ITEM4 - Financial inclusion: Lessons between the South and the North
April 11 & 12, 2013, Paris, France

Presentation of the paper:
Financial Inclusion: Is it a Commercial Model or Social Model
Financial Inclusion

Based on the fundamental principle of 5A’s of ensuring Adequacy, Availability of financial services, Awareness of such services, Affordability and Accessibility of the financial products through a combination of delivery channels and technology enabled services and processes.
Reserve Bank of India (RBI) adopts two approaches to achieve Financial Inclusion,

1. the minimalist approach – availability of basic financial products and services.

2. the expanded approach – availability of ancillary financial products such as general insurance, health insurance, micro-pension, housing finance and mutual fund. Both the approaches form a broader context of economic inclusion
Objectives:

To identify the need for financial inclusion in India and compare the Financial Inclusion index of India with the indices of developed countries like European countries

To Study the challenges to India in financial inclusion

To explain how commercialization occurs resulting in the loss of social inclusion
Research Methodology:

The study adopts the financial inclusion methodology as given by Sarma (2008) in his working paper on Index of Financial Inclusion. On the indicators: banking penetration (BP-pi), availability of the banking services (BS-ai) and usage of the banking system (BU-ui) – we can represent a country i by a point (pi, ai, ui) in the three dimensional Cartesian space, such that 0 ≤ pi, ai, ui ≤ 1. The data is available in the Global Findex, for the year 2011. The three dimensions of financial inclusion are taken viz., banking penetration (pi), number of bank accounts can be used as a proportion of the total population as an indicator of this dimension, availability (ai) - the number of ATMs, and the number of bank branches per 1000 population and usage (ui) and for financial (banking) penetration dimension, the data used is “Bank Deposit Accounts” including checking (or current), savings, and time deposit accounts for business, individuals and others.
Phase I (1950-70): Consolidation of the Banking Sector and Facilitation of Industry and Trade
Phase II (1970-90): Focus on channelling of credit to neglected sector and weaker sections.
Phase III (1990-2005): The focus was on strengthening the financial institutions as part of financial sector reforms.
Phase IV (2005-2010): Financial Inclusion was explicitly made as a policy objective through its Annual Policy Statement of the Reserve Bank 2005-06.
Phase V: National Financial Inclusion Plan 2010-2015
| **Commercial bank branches per 1,000 km²** | 30.43 | **Commercial bank branches per 100,000 adults** | 10.64 |
| **ATMs per 1,000 km²** | 25.43 | **ATMs per 100,000 adults** | 8.90 |
| ** Outstanding deposits with commercial banks (% of GDP)** | 68.43 | **Outstanding loans from commercial banks (% of GDP)** | 51.75 |
| **Deposit accounts with commercial banks per 1,000 adults** | 953.06 | **Loan accounts with commercial banks per 1,000 adults** | 142.02 |
| **Household deposit accounts with commercial banks per 1,000 adults** | 853.02 | **Household loan accounts with commercial banks per 1,000 adults** | 20.62 |
Algebraically,

\[ IFI = 1 - \sqrt{\frac{(1 - p_i)^2 + (1 - a_i)^2 + (1 - u_i)^2}{3}} \]
Waves of Inclusion: Commercial or Social?

In the European context, microcredit, the provision of loans for microenterprise development, predominates. In this context, microcredit is one part of the microenterprise development agenda as it refers to provision of micro-loans for microenterprises. The Report on “From Financial Inclusion to Social Inclusion” focuses on microcredit and business creation as a tool for social and financial inclusion.

- A: MF for inclusion through self-employment
- B: MF to support services to self-employed and adapt legal environment
- C: MF for improving personal financial capacity and fighting overindebtedness
- D: MF for inclusion through personal microcredit, housing or consumer loans
When we talk about India, the presence of MFI has three distinct waves. The first wave was the Grameen Bank model through which poor were reached. The second wave was when these MFIs reached scale and sought methods to morph into commercial organisations. The third wave was when MFIs started looking at microfinance for business. From 2002 onwards, MFIs started implementing a language of transformation.
<table>
<thead>
<tr>
<th>Region</th>
<th>MPI (average)</th>
<th>MPPI (average)</th>
<th>Financial Inclusion Results</th>
</tr>
</thead>
<tbody>
<tr>
<td>Northern Region</td>
<td>.27333</td>
<td>.62333</td>
<td>financial inclusion results in elimination of poverty</td>
</tr>
<tr>
<td>North Eastern Region</td>
<td>1</td>
<td>1.65</td>
<td>financial inclusion results in elimination of poverty</td>
</tr>
<tr>
<td>Eastern Region</td>
<td>1.015</td>
<td>0.8125</td>
<td>financial inclusion does not result in elimination of poverty</td>
</tr>
<tr>
<td>Central Region</td>
<td>.5075</td>
<td>0.3725</td>
<td>financial inclusions do not result in elimination of poverty</td>
</tr>
<tr>
<td>Western Region</td>
<td>.7666</td>
<td>1.18</td>
<td>financial inclusion results in elimination of poverty There is social Inclusion</td>
</tr>
<tr>
<td>Southern Region</td>
<td>2.258</td>
<td>3.248</td>
<td>financial inclusion results in elimination of poverty There is social Inclusion</td>
</tr>
<tr>
<td>India</td>
<td>.970066</td>
<td>1.31438</td>
<td>financial Inclusion results in elimination of poverty to certain extent</td>
</tr>
</tbody>
</table>
Limitations

• Only supply-side information (macro) is used and not demand side information

• Apart from IMF’s FAS, there are surveys available-Global payment systems survey, MIX, BankScope, FinStats, IMF’s IFS, IMF’s Financial Soundness indicators

• Demand-side: Year-long household survey (financial diaries) is not available for India.

• Only three indicators endorsed of IMF used to analyse

• Individual Banks’ information are not comparable.
Conclusions / Recommendations

EU is being directed towards social inclusion
However, India has just started working and in the second stage of financial inclusion
A link has to be built between financial inclusion and social inclusion