitter MFIs may survive and they will find their own space in the financial sector. However, the model to be effective, successful and viable, RBI needs to change the rules and regulations governing MFIs. The ideal and viable model will be one where the MFIs will be sponsored by Banks including RRBs. These outfits will work in all the unbanked areas under the close supervision of the sponsoring Bank. They may also be allowed to accept deposits at the market rates, to sell mutual fund and insurance products, etc. in addition to their main activity of lending. This will help them to charge lower rates for loans. MFI model will thus become a real game changer.

D. Primary Agricultural Credit Societies (PACS)

There are nearly one lacks Primary Agricultural Credit Societies (PACS) with membership of over 14.50 Crore, located in the rural hinterlands of the country. PACS are ideally suited to provide a comprehensive range of services like savings, credit, insurance and remittances to their clients, provided there is a workable tie up with the higher tier cooperative banks. Thus, their role in financial inclusion cannot be underestimated. Consequent upon implementation of the recommendations of Vaidyanathan Committee, many PACS are well poised to take up viable business activities. On realizing their importance, a few States have started utilizing their services for all activities related to agriculture. In a few states, PACS have started extending remittances, insurance, etc. NABARD has. started supporting PACS for computerization. It would be, therefore, feasible to have CBS for integration of technology based inclusion models for PACS as well. The model would also improve the viability of these institutions.

E. HUB & SPOKE Branch Model

No model can be better than a Brick & Mortar branch banking with full-fledged facilities. However, because of the cost implications, it may not be feasible for the present. To this end, the ideal model would be Hub n Spoke Model. While Hub is one of the existing/new full-fledged Branch, Spokes are 'N' number of Mini Branches in and around the Hub and are linked to it. Mini Branch can work in self-service mode or in an assisted mode. While the former is suitable for urban FI, the latter is for rural FI. Self-service mode includes ATM, Kiosk, Internet Banking, Phone Banking (IP based), e-Form Channel (Smart Account Opening), etc. Teller /SWO assisted mode requires Desktop/Laptop, Cash Recycler (safe), Printer/Scanner, etc. In this particular model, while a few services can be on real time basis, others like application for opening of accounts, loan, MF / Insurance products, etc. can be procured for processing at Hub subsequently. To make this model cost effective and operationally efficient, the facilities can be provided with the help of mobile vans.

F. Post Offices

The Expert Committee on harnessing the India Post Network on Financial Inclusion came up with a wide range of recommendations on the role of post offices in financial inclusion by entering into partnership with Banks, upgrading the technological infrastructure, modernizing transaction platforms, developing low cost small ticket remittance mechanisms and facilitating electronic fund transfers. The Committee also recommended for are view of the role of post office as an agent of GOI and to enable the institution to act as its own account in the financial inclusion space. India Post, with a network of more than 1.55 lacks post offices — mostly in rural areas is in the process of getting Cabinet approval for Bank linkage. Since post offices already accept deposits, converting into a full-fledged bank branch may be quite feasible. The department proposes to acquire ATMs in a bid to modernize its operations. India Post is reportedly finalizing tie up with various banks. Some banks have already forged partnerships with post offices for expanding their outreach. SBI and India Post have entered into a partnership in which, postmen will act as BCs for SBI in more than 12,000 villages. They will be collecting deposits, offer small credits and remittance facilities in those villages.

10. Conclusion

Financial Inclusion is the road which banks in India needs to travel towards becoming a major player. Banks that have global ambitions must meet local aspirations. Financial access will also attract global market players to our country that will result in increasing employment and business opportunities. As we have all recognized, technology is a great enabler and has to act as a ladder to achieve the ultimate goal of providing financial services to the financially excluded. A line of caution here is that in order to serve millions of our poor villagers, what we need is "Technology with a human touch". Banks should, therefore, take extra care to ensure that the poor are not driven away from banking because the technology interface is unfriendly. This requires training the banks' frontline staff and managers as well as Business Correspondents on the human side of banking. Sufficient provisions should be in built in the business model to take care of customer grievances. It can be summarized that the "*The future lies with those who see the poor as their customers*" as commerce for the poor is more viable than the rich. In this task, a concerted and structured effort by all stakeholders is necessary.

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