# Financial Inclusion: A way to sustainable growth

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**Abstract**

Inclusive growth is possible only through proper mechanism which channelizes all the resources from top to bottom. Financial inclusion is an innovative concept which makes alternative techniques to promote the banking habits of the people. However for attaining the objectives of inclusive growth there is a need for resources, and for resource generation and mobilization financial inclusion is required. It plays a very crucial role in the process of economic growth. The present paper focuses on to understanding inclusive growth phenomenon its need and financial inclusion as an instrument to attain it. The research has been done using secondary data source. We use the data to benchmark financial inclusion-the share of the population that uses formal financial services in developing countries around the world, and to investigate the significant country and individual-level variation in use of formal and informal financial systems. The study also presents the extent of inclusion among selected countries.

**Keywords**: Inclusive & Sustainable Growth, Financial Inclusion

## 1. Introduction

Growth needs to be sufficiently inclusive if its benefits have to be shared among all or else the growth process itself shall be jeopardized and derailed. In order to achieve 'inclusive growth', both State based interventions and Market based instruments are required. However, an important limitation of 'market' as an institution is that it is '*not wealth neutral'* and given this perspective, the concept of 'Financial Inclusion' fits in. Financial Inclusion needs to be seen as an instrument that would move the wealth effect towards a neutral domain. Thus, as a concept Financial Inclusion has the potential to contribute substantially towards 'inclusive growth'. Inclusive growth as a strategy of economic development has received renewed attention in recent years owing to rising concerns that the benefits of economic growth have not been equitably shared. Empirical evidence shows that countries with large proportion of population excluded from the formal financial system also show higher poverty ratios and higher inequality. Today the term 'bottom of the pyramid' refers to the global poor most of who live in the developing countries. These large numbers of poor are required to be provided with much needed financial assistance in order to sail them out of their conditions of poverty. Accordingly, there is felt a need for policy support in channeling the financial resources towards the economic upliftment of resource poor in any developing economy.

The World Bank financial access 2009 looked at financial access differences between developed and under-developed countries. Their findings were very distinctive. They discovered (obviously) that the developed European countries were better exposed to financial services and accounts ownership. They collected some set of indicators of financial access in countries around the world. Such indicators included the number of deposit accounts and loans, the number of deposit clients and borrowers, and the number of financial access points, such as branches, agents, and automated teller machines.

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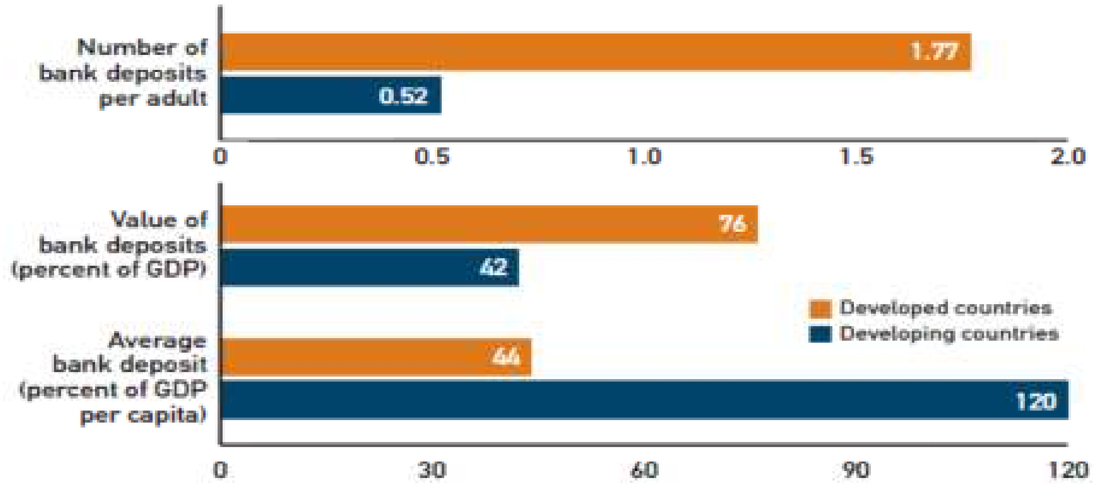


Figure 1: Financial Access of Developed and Developing Countries
Source: World Bank Financial Access (2009)

## 2. Review of Literature

In banking worldwide, the service environment is becoming very competitive and is featured by many demanding customers and banks are seeking various ways of getting more unreached areas. Even so, many parts of the underdeveloped world do not share a similar view in terms of the availability of banking services at their disposal. In some areas of concern, there is the issue of long distances between communities and bank branches and also the unavailability of cheaper banking facilities. Some of them incur some amount of cost on wanting to have access to ATMs or other banking services. Sometimes, the issue could be that some people do not see the need for these services and so banks have to device several means of easing off the pressures of accessing these services. Therefore, the quality of service becomes an integral part of the financial institutions attempt to reach the unbanked. The attitudes of banks and non-banking institutions should be channelled towards seeing these unreached areas as a competitive edge as they constitute a majority of the population in underdeveloped areas. There is a need to further look into the matter of financial exclusion/inclusion, service quality and strategies that will help in customer outreaching.

According to **Kendall et al., (2010)**, in developing countries there is an estimate of 0.9 accounts per adult and 28% banked adults. He stated that the rise of financial inclusion as an important policy goal is due in part to mounting evidence that access to financial products can make a positive difference in the lives of the public. The European Commission Manuscript 2008 defines financial exclusion as a process whereby people encounter difficulties accessing and/or using financial services and products in the mainstream market that are appropriate to their needs and enable them to lead a normal social life in the society in which they belong. They also stated that there is some widespread recognition that financial exclusion can be referred to as part of a much wider social exclusion, faced by some groups who lack access to quality essential services such as jobs, housing, education or health care.

**Kempson and Whyley (2000)**, in their study, established six types of financial exclusion:

- **Physical access exclusion**: This, they stated, is brought about by the closure of local banks or building societies and lack of reliable transport to reach alternatives.
- **Access exclusion**: This type of access is restricted through risk assessment, with people being denied a product or service as they are perceived to be high risks.

- **Condition exclusion**: This is when conditions are attached to products or services thereby making them inaccessible to some.
- **Price exclusion**: This occurs when products are available but at a price that is unaffordable.
- **Marketing exclusion**: where sales and marketing activity is targeted on some groups, or areas, at the expense of others.
- **Self-exclusion**: when individuals do not seek financial products and services for reasons including fear of failure, fear of temptation or lack of awareness.

**Kempson (2006)** gave some explanations to the reasons why people are financially excluded. He said that these reasons could vary from country to country. He stated the importance of bank required identification and documents, the terms and conditions of bank accounts, levels of bank charges, physical access and cultural barriers in financial inclusion.

**Kempson (2006)** explained that Different banks across the world have different terms and conditions to opening accounts with them. Such terms as amount of money to open with, the amount of minimum/maximum balance etc. This goes a long way to having an effect on the extent of financial inclusion. These different types of terms and conditions can deter or prevent people with low incomes to open an account.

**OFT (1999, cited in Wallace and Quilgars, 2005)** stated that the fear of getting overdrawn and incurring high bank charges was a major discouraging factor for many people on low or modest incomes to obtaining an account.

"A credit union also has an obligation to educate their members in effective and responsible management of money, and credit unions offer debt and money advice to their members alongside financial goods and services and insurance products" **(Credit Unions Act 1979, cited in Commission of Rural Communities, 2007)**. The absence of this will inevitably lead to an exclusion from financial facilities and services.

**Tagoe et al., (2006**) gave several success factors as essential for a good and well conclusive inclusion of individuals in the utilization of financial facilities and services. Having access to financial services requires one to be well knowledgeable about the services at stake. There is a high requirement for the availability of basic banking services.

**Basu, Priya (2005)** in her study stated that the strategies that were designed to increase access to finance for the poor have not delivered their intended outcomes. It is not just policies, but institutions and markets that need to be transformed so as to improve the efficiency of the formal rural finance sector.

However some of findings show that the programme is not reaching the bottom poor people and the group loans are utilized for non-income generating activities.

## 3. Research Methodology

The type of research is descriptive in nature. The present study is aimed at reviewing the extent of financial inclusion across some developing countries of world.

### 3.1 Objectives of the study:

- To understand how financial inclusion act as an instrument to attain inclusive growth.
- To know the extent of financial inclusion in selected developing countries.
- To ascertain India's position among selected countries in terms of financial inclusion.

### 3.2 Scope of the Study:

The study is confined to developing economies like India, China, Sri Lanka, South Africa, Russian Federation and Brazil. However, some of the facts and figures presented in the study give the picture of global scenario.

**3.3 Data Collection:**

The data collected for the study is comprised of secondary data only which has been collected from various websites and published sources.

## 4. Financial Inclusion

In simple terms, Financial Inclusion means provision of banking services at an affordable cost to the vast sections of disadvantaged and low-income groups. These include access to savings, credit, insurance, payments and remittance facilities by the formal financial system to those who tend to be excluded. Importance of financial inclusion arises from the problem of financial exclusion of nearly 3 billion people from the formal financial services across the world. According to Transact, the national forum for financial inclusion, 2007, "Financial inclusion is a state in which all people have access to appropriate, desired financial products and services in order to manage their money effectively. It is achieved by financial literacy and financial capability on the part of the consumer and financial access on the part of product, services and advice suppliers." The effort of all institutions both financial and developmental is aimed at encouraging inclusion. The use and access of financial services has been at the stem of study for major regulatory financial institutions. Some developed countries report annually on the level of access of finance for economic and social developments. Technology is gaining grounds on banking services through the use of ICT devices. Some of the various ways of encouraging and ensuring financial inclusion is in the circulation of deposit accounts, loans, insurance and automated electronic transfers.

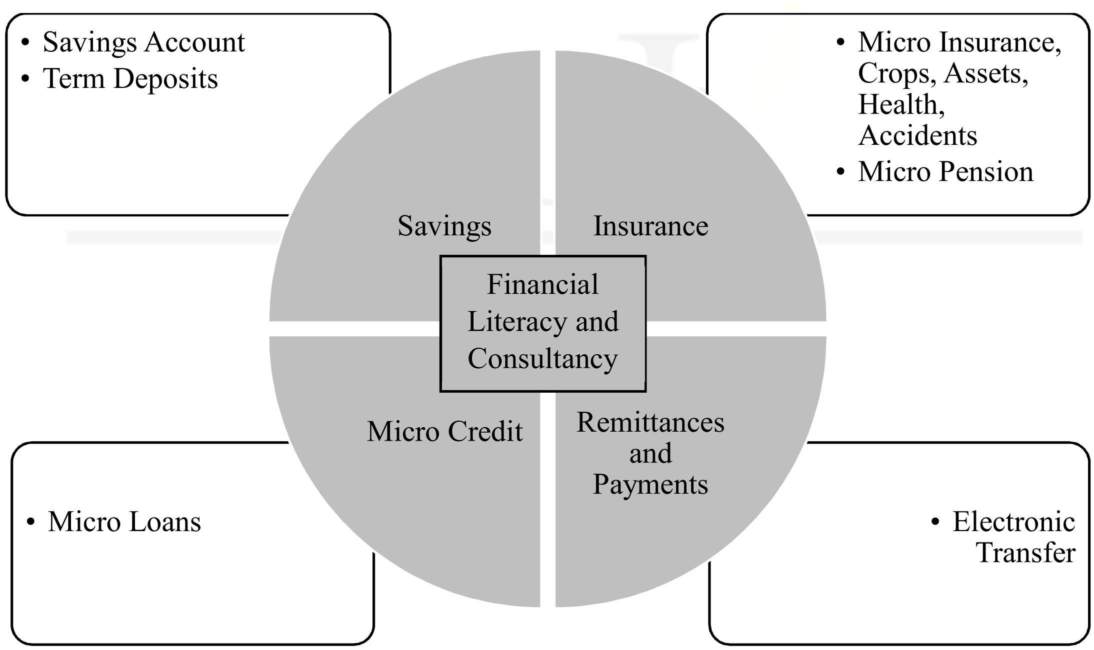


**Figure 2. Components of financial inclusion**

## 5. Global Scenario

The level of financial inclusion varies widely around the world. Globally, about 50 percent of adults have a bank account, while the rest remain unbanked, meaning they do not have an account with a formal financial institution. Not all the 2.5 billion unbanked need financial services, but barriers such as cost, travel distance, and documentation requirements are critical. For example, 20 percent of the unbanked report distance as a key reason they do not have an account. The poor, women, youth, and rural residents tend to face greater barriers to access. Among firms, the younger and smaller ones are confronted by more binding constraints. For instance, in developing economies, 35 percent of small firm sreport that access to finance is a major obstacle to their operations, compared with 25 percent of large firms in developing economies and 8 percent of large firms in developed economies.

**Financial Inclusion: A Cross Country Analysis of some Developing Economies**

Developing economies are defined according to their gross national income i.e. GNI per capita per year. Countries with GNI of US $ 11,905 and less are defined as developing economies. Selected developing economies are compared on basis of various financial indicators which determines their extent of exclusion/ inclusion.The indicators of financial inclusion measure how people save, borrow, make payments and manage risk. The data related to savings, borrowings, and some other financial indicators is presented and analysed below in following tables and through their graphical representation.

**Table 1:Adults with an account at formal Financial Institution (%age)**

| Characteristics | | India | China | Sri Lanka | South Africa | Russian Federation | Brazil |
|---|---|---|---|---|---|---|---|
| By Gender | Male | 43.73 | 67.58 | 69.98 | 56.38 | 48.78 | 61.1 |
| | Female | 26.49 | 60.00 | 67.23 | 51.02 | 47.70 | 51.02 |
| By Education | Primary or Less | 30.51 | 56.73 | 62.88 | 42.25 | 24.19 | 47.15 |
| | Secondary or more | 59.46 | 81.87 | 76.41 | 58.32 | 54.66 | 63.83 |
| By Rural/urban residence | Rural | 33.14 | 58.01 | 67.71 | 46.34 | 45.52 | 51.90 |
| | Urban | 40.95 | 82.10 | 72.41 | 67.70 | 52.99 | 59.30 |
| By Income | Low | 27.11 | 47.11 | 58.26 | 41.09 | 40.24 | 41.23 |
| | High | 44.41 | 75.39 | 77.92 | 62.89 | 53.92 | 65.60 |
| By Age | Young(15-24 years) | 27.30 | 65.29 | 68.71 | 40.76 | 32.81 | 36.34 |
| | Older (25+ years) | 38.02 | 63.28 | 68.47 | 59.09 | 51.85 | 61.98 |

Source: Compiled from Global Financial Inclusion Database, World Bank, 2012

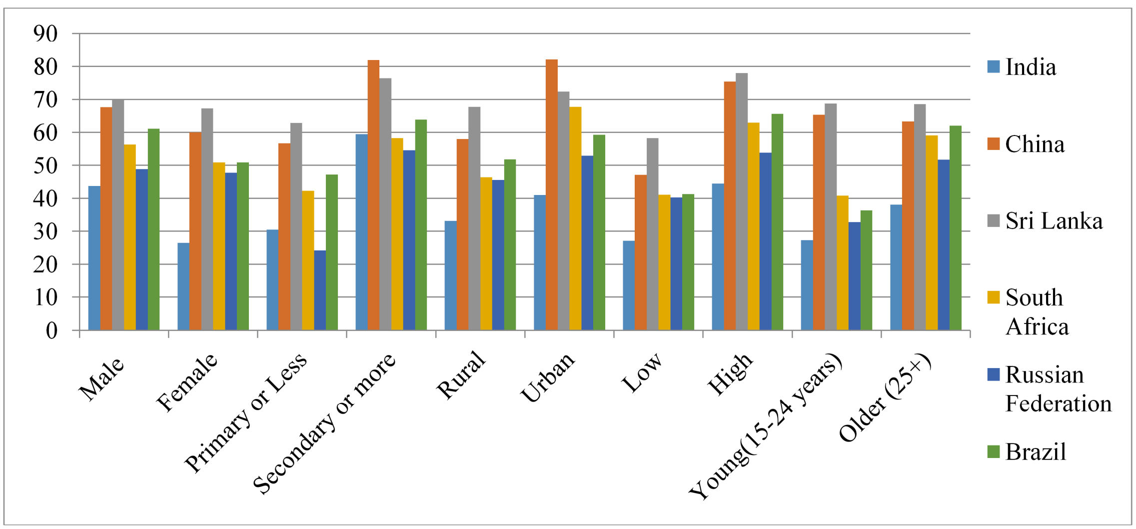


**Figure 3. Adults with an account at formal Financial Institution (%age)**

**Interpretation:**

It can be seen from the above data that by gender Sri Lanka ranks at the top with 69.98% of males and 67.23% of females having an account at formal financial institutions whereas India is at the bottom with only 43.73% males and 26.49% of females with an account at financial institution. Similarly, by income and age also Sri Lanka is at the top. However if we see from the side of rural/urban residence China has the highest no. of urban and Sri Lanka has highest no. of rural residential with 82.1% and 67.71% respectively, which are having their accounts at formal financial institution.

**Table 2: Savings at formal Financial Institution in past year (%age)**

| Characteristics | | India | China | Sri Lanka | South Africa | Russian Federation | Brazil |
|---|---|---|---|---|---|---|---|
| By Gender | Male | 15.99 | 32.02 | 30.2 | 23.67 | 10.02 | 12.97 |
| | Female | 7.09 | 32.09 | 26.22 | 20.55 | 11.55 | 7.8 |
| By Education | Primary or Less | 9.81 | 26.74 | 24.2 | 14.32 | 9.21 | 7.19 |
| | Secondary or more | 20.79 | 46.09 | 33.52 | 25.3 | 11.32 | 13.11 |
| By Rural/urban residence | Rural | 11.15 | 27.02 | 26.1 | 18.08 | 9.69 | 9.07 |
| | Urban | 12.58 | 48.06 | 37.67 | 29.77 | 12.56 | 11.4 |
| By Income | Low | 10.44 | 18.25 | 18.97 | 14.86 | 8.79 | 5.76 |
| | High | 12.91 | 41.68 | 36.43 | 27.39 | 12.38 | 13.3 |
| By Age | Young(15-24 years) | 27.3 | 65.29 | 68.71 | 40.76 | 32.81 | 36.34 |
| | Older (25+ years) | 12.88 | 33.59 | 27.37 | 26.08 | 11.93 | 11.12 |

Source: Compiled from Global Financial Inclusion Database, World Bank, 2012

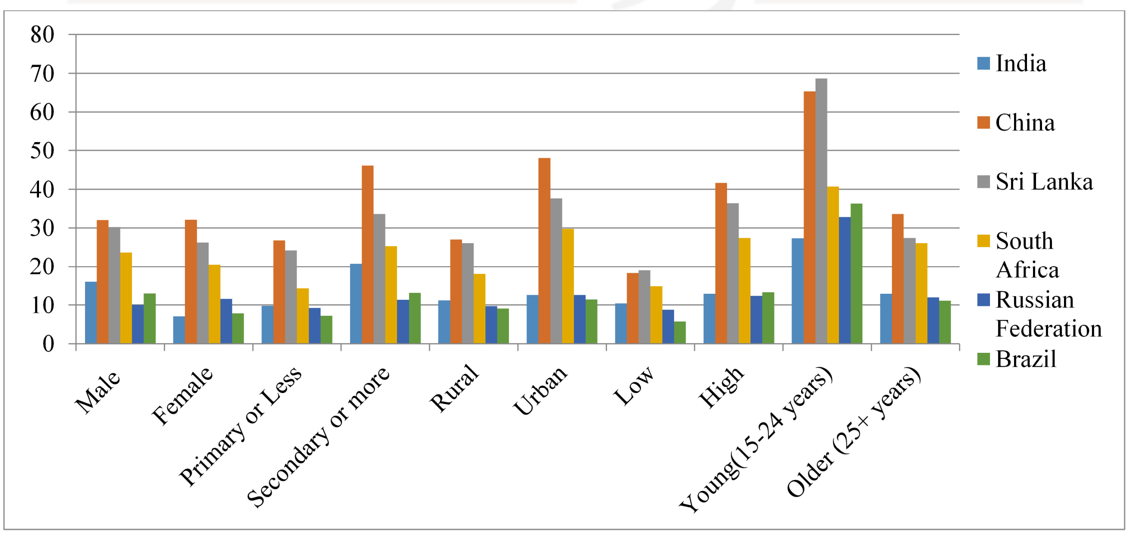


**Figure 4: Savings at formal Financial Institution in past year (%age)**

**Interpretation:**

It can be seen from the above facts and figure that China is the country where savings at formal financial institution is maximum. The gap between the savings of males and females is maximum in case of India i.e. around 8% and again India lies at bottom along with Brazil and Russian Federation in terms of savings at formal financial institution. Also the gap between savings of less educated people and people having higher education is maximum again in India from which we can assess that financial literacy can be one of the parameter which hinders the financial inclusion process in countries like India. In terms of rural/urban residence China is at the top with 27.02% rural and 48.06% urban residential having savings at formal financial institution whereas Brazil ranks at the last with only 9.07% rural and 11.4% urban residential having savings at some financial institution.

**Table 3: Loans from formal Financial Institution in past year (%age)**

| Characteristics | | India | China | Sri Lanka | South Africa | Russian Federation | Brazil |
|---|---|---|---|---|---|---|---|
| By Gender | Male | 8.62 | 8.36 | 15.87 | 11.36 | 8.01 | 6.55 |
| | Female | 6.74 | 7.42 | 19.39 | 6.47 | 7.42 | 6.12 |
| By Education | Primary or Less | 7.81 | 7.05 | 18.00 | 4.25 | 2.5 | 5.97 |
| | Secondary or more | 7.11 | 7.71 | 17.38 | 10.77 | 9.02 | 6.65 |
| By Rural/urban residence | Rural | 8.18 | 6.92 | 17.86 | 6.83 | 7.04 | 6.91 |
| | Urban | 5.92 | 8.28 | 17.30 | 12.77 | 8.88 | 5.85 |
| By Income | Low | 7.90 | 7.68 | 19.13 | 4.81 | 6.34 | 3.57 |
| | High | 7.46 | 6.96 | 16.47 | 11.54 | 8.66 | 8.21 |
| By Age | Young(15-24 years) | 4.47 | 3.54 | 10.78 | 1.93 | 4.36 | 0.69 |
| | Older (25+ years) | 8.83 | 7.89 | 19.74 | 11.78 | 8.48 | 8.1 |

Source: Compiled from Global Financial Inclusion Database, World Bank, 2012

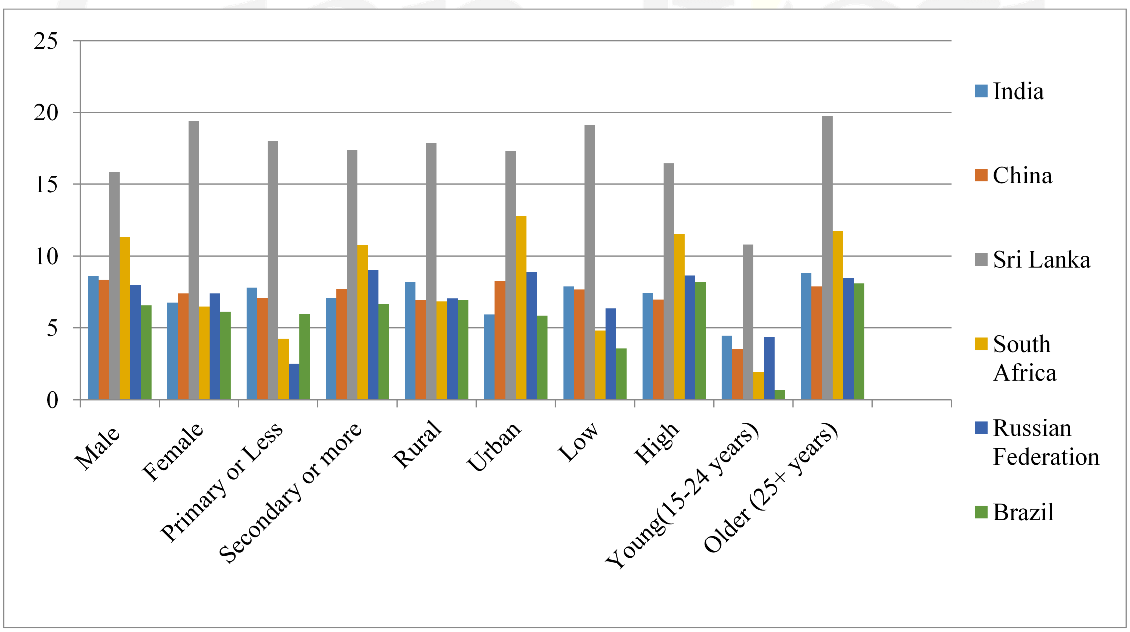


**Figure 5: Loans from formal Financial Institution in past year (%age)**

**Interpretation:**

It is clear from the above data and figure that Sri Lanka ranks at the top in terms of borrowings from financial institution whereas Brazil ranks at the last. Very less percentage of population in India borrowed from financial institution as can be seen in the table but still in terms of borrowings India is on par with other developing countries like China, Russian federation etc. but the gap between Sri Lanka and other developing economies is very wide in terms of borrowings from financial institution.

**6. Access to Banking – India vis-à-vis other developing economies**

Geographic and demographic penetration indicates the outreach of banking sector. Geographic penetration can be measured in terms of number of bank branches per 1000 sq km. Larger number of branches per sq. km. indicate smaller distances to the nearest physical bank outlets and hence easier geographical access. Demographic penetration can be measured in terms of per capita measure of bank branches or in other words the population served by each branch in a country. The per capita measure reflects the average number of people served by each physical outlet. Thus, a higher value connotes fewer clients per branch and is an indicator of easier access.

**Table 4: Geographic and demographic penetration of Bank Branches**

| Country | No. of Bank Branches per 1000 sq km. | No. of Bank Branches per 100000 adults |
|---|---|---|
| **India** | 30.4 | 11.4 |
| **China** | NR | NR |
| **Sri Lanka** | 42 | 17.5 |
| **South Africa** | 3 | 10.4 |
| **Russian Federation** | 2.7 | 38.2 |
| **Brazil** | 7.9 | 47.3 |
| Total | 86 | 123.8 |
| Average | 14.33 | 20.63 |
| Median | 5.45 | 14.45 |

Source:Global Financial Inclusion Database, World Bank, 2012
NR: Not reported

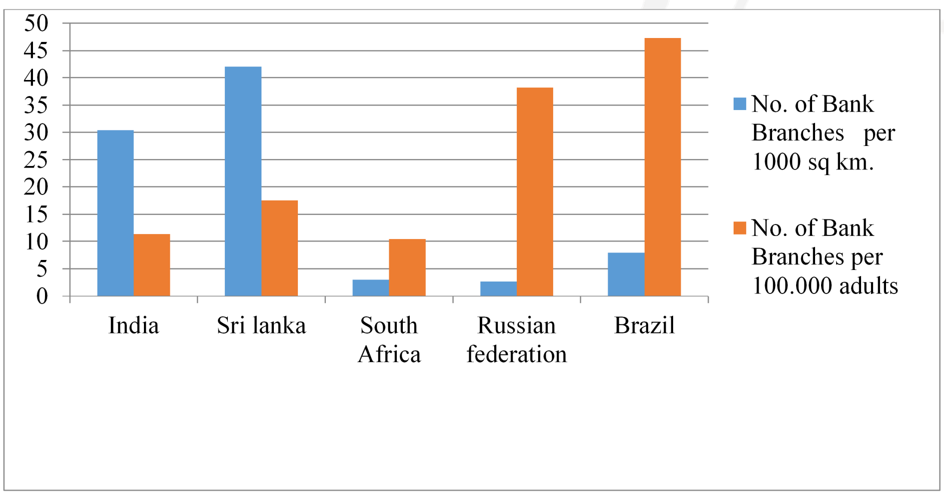


**Figure 6: Geographic and demographic penetration of Bank Branches**

The median number of branches per 1000 sq. km. is 5.45. Thus, based on the above, in terms of branch access geographically, India does not fare badly compared to other countries. Russian Federation ranks at the bottom with less than 2.7 bank branches per 1000 sq km. and on the other hand Sri Lanka is at the top among selected countries with 42 bank branches per 1000 sq km. In terms of demographic penetration median figure is 14.45 which is close to the

Sri Lanka as can be seen from the table. For India the figure is 11.4 branches per lakh persons which is less than the median. Thus, in terms of geographical penetration (branches per 1000 sq. km.), India fares much better than the demographic penetration in terms of access.

**Conclusion**

The problem of financial exclusion is not exclusive to the developing world. The developed countries too have been affected by it and many poor and disadvantaged people in the world still lack access to financial services. However, the type, degree and magnitude differ between the two worlds. Therefore, emphasis has been on empowerment of the disadvantaged groups for access to public goods and services including banking services in the developed countries. For achieving the current policy stance of "inclusive growth" the focus on financial inclusion is not only essential but a pre-requisite. And for achieving comprehensive financial inclusion, the first step is to achieve credit inclusion for the disadvantaged and vulnerable sections of our society. It may be observed that even in the developed countries, the State has accepted financial inclusion as an important measure for the empowerment of poor and disadvantaged sections of the society. In conclusion it can be said that financial inclusion has picked up in developing economies in the last few years but still it is far from adequate. Banks need to create awareness amongst people through various means of mass communication like television channels etc. and also various financial literacy programmes can be carried out to reach the unreached populace in order to achieve sustainable growth of a country.

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