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Financial Inclusion of Scheduled Commercial Banks in India

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Abstract

Background: The first notable policy adopted since independence in India to address the credit needs of the rural masses was nationalization of commercial banks in 1969 with 'mass banking' replacing the then prevalent 'class banking'. With financial liberalization since 1991, there occurred a reversal from the social objectives of banking to financial viability, profitability and competitiveness. Recently, based on the concerns that banks have not been able to include vast segment of population in its services coverage, the Reserve Bank of India formulated a policy of financial inclusion with an intention to provide access to financial services to the poor. The public sector scheduled commercial banks (SCBs) were assigned a major role to provide financial inclusion due to their immense geographical spread and in this context the article examines the progress of financial inclusion of SCBs in India.

Materials and Methods: The financial inclusion status of SCBs is examined with respect to spatial and sectoral outreach**.** The spatial aspect refers to the outreach of the SCBs in terms of areas which are generally considered as excluded from the formal sector like the rural and semi-urban areas. The sectoral aspect studies how far the SCBs have been successful in satisfying the needs of the credit thirsty sectors of the economy, like agriculture which is capable of eliminating poverty. Ratio of rural and semi urban offices, employees, credit account, credit amount, deposit account, deposit amount and agriculture account, agriculture amount etc. to their respective totals and annual average growth rate is used as indicators.

Results: Despite the emphasis on financial inclusion in terms of policy, the actual attainments of SCBs in terms of financial inclusion are far from satisfactory. There is a glaring difference between the percentage share of rural and semi urban accounts and the share of credit or deposit from these areas implying that the measuring rod 'an account per household' of financial inclusion falls short and can be very misleading in terms of policy prescriptions. The share of deposits mobilized from rural and semi urban areas is considerably larger than the share of credit allocated to these areas, indicating a high level of inefficiency in the allocation of resources and a bias in favor of urban and metropolitan centers.

Key Words: Financial inclusion; scheduled commercial banks; sectoral outreach; spatial outreach.

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I. INTRODUCTION

The burden of indebtedness in rural India has been very prevalent since the pre-independence period. Available literature points out that, there are four major problems with respect to the supply of credit to the Indian countryside. Firstly, supply of formal sector credit to the country side as a whole has been inadequate, secondly, rural credit markets themselves have been very imperfect and fragmented, thirdly, the distribution of formal sector credit has been unequal, particularly with respect to region and class, caste and gender in the countryside and fourthly the major source of credit to rural households has been the informal sector. (Basu, 2005). Given these issues, the objectives of rural credit policy in the post-independence period were 'to ensure sufficient and timely credit, at reasonable rates of interest to as large a segment of the rural population as possible' (Rangarajan, 1996). The policy instruments to achieve these objectives were to be: first, extension of the geographical and functional reach of the formal sector, second directed lending, and third, concessional or subsidized credit.

As such, the strategy during the 1970s and 1980s was to give a leading role to the nationalized commercial banks. One of the aims of nationalization of banks was 'social and development banking' by meeting rural credit needs and reducing the role of informal sector credit. Under this policy, there was a thrust on setting up of bank branches in rural areas. The nationalization of banks and subsequent developments led to the expansion of the geographical and functional reach of commercial banks, regional rural banks and co-operative credit institutions. Access to finance for the rural poor also somewhat improved after nationalization of banks. However, with the onset of economic reforms in the early nineties there was a distinct shift in the banking policy (Chavan, 2007). The focus of the banks during the reform periods has been on enhancing the efficiency and profitability and as a result, many of the regulations that were applied on the banking system during the pre-reform period have been relaxed in order to allow a market-based and more liberalized operation of the banking system. This has led to exclusion of most of the rural households from the formal financial system. A large body of literature has also noted that, despite vast expansion of financial institutions, a large number of groups of households still remain excluded from the opportunities and services such as savings, credit, remittance facility and insurance facilities provided by the financial sector since liberalization (Rao, 2007).

In this context, there has been a wide spread interest in minimizing the incidence of financial exclusion and ensuring financial inclusion of the hitherto under-served population. By Eleventh Plan the policy of inclusive growth has been documented in our plan agenda and among the strategies aimed at attaining inclusive growth, financial inclusion became the prominent one. Concurrently India has sought to achieve financial inclusion through three prominent financial institutions: rural co-operatives, public sector scheduled commercial banks (SCBs) and regional rural banks. Due to wider network of banking institutions, public sector commercial banks have a greater role for promoting financial inclusion in India and against this context, the present study analyses the role of public sector scheduled commercial banks in promoting financial inclusion in the country.

II. OBJECTIVE OF THE STUDY

To examine the financial inclusion of public sector scheduled commercial banks in India with focus on supply side aspects of sectoral and spatial outreach.

III. MATERIALS AND METHODS

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 (Rangarajan, 2008). Public sector scheduled commercial banks have been given a greater role in financial inclusion strategy and encouraged to open branches in rural and underbanked areas, promote Self Help Group linked credit schemes, provide other services such as equity and insurance products etc. as part of the financial inclusion policy adopted by Reserve Bank of India in 2008. The concept of financial inclusion with regard to scheduled commercial banks is defined as to cover two broad aspects - the spatial aspect and the sectoral aspect. The spatial aspect refers to the outreach of the public sector scheduled commercial banks in terms of areas which are generally considered as excluded from the formal sector like the rural and semi-urban areas. The sectoral aspect studies how far the public sector scheduled commercial banks have been successful in satisfying the needs of the credit thirsty sectors of the economy which are capable of eliminating poverty, particularly the agriculture sector.

To study the spatial aspect of financial inclusion, the outreach of public sector scheduled commercial banks in rural and semi urban areas has been taken into account as they are considered the most excluded areas of the economy. The following indicators have been used to analyze the spatial aspect:

X_1 - Percentage of rural and semi urban offices of each bank group to the irrespective total number of offices

X_2 - Percentage of employees employed in rural and semi urban areas of each bank group to their respective total number of employees

X_3 - Percentage of rural and semi urban credit accounts of each bank group to their respective total number of credit accounts

X_4 - Percentage of rural and semi urban outstanding credit amount of each bank group to their respective total outstanding credit.

X_5 - Percentage of rural and semi urban deposit accounts of each bank group to their respective total number of deposit accounts

X_6 - Percentage of rural and semi urban deposit amount of each bank group to their respective total deposits

There has always been a bias in favor of heavy industries or the firms enjoying economies of large-scale production as far as availability of bank credit is concerned. However, agriculture sector is a priority sector which requires massive credit for machinery and equipment and which is capable of providing sustainable livelihood to the rural masses. Hence the indicators taken into account to understand the sectoral outreach of financial inclusion of banks are:

Y_1 - Percentage of agriculture credit accounts of each bank group to their respective number of total credit accounts

Y_2 - Percentage of agriculture credit outstanding of each bank group to their respective amount of total credit outstanding

Annual average growth rate of the indicators has also been worked out to understand the trend.

The data source for the study includes publications of the RBI, particularly Statistical Tables Relating to Banks in India. Public sector scheduled commercial banks are divided into SBI and Associates (SBI) and Other

Nationalised Banks (NB) and the time period selected is 1996 to 2017, i.e., after the implementation of liberalization reforms in the banking sector in 1996 and the subsequent implementation of the recommendations of the Rangarajan Committee on Financial Inclusion in 2008.

IV. DISCUSSION

4.1 Spatial aspect of financial inclusion of scheduled commercial banks

Financial inclusion through spatial outreach of the SCBs provides an understanding of the extendibility of services of banks to the vulnerable areas -i.e., how far the bank groups have been successful in reaching out to the excluded areas of the nation like the rural and semi urban areas. The section focuses on studying the trend of bank branches, employees, credit accounts, credit amount, deposit accounts and deposit amount corresponding to rural and semi urban areas of a particular bank group as a proportion of the national figures of the same bank group.

Table 1. Financial inclusion in terms of spatial outreach of scheduled commercial banks -I

	X1		**X2**	
Year	**SBI**	**NB**	**SBI**	**NB**
1996	88.11	64.66	45.04	34.61
1997	86.63	62.9	45.35	34.69
1998	71.07	62.62	44.96	34.48
1999	70.58	61.99	44.86	34.49
2000	70.21	61.79	45.13	34.86
2001	69.89	61.53	45.7	36.14
2002	69.68	61.05	45.33	36.71
2003	69.52	61.23	45.97	36.65
2004	69.33	60.92	46.65	37.21
2005	68.98	60.09	45.97	36.43
2006	66.01	57.10	42.33	33.63
2007	64.44	57.02	39.15	34.30
2008	64.38	54.86	44.17	34.96
2009	62.61	54.41	45.37	35.96
2010	58.94	51.58	21.49	21.79
2011	59.14	52.19	41.71	35.96
2012	59.01	53.22	43.36	38.66
2013	59.29	54.34	44.99	40.23
2014	59.19	56.16	44.93	40.67
2015	59.16	56.76	45.41	42.60
2016	58.97	57.12	47.60	43.81
2017	58.83	56.80	45.54	43.41
AAGR	**-1.81**	**-0.59**	**2.51**	**2.35**

Note: **-** AAGR – Annual Average Growth Rate

Source: Statistical Tables Related to Banks in India, RBI, (Various Issues)

The share of rural and semi urban offices has been selected as a variable because it shows the share of the total resources that the bank groups have allocated for the rural and semi urban areas. Thus, X_1 is the representative figure showing how the resources are flowing into the rural and semi urban areas in comparison with the national figures. The share of rural and semi urban offices has been falling continuously for all the bank groups over the years. Even though state bank and nationalized bank groups have more than half of their offices in the rural and semi urban areas, during the study period (1996 – 2017), their share fell from 88.11 per cent to 58.83 per cent and from 64.66 per cent to 56.80 per cent for SBI and NB respectively. In other words, both SBI and associates and other Nationalized Banks were pulling out of the rural and semi urban areas and reducing their share of rural and semi urban offices. The annual average growth rate is negative for both SBI and NB with regard to the share of rural and urban bank branches. The variable X_2 stands for the percentage share of employees in rural and semi urban areas to the total number of employees of a particular bank group. Table 1 shows the percentage share of employees in the rural and semi urban areas from 1996 – 2017. Except 2007 and 2010, the percentage share of rural and semi urban employees for SBI fluctuate between 41per cent and 45 per cent. For the case of nationalized banks, the percentage share of rural and semi urban employees also shows a fluctuating trend till 2010 and thereafter the share is increasing. Hence there is a slight positive value for annual average growth rate with regard to the share of rural and semi urban employees, however considering the need of banking in the rural areas this slight increase is not capable of meeting the rural demands. The financial inclusion drive declared by Reserve Bank of India since 2008 has not made any improvement in the percentage share of bank branches in the rural and semi urban areas of India.

Table 2. Financial inclusion in terms of spatial outreach of scheduled commercial banks -II

	X3		**X4**		**X5**		**X6**	
Year	**SBI**	**NB**	**SBI**	**NB**	**SBI**	**NB**	**SBI**	**NB**
1996	78.82	73.74	27.26	23.82	60.33	49.43	40.47	32.21
1997	76.96	72.58	27.62	24.28	59.86	49.95	41.75	32.96
1998	76.7	73.08	27.6	23.79	61.49	50.24	41.79	32.31
1999	75.51	69.53	27.24	23.13	62.39	50.29	41.89	32.23
2000	74.09	67.64	26.48	22.47	62.81	50.56	42.11	32.65
2001	78.00	62.87	24.5	21.22	62.43	51.01	41.56	32.54
2002	75.27	67.75	25.66	22.31	63.00	50.69	42.07	32.79
2003	76.00	67.76	27.39	22.25	63.11	51.06	41.59	32.3
2004	74.25	68.07	27.63	21.89	62.34	51.36	37.71	30.37
2005	74.24	69.33	27.91	21.39	62.52	51.7	37.11	28.53
2006	71.44	65.88	25.73	18.48	56.85	48.85	33.52	25.22
2007	73.37	66.24	24.19	17.85	57.43	49.63	32.04	23.78
2008	72.61	68.12	24.87	16.38	57.54	49.97	30.00	22.66
2009	73.31	67.19	23.7	15.35	58.80	50.77	30.37	21.79
2010	73.94	46.91	24.53	17.81	60.12	50.11	32.89	20.14
2011	74.41	71.48	23.88	14.86	61.22	51.65	33.49	19.75
2012	74.83	69.51	26.03	15.56	62.80	53.16	33.90	20.75
2013	76.39	74.28	25.56	16.82	64.54	55.08	33.79	21.10
2014	76.38	75.08	24.56	17.71	66.44	57.27	34.72	21.91
2015	75.75	75.49	24.84	19.01	67.85	58.41	35.02	23.17
2016	74.75	74.95	24.45	20.69	68.68	60.26	35.29	25.18
2017	72.38	73.31	25.09	20.70	67.68	59.47	35.76	26.44
AAGR	**-0.38**	**0.792**	**-0.301**	**-0.384**	**0.58**	**0.90**	**-0.50**	**-0.81**

Note: - AAGR – Annual Average Growth Rate
Source: Statistical Tables Related to Banks in India, RBI, (Various Issues)

The Table 2 shows the percentage share of rural and semi urban credit to total credit of both the bank groups under consideration. From the available data it is inferred that both in the case of credit accounts and the amount of credit outstanding the share of rural and semi urban areas has been falling. Among the bank groups the percentage share of credit accounts was high in state bank groups. In case of SBI, it was 78.82 per cent in 1996 and 73.74 per cent for nationalized banks. Over the years from 1996 to 2017 the percentage share of rural and semi urban accounts for the SBI shows a fluctuating trend and it declined to 72.38 per cent in 2017. In the case of nationalized banks, the share remains the same trend and it was 73.74 per cent in 1996 and 73.31 per cent in 2017. The outstanding credit in rural and semi urban areas has also registered a fall over the years, for SBI the fall has been from 27.26 per cent to 25.09 percent in 2017. The nationalized bank group also recorded a fall from 29.47 per cent of outstanding credit in rural and semi urban to 20.70 per cent during the reference period. Another visible trend is the difference between the percentage share of accounts and the percentage share of outstanding credit. For instance, in 1996, percentage share of accounts in rural and semi urban areas for state bank groups and nationalized banks was 78.82 per cent and 73.74 per cent respectively, whereas the percentage share of outstanding credit was just 27.26 per cent, and 23.82 per cent. In 2017, percentage share of accounts in rural and semi urban areas for the bank groups mentioned above shows 72.38 per cent and 73.31per cent respectively and the percentage share of outstanding credit was 25.09 per cent, and 20.70 per cent respectively. It shows there is a wide disparity between the two variables, implying that the high number of credit accounts does not mean that inclusion is taking place. Thus, the rise in the number of accounts (as often quoted as a measuring rod of financial inclusion) can be very misleading.

The share of the number of deposit accounts in the case of SBA and NB groups hast registered a slight increase, it rose from 49.43 per cent in 1996 to 50.77 per cent in 2009 in the case of NB group. In the case of SBA, it fell from 60.33 per cent to 58.80 per cent during the same period. Since 2010 onwards the share of deposit accounts started to increase and in 2017 the share of deposit accounts increased to 67.68 per cent for SBA and 59.47 per cent for NB. However, the percentage share of rural and semi urban deposits to total have registered a fall in the case of all the bank groups. In the case of SBI group it fell from 40.47 per cent in 1996 to

35.76 per cent in 2017. The NB group also registered a fall during the reference period, which fell from 32.21per cent in 1996 to 26.44 in 2017. There has also been a marked difference in the share of deposits mobilized from rural and semi urban areas and the credit allocated to these areas as the share of deposits mobilized is considerably larger than the share of credit allocated to these areas. This shows a high level of inefficiency in the allocation of resources and a bias in favor of urban and metropolitan centers.

4.2 Sectoral aspect of financial inclusion

Agriculture sector in India is still the breadwinner for more than 65 per cent of the population. Thus, investment in agriculture is imperative for increasing the standard of living of the people. However, since the majority of farmers in India belong to the small and marginal category, they shy away from taking loans from the formal sector due to the complex set of formalities that have to be taken care of and due to the lack of collateral for getting a loan. Thus, they find moneylenders more accessible in comparison to the formal financial institutions. Taking this into consideration the Reserve Bank of India and the Government of India has been taking many steps for attracting the farmers towards the formal institutions and thus to accelerate the process of financial inclusion. The financial inclusion of SCBs in terms of sectoral outreach (credit to agriculture) is examined below.

Table 3. Financial inclusion in terms of sectoral outreach of scheduled commercial banks

	Y1		**Y2**	
Year	**SBI**	**NB**	**SBI**	**NB**
1996	43.29	39.61	16.95	14.64
1997	43.23	39.85	14.2	13.59
1998	43.62	40.96	12.97	13.11
1999	44.17	40.61	13.08	11.55
2000	44.91	42.27	12.32	11.52
2001	42.43	39.51	11.58	11.79
2002	42.07	39.33	11.14	11.15
2003	39.46	36.13	11.91	10.80
2004	38.85	36.16	10.36	10.48
2005	41.47	37.17	10.11	8.32
2006	38.48	36.21	11.93	10.30
2007	37.3	36.87	11.19	11.18
2008	34.28	37.3	12.13	12.54
2009	37.7	41.85	11.68	11.98
2010	35.9	41.9	12.19	13.34
2011	44.8	44.36	12.50	13.15
2012	45.7	44.45	12.23	13.23
2013	46.5	45.31	12.73	13.34
2014	47.62	50.12	11.93	11.74
2015	49.28	52.25	11.40	11.20
2016	51.28	55.36	11.54	11.79
2017	53.78	61.12	11.86	12.43
AAGR	**1.26**	**2.20**	**-1.40**	**-0.34**

Note: - AAGR – Annual Average Growth Rate

Source: Statistical Tables Related to Banks in India, RBI, (Various Issues)

The percentage share of agriculture credit accounts for SBI has increased slightly over the years. The accounts increased from 43.29 per cent in 1996 to 53.78 per cent in 2017, with fluctuations. In the case of nationalized banks, except for some years the percentage share of accounts increased over the years. It was 39.61 per cent in 1996 and increased to 61.12 per cent in 2017. It is interesting to note that the share of credit accounts has shown an increasing trend for SBI, whereas the credit amount through these accounts shows a falling trend. The percentage share of credit amount for SBA was 16.95 per cent in 1996 and continually declined to 11.19 per cent in 2017. For the case of nationalized banks, the percentage share of agriculture credit was 14.64 per cent in 1996 and it declined to 12.43 in 2017. The annual average growth rate of credit to agriculture sector is negative for both SBI and other Nationalized banks. It is to be noted that there is a marked difference between the share of agriculture credit accounts and the share of outstanding credit; the share of outstanding credit has always been significantly lower than the share of accounts. This may be due to the reason that the majority of farmers belong to the small and marginal categories who take small amount of loan from the formal financial institutions just to cover their operating costs and do not take loans for the sake of large-scale investment in their fields.

The analysis with respect to the financial inclusion of SCBs provides the result that there has been a withdrawal of SCBs from the rural and semi urban areas in terms of their branches, employees, credit and deposit amount and lending to agriculture sector. Going by the objective of financial inclusion, one theoretical argument put forward by Patnaik is that, as a result of financial liberalization, formal financial sectors are reluctant to lend to agriculture sector and other poorer sections of the people (Patnaik, 2005).The theoretical argument is that, the essence of financial liberalization consists in three sets of measures: first to open up the country to the flow of international finance; second to remove controls and restrictions on the functioning of domestic banks and other financial institutions so that they get properly integrated as participants in the world's financial markets; third, to provide autonomy to the central bank from the government so that its supervisory and regulatory role vis-à-vis the banking sector is disassociated from the political process of the country. Financial liberalization necessarily leads to an increase in those real interest rates in the economy that impinge on investment decisions, particularly in sectors that were earlier recipients of subsidized finance (for example, agriculture). Second financial liberalization necessarily leads to a reduction in the proportion of credit available to the agriculture sector. Supporting Patnaik's argument, our study shows that the formal financial system excludes rather than including the needy sections of the population during the liberalization period and the drive towards financial inclusion has not resulted in any change in the pattern of sectoral and spatial outreach of public sector scheduled commercial banks.

V. CONCLUSION

The Committee on Financial Inclusion has exhorted the Reserve Bank of India to implement policies to tap the resources of scheduled commercial banks, since commercial banks with its vast geographical coverage have great potential to bring about financial inclusion. However, it is revealed from the study that despite the emphasis on financial inclusion in terms of policy, the actual attainments are far from satisfactory. The share of rural and semi urban areas in terms of all the indicators of financial inclusion have been falling. There is a glaring difference between the percentage share of rural and semi urban accounts and the share of credit or deposit from these areas implying that the measuring rod 'an account per household' of financial inclusion falls short and can be very misleading in terms of policy prescriptions. Moreover, we could also observe a wide gap between the share of deposits mobilized from and the share of credit allocated to the rural and semi urban areas as the share of deposits mobilized is considerably larger than the share of credit allocated to these areas. This shows a high level of inefficiency in the allocation of resources and a bias in favor of urban and metropolitan centers. Thus, the steps taken by the government and the RBI are falling short of the desired objectives of financial inclusion as far as scheduled commercial banks are concerned.

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