ROLE OF FINANCIAL INCLUSION IN THE MULTI SECTORAL INCLUSIVE GROWTH OF THE NATION

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ABSTRACT

The concept of inclusive growth combines the participation in the process of growth with the sharing of benefits from the achievements as a result of the growth. In this article, an effort has been made to understand the concept of inclusive growth and its dependence on the key sector of financial development which acts like a thread in binding all the sectors together to ensure inclusive growth with participation of excluded groups directly or through the link of financial sector indirectly. It has been highlighted that the benefits of inclusive growth have to be equitably distributed among various sectors to spur growth and not merely distribution of income leading to simply a welfare activity. In this regard, role of RBI has been identified to be of paramount importance and RBI has been pursuing the agenda of financial inclusion with full vigor in the recent past. Apart from this, a requirement for structural transformation in the economy is identified through various means such as simplification of tax laws, efficient allocation of resources, and increased participation of private sector through CSR activities.

KEY WORDS: Inclusive growth, Financial Inclusion, Reserve Bank of India

INTRODUCTION

The concept of inclusive growth combines the participation in the process of growth with the sharing of benefits from the achievements as a result of the growth. Thus inclusive growth is the outcome as well as a process. On one hand, inclusive growth aims at ensuring the participation of all sectors in the process of growth whereas on the other hand, it works to ensure that everyone in all the sectors shares the benefits of growth equitably. In fact, participation in the process of growth without having the opportunity to share the benefits will be unjust and shall ultimately retard the process of growth and sharing benefits without participation will again be unjust leading to draining of resources and making it a simply welfare activity with no specific contribution to productivity .As such, inclusive growth can be observed from long-term perspective as the focus on productive employment rather than on direct income redistribution, as a means of increasing income for excluded groups and also making efforts for their inclusion.

As discussed above, almost all the sectors existing in the country have impact on the economic development of the country responsible for inclusive growth. Some of the major sectors responsible for the inclusive growth of the nation are listed below:

1. Financial Sector
2. Agricultural Sector
3. Corporate Sector
4. Public Sector
5. Information Technology
6. Automobile
7. Aviation
8. Space Technology
9. Pharmaceuticals
10. Technology

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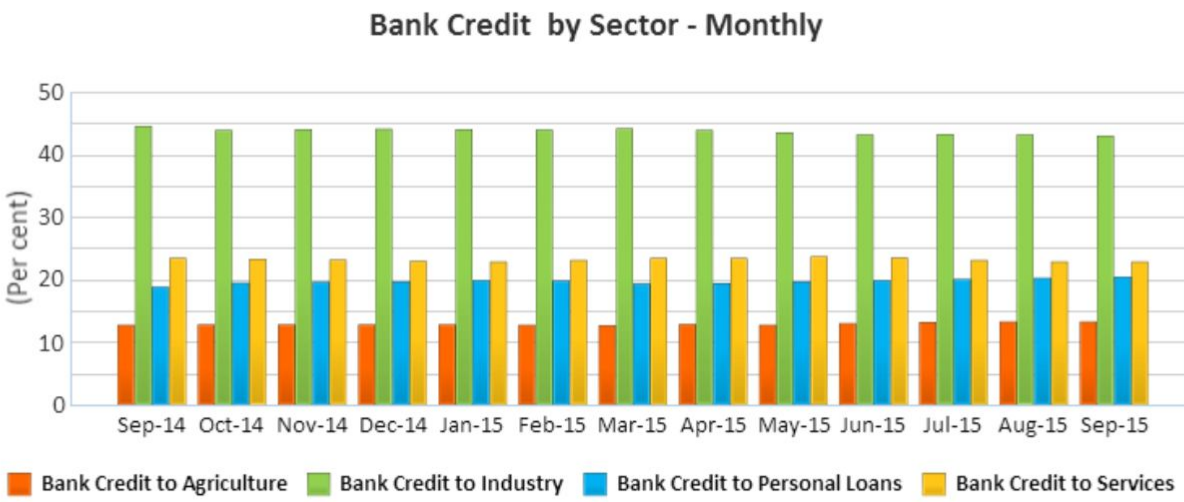
Although, all the sectors listed above and many more contribute to economic development and economic growth of the country .However, the key role is played by the financial sector because this sector is the source of funds being pumped into various other sectors.. The financial sector is the common thread, which binds all the sectors that are responsible for the growth and facilitates investment decisions for ensuring the planned inclusive growth. Financial development creates enabling conditions for growth through either a supply leading (financial development spurs growth) or a demand-following (growth generates demand for financial products) channel. There is a large body of empirical research available which supports the view that development of the financial system contributes to economic growth (Rajan & Zingales, 2003). Hence, there is a general consensus amongst economists and policy makers that financial development spurs economic growth. Also, Inclusive growth can only be achieved if there is general economic growth. Therefore, an in depth study of the financial development and economic growth is essential to have insight into the process of inclusive growth and also equitably sharing the benefits by resorting to healthy investment decisions for ensuring healthy growth of various sectors participating in the process.

FINANCIAL DEVELOPMENT AND ECONOMIC GROWTH

Not only hypothetical and theoretical approaches emphasize relation between finance and growth, but empirical evidences consistently emphasize the robust nexus between finance and growth .At the cross-country level, evidences indicate that various measures of financial development (including assets of the financial intermediaries, liquid liabilities of financial institutions, domestic credit to private sector, stock and bond market capitalization) are robustly and positively related to economic growth (King & Levine, 1993 &Levine & Zervos, 1998). Other studies establish a positive relationship between financial development and growth at the industry level (Rajan & Zingales, 1998). Even the recent endogenous growth literature, building on 'learning by doing' processes, assigns a special role to finance (Aghion & Howitt, 1998 & 2005).As such, it is not extreme position to conclude that no growth is possible in any sector without financial development viz. for any growth availability of finance is essential. Any sector devoid of finances may not be in a position to successfully participate in the process of inclusive growth.

A developed financial system increases the access to funds. The main constraint of an underdeveloped financial system is that it is unable to make the funds available for less productive sectors of the economy and therefore many people and sectors have to depend on their own funds and resort to informal sources of financing such as money lenders which are high cost sources. Lower the availability of funds and higher their cost, fewer would be the economic activities that can be financed and hence the resulting economic growth will also be lower. Table 1 given below illustrates the sector wise deployment of Bank Credit till September 2015:



Source: Real-Time Handbook of Statistics on the Indian Economy.

From the Table 1 above, the data on bank credit by different sectors shows the following trends:

1. Credit to agriculture is the least in all the months from September 2014 to September 2015
2. Majority of the loans have always been extended to the industrial sector.
3. There have not been considerable variations in the division of loans amongst the various sectors over the year.

The trend indicated above is not healthy for ensuring healthy economic development and thereby growth of the country. As shown in the above table, only 11% of loans being extended to the agricultural sector results in the majority of borrowing being done from the moneylenders which creates scope for the exploitation of these farmers. Also, increase in share of the moneylenders would impose an unhealthy drain on the economy and would result in retardation of the growth. The same is true for the credit requirements of the services sector. Thus, it is important that the Central Bank of India along with the Government of India would take upon it, the onus of formulating proper monitoring and regulatory mechanism along with conducive credit policy for economic growth.

Fortunately, India is moving towards having developed financial system where access to money for investment is becoming easier gradually. There are a number of financial institutions in public sector as well as private sector ready to finance healthy investments for ensuring growth. However, in a developed financial system, the responsibility of the central bank i.e. Reserve Bank of India increases manifold for monitoring & regulating the money demand and supply to various sectors for ensuring inclusive growth. Major policy formulations are also the responsibility of this bank to exercise complete financial control on private as well as public sectors. Ensuring penetration of banking to excluded groups in rural, hilly, tribal and other non-accessible areas is also the responsibility of the central bank of the country for achieving inclusive growth with participation of maximum groups and maximum sectors.

FINANCIAL DEVELOPMENT, GROWTH AND STABILITY

Discussions in the preceding paragraphs have concluded that for inclusive growth, economic growth is essential which is possible by financial development system of the country. However, it is the pace of financial development that plays decisive role in the stability of the system. At this stage, regulatory mechanism by the central bank plays an important role. Although, due to operation of several regulatory mechanism, the process of financial development may get slowed down; However, it is essential to maintain the stability of the financial system. As such, financial development for economic growth has to be controlled at a sustainable level so that stability of the financial system of the country is ensured and the country is not driven to financial crisis as has been witnessed in many countries in the recent past.

ROLE OF RESERVE BANK OF INDIA (RBI)

The Reserve Bank of India and the Government of India have been making efforts to increase the penetration of banking in the country including the remote hilly, rural and tribal areas. Some of these measures include:

1. The creation of State Bank of India in 1955;
2. Nationalization of commercial banks in 1969 and 1980;
3. Initiating the Lead Bank Scheme in 1970;
4. Establishing Regional Rural Banks (RRBs) in 1975;
5. Introducing a Self-help Group (SHG)-Bank Linkage Programme in 1992 and
6. Formulating the Kisan Credit Card scheme in 2001. (Mohan, 2006)

In addition to the above, financial inclusion also found a place in the policy documents only very recently. In the Annual Policy of the Reserve Bank of India for 2004-05, the Governor, Dr. Reddy observed and I quote –

"There has been expansion, greater competition and diversification of ownership of banks leading to both enhanced efficiency and systematic resilience in the banking sector. However, there are legitimate concerns in regard to the banking practices that tend to exclude rather than attract vast sections of population, in particular pensioners, self-employed and those employed in unorganized sector. While commercial considerations are no doubt important, the banks have been bestowed with several privileges, especially of seeking public deposits on a highly leveraged basis, and consequently they should be obliged to provide banking services to all segments of the population, on equitable basis."

Pursuant to this, the Reserve Bank of India has undertaken a number of measures with the objective of attracting the financially excluded population into the structured financial system. This policy directive for inclusion of financially excluded groups would go a long way in ensuring inclusive growth of the Country. These parameters of financial inclusion are given below:

1. Opening of No Frills Accounts

In November 2005, a new concept of banking was introduced, known as 'no-frills' account with 'nil' or very low minimum balance to make such accounts accessible to vast sections of the population. In 2012, the nomenclature was changed to Basic Savings Bank Deposit Accounts (BSBDAs) for all individuals with zero minimum balance and facility of ATM Card/ Debit card. There is no charge on deposits and up to four withdrawals in a month are allowed. By doing this, every person has the right to open a bank account. Banks have been advised to provide small overdrafts in such accounts to meet emergency credit requirement in hassle free manner.

2. Simplification of KYC norms:

In order to ensure that all the financial needs of the customers are met, banks are advised to offer a minimum of four basic products, viz.;

- A savings cum overdraft account;
- A pure savings account, ideally a recurring or variable recurring deposit;
- A remittance product to facilitate EBT and other remittances; and
- Entrepreneurial credit products like a General Purpose Credit Card (GCC) or a Kisan Credit Card (KCC).

3. **Engaging Business Correspondents:**

In January 2006, the Reserve Bank of India permitted banks to engage Business Facilitators (BFs) and Business Correspondents (BCs) as intermediaries for providing financial and banking services. The BC Model allows banks to provide door step delivery of services especially to do "cash in - cash out" transactions, thus addressing the "last mile" problem. The list of eligible individuals/entities who can be engaged as BCs is being widened from time to time by adopting a test and learn approach to this process. In September 2010, RBI has allowed for profit organizations excluding NBFCs to operate as BCs. Banks can now leverage on the penetrative network of mobile companies. Mobile network companies have joined hands with banks to make available banking services to India's unbanked population. The agents of mobile companies work as Customer Service Providers (CSPs) and provide BC services, thus expanding the outreach of banks.

4. **Use of Regional Language:**

Option for use of regional language for banking operation has made local population comfortable with the banking services being provided. There is now no communication gap between beneficiaries and service providers leading to greater participation in the schemes and inclusion in growth of the country.

5. **Use of Technology:**

Manual factor is gradually being phased out from all the fields by introduction of latest technologies. This has resulted in increase of confidence of the beneficiaries in all the sectors. In addition, dependency on individuals is getting reduced leading to increase in efficiency and ultimately productivity.

6. **Introduction of General Credit Cards:**

Introduction of General Credit Cards has greatly facilitated the beneficiaries in getting various type services from banking operation. It has reduced the number of visits to bank branches.

7. **One-time Settlement:**

One time settlement of beneficiaries, whenever required, has infused great confidence in the public and also provides financial resources whenever needed.

8. **Financial Education:**

Financial literacy to excluded groups in the remote areas has helped in getting these groups included in the financial development process for inclusive growth of the country. (Shodhganga.in)

REGULATORY MECHANISM BY RESERVE BANK AND INCLUSIVE GROWTH

Apart from the efforts made to include the excluded groups in the financial development of the country as discussed in the preceding paragraphs, the necessity of regulatory mechanism on the credit policy , money supply etc. is experienced when the financial stability of the system needs to be ensured.

To embark upon appreciable inclusive growth in the country, greater emphasis on economic growth is essential which can be achieved by sound financial development policies. However, a word of caution needs to be exercised to control the pace of financial development. Uncontrolled, financial development with fast pace leads to unsustainable growth and the financial system becomes unstable (Sahay, et al., 2015).

To ensure stability of the financial system of the country, the pace of financial development is to be controlled by the central bank of the country. Controlling the pace of financial development may lead to retardation in the economic growth and consequently inclusive growth. However, this trend is desirable till such time as the sustainable level of financial development and economic growth is achieved.

For controlling the financial development, the Reserve Bank of India regulates the money supply i.e. access to the money by adopting suitable credit policy. There are many other similar controlling mechanisms available with apex bank to control the financial development to a required level to spur sustainable controlled growth so that the financial system is saved from the perils of instability.

In the event of inability of apex bank to properly regulate the monetary mechanism of the country, there are dangers of the financial system losing stability and the country may plunge into a financial crisis known as financial deepening which has been experienced by many countries in the past. As such, by suitable regulatory mechanisms a tradeoff has to be established between the financial development coupled with economic growth and financial stability.

TAXATION POLICIES AND THEIR IMPACT ON INCLUSIVE GROWTH

Taxation is a major factor in the financial growth of the country. With the policies of taxation, the government makes effort to collect revenues from the sectors which can afford to pay out of their surpluses. This money is used for the projects which are not always economically viable but essentially to be implemented for discharging social responsibility. Many projects of public interest financed through government spending may not be viable to ensure adequate rate of return on the capital employed, but they are to be essentially implemented to spur healthy economic growth.

Depending of their method of collection, the taxes are divided in two major categories i.e. Direct Taxes and Indirect Taxes. Further classification of the taxes is based on the taxes collected by the states and those collected by the centre (in federal structure of the government). The entire gamut of taxes is named as, Income Tax (Individual and Corporate), Service Tax, Sales Tax, VAT etc.

Taxes collected by the central government in the federal structure are further apportioned among the states for meeting their social liabilities depending on the prevailing conditions in that state. A good percentage of these taxes is spent by the central government on the projects related to social upliftment and of public interest and a fraction of these taxes is kept for meeting the situations of crisis in case floods, earthquakes, draughts etc.

From the above discussion on the tax collection and its disbursement, it is evident that tax money contributes to the inclusive growth of the country by ensuring development in those sectors where projects are not viable on the principles of rate of return but to be essentially implemented for ensuring growth in these sectors so that ultimately spur in the inclusive growth is achieved.

CORPORATE SOCIAL RESPONSIBILITY AND INCLUSIVE GROWTH

Similar to the taxation as discussed above, a potent source for ensuring development in the areas of public interest and projects of social upliftment is the investment through Corporate Social Responsibility (CSR) of corporate sector where a fixed percentage of their surplus has to be spent on the projects of social upliftment of the society. This is a very potent source for the development of infrastructure in the socially backward areas where normally no financially viable scheme can be implemented. Through development of infrastructure in such areas, the corporate sector is contributing in a big way in the inclusive growth of the country.

CONCLUSION

Inclusive growth has come to the forefront of the growth agenda of India in the recent years. Efforts are being extended to ensure that every sector plays a productive role in the growth of the country for which financial inclusion has been identified as the prerequisite. Financial inclusion is the binding thread that connects all the other sectors by ensuring equitable distribution of finance amongst all the sectors. This will ensure growth of all the sectors rather than turning the government help of providing appropriate finance into a welfare activity. In the preceding sections we have given enough arguments to prove that financial inclusion is the most essential ingredient of inclusive growth especially in case of developing economies like India.

Role of RBI is of paramount importance in this regard and RBI has been pursuing the agenda of financial inclusion with full vigour in the recent past. The measures of RBI like no frills account, simplification of KYC norms, engaging business correspondents, using regional language, use of technology, introduction of GCCs, one time settlement and financial education are steps in the same direction. Besides financial inclusion inclusive growth will have to be achieved through various structural transformations in the economy like simplification of tax laws and making them more tax payer friendly, efficient allocation of resources collected through taxation in the economy, increased participation of private sector through their CSR activities etc. are some of the transformations on which the government is working.

However, there is still a long way to go in terms of achieving sustainable and inclusive economic growth.

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