

Study on Role of Small Finance Banks for Achieving Financial Inclusion in India

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ABSTRACT

Financial Inclusion or inclusive financing is the delivery of financial services at affordable cost to vulnerable and weaker section of the society in comparison to financial exclusion where those services are not available due to less affordability and lack of reach to this under privileged section of society. This paper focuses on effective financial system and for the same government has introduced various initiatives starting from Jan-dhan Yojana to giving licenses to local bank to operate as Small Bank in India. The paper highlights the role of Small Banks in the growth and development of economy by involving more people into the formal financial sector through financial inclusion.

Keywords: Banking Services, Affordability, Financial Inclusion, Micro Finance.

INTRODUCTION

The dawn of financial inclusion in Indian context was a decade ago when Y. Venugopal, the then Governor, proffered it in annual policy of the reserve banks. [April 2005]. It was suggested that banks should amend their present policies in accordance with the objectives of financial inclusion initiative by present government. The main focus of the central bank was to construct a bridge between banks and financially excluded population. In light of the above fact RBI implemented the recommendations of Khan Committee Report and gave instructions to banks to provide No Frills Bank Accounts. General public was also provided with an opportunity to open accounts with annual deposits up to 50,000. As according to (S&P survey, 2015) only 20 percent of Indian women are financially literate. Another survey by (National Centre for Financial Education, 2015) showcased that female literacy is 52.12 per cent, out of which only 12 per cent are financially literate.

Government of India (GOI) and Reserve Bank of India have been playing a pivotal role in including people in the Financial System since 1975. Kisan Credit Card (KCCs), Banking Correspondent-Banking Facilitator Model, SHG-Bank Linkage Program, Direct Benefits Transfer, USSD Mobile Banking, Regional Rural Banks, Rashtriya Mahila Kosh, Rashtriya Swasthya Bima Yojana are being the major weapons of the Indian Government in making the Financial inclusion campaign a success. The recent of Indian government initiative with Jan Dhan Yojna. India holds a place in Guinness book of world record in opening 18,096,130 accounts in one week as a part of financial inclusion campaign.

Although later it was found that over 92,52,609 were frozen on March 24, 2017 due to lack of transactions since last one year. Around 77 per cent people were baffled by the complicated procedure of debit card and complex transaction procedure. These steps have played a major role in expanding the banking network and their customer base. But Government of India later realized that these schemes have not been able to meet the expectations. Inefficiency of the banking system did not reduce the influence of the private money lenders much. As 43 per cent Rural Households still borrow from Informal sources. These schemes had not promoted the habit of saving at banks as only 13.5 per cent of Total Account Holders have saved any money in these accounts in 2015-16. Most of accounts are still dormant. This reports the deteriorated condition of financial inclusivity in India. As an incremental step towards achieving financial inclusion Indian Government have supported the establishment of Micro- Finance Institutions to set up Small finance banks in India(Raman,2012). Both these measures are really path breaking and can prove to be major success in achievement of Financial Inclusion. This Research paper attempts to point out the positive impact of Small Banks for achieving Financial Inclusion. It is estimated that India has 13 bank branches per 100000 people(Gupte et al. 2012) therefore Small Banks will help in alleviating financial inclusion by reaching the unreached, catering individuals with Small Savings Accounts, giving aid to low income household through remittances and micro credit facilities.

CONCEPT OF SMALL BANK

Small finance banks have foster the fundamental financial services in rural and unserved sector of the economy(Rajan, 2016).A small bank must have minimum paid-up capital of 100 crores is required to qualify as above. As per companies act 2013 banks get their license under section 22 of banking regulation act 1934. They can further apply as a scheduled commercial bank if found suitable as per section 42 (6) (a) of the reserve bank of India act,1934, Small finance banks plays a pivotal role in proper channelizing of saving in an efficient and effective manner in rural and semi – urban areas of India, which showing positive signs in overall development. The population which is out of the reach of other commercial banks serves as a target population for small banks. Individuals, Corporate, Trusts or Societies helps in promoting these banks.

According to the guidelines issued by Reserve bank of India small banks can lend up to 25 lakhs. The operations of the bank should be fully networked through technology. RBI took measures for effective financial inclusion and recently granted ‘in-principle’ licenses for 10 small finance banks with an 18-month deadline to start operations. Out of ten entities, eight are micro finance institutions. Among them only Equitas Small Finance Bank has started operating so far. According to the RBI guidelines issued in November 2014, the objective of a small finance bank is to boost financial inclusion by offering credit to small business units, micro and medium enterprises. The guidelines state that 75 per cent of their loan portfolio must lend to the priority sector. These banks have the potential to function almost like a normal commercial bank, but at a much smaller Operating cost. It can offer basic banking services, accept deposits and lend to potential and untouched sector by linking them to formal banking sector. They help in the branch expansion campaign of the Indian Banking system. Branch expansion in the rural area is positively correlated to the economic development of the country (Burgess and Pande, 2003). It also leads to poverty reduction in these areas (Burgess and Pande, 2005). These banks will play a crucial role in the success of financial inclusion in India.

List of Entities who have been granted In-Principle Approval by RBI to open Small Banks are mentioned below: Au Financiers (India) Ltd., Jaipur [from 2 November 2017it has become a scheduled commercial bank], Capital Local Area Bank Ltd., Jalandhar, Disha Microfin Private Ltd., Ahmedabad, Equitas Holdings P Limited, Chennai, ESAF Microfinance and Investments Private Ltd., Chennai, Janalakshmi Financial Services Private Limited, Bengaluru, RGVN (North East) Microfinance Limited, Guwahati , Suryoday Micro Finance Private Ltd., Navi Mumbai, Ujjivan Financial Services Private Ltd., Bengaluru, Utkarsh Micro Finance Private Ltd., Varanasi.

Role of Small Banks to foster Financial Inclusion: The present need of our economy is high quality and secure banking transaction with low cost of delivery to poor people. This will encourage customers to do cash-less transactions which will help the government to track the flow of money that not only reduce black money but also help to develop a robust technological framework (Unda, L. A., & Margret, J. 2015). Traditional branch-based banking model states that the cost of transactions, for a Small bank, need to be significantly lower. The orthodox mentality of people to save at home and lack of trust on formal banking sector creates an obstacle in the path of financial inclusion. The reason behind this roadblock is the paucity of banks in rural areas. The number of rural branches has seen a downfall from 54 per cent in 1994 to 42 per cent in 2016.Many people in

rural areas lend or deposit their hard-earned money through informal sector which framing an obstacle for the government to construct a strong financial system (Jayaratana and Wolken, 1999). Small Banks can change this scenario, these banks can play a role of mobilizer of awareness regarding financial inclusion and help to link the rural economy with formal financial sector (Chakrabarty, K.C. (2013). The main USP of small finance banks is low operating cost which give them an advantage to survive in the market with minimal profit. They also get assistance from government in case of bad debts. The small finance banks are more active in rural area and acquainted with the need of the people. This may also lead to new products and services in order to meet the evolving customer needs. These banks are also capable of lending at low cost to small businesses (Dangi, N., & Kumar, P. 2013).

CONCLUSION AND POLICY IMPLICATIONS

The success of financial inclusion highly depends on financial literacy. The support of small finance banks can help Government to organize workshops to financially educate people. As a financial intermediary, the small bank can bring the untouched sector of the economy in the ambit of formal financial system. It is a win-win situation for both the counterparts for banks. It creates new opportunities to expand its operations and grow its brand value in unserved sector and target niche sector, on the other hand, Government is also able to implement its policies successfully. The current requirement of Indian economy is 4A's (awareness, affordable, accessible and accountable) financial services and Small banks can assist to build a sturdy and financially inclusive economy in India. As there is a positive correlation between financial inclusion and economic growth.

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