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# FINANCIAL INCLUSION

Global Financial crisis has highlighted the importance of consumer protection and financial literacy for the stability of financial sector to ensure inclusive growth

**M**ore than two billion people worldwide go without access to formal financial services, many of them are the world's poorest. Until the recent global financial crisis, the global economy was adding an estimated 150 million new consumers of financial services each year. Most of these new consumers are in developing countries where consumer protection and financial literacy are still in their infancy. Household use of financial services has been rising rapidly in emerging countries, yet consumer protection and financial literacy remain weak. The recent global recession had further worsened the plight of consumers. The global financial crisis has highlighted the importance of consumer protection and financial literacy for the stability of the financial sector.

## FINANCIAL INCLUSION AND INCLUSIVE GROWTH

Financial inclusion refers to ensuring access to appropriate financial products and services needed by vulnerable groups, such as weaker sections and low income groups, at an affordable cost in a fair and transparent manner from the mainstream service providers. The biggest challenge India is facing today is to ensure inclusive growth. It is important to ensure that while the Indian economy grows rapidly; all segments of society are part of this growth process, preventing any regional disparities from derailing such growth. Thus, there is an urgent need today to link all households that are excluded from formal financial services.

Financial inclusion includes access to financial products and services such as no frill bank account, check in account, micro-credit, savings products, remittances

& payment services, insurance, health-care, mortgage, financial advisory services, entrepreneurial credit, pension for old age, business correspondence and self help group branchless banking etc. Lack of access to financial services are due to several reasons such as shortage of sources of financial services in our rural areas, high information barriers and low awareness, inadequate access to formal financial institutions etc. among many others. Those who are excluded are: marginal farmers, landless labor, workers in unorganized sector, urban slum dwellers, migrants, ethnic minorities and other socially excluded groups.

## EXTENT OF EXCLUSION IN INDIA

However the reality is that out of 1.21 billion Indians, only about 40 percent citizens have access to banking services. Only 38 percent (32,000 branches) of the





products are more sophisticated. Progress on financial inclusion therefore carries the risk of producing more inexperienced and vulnerable customers.

### INCREASING COMPETITION

The financial services sector in India has grown rapidly in the past two decades after the economic reforms initiated by the government in the early 90s. Increasing competition from private sector banks and multinational banks has forced the state-owned banks to revamp their marketing strategies and revamp their operational models. Promoting competition in financial services is a key element in ensuring good consumer protection. The creation of a more competitive environment in banking was one of the explicit objectives of the banking sector reform in India and the degree of competition has increased to some extent within the banking system. Several new private banks have started operations and foreign banks have also been allowed to expand their branches more liberally than in the past.

### INNOVATIVE TECHNOLOGIES AND ALTERNATIVE BUSINESS MODELS

Recent developments in technology have transformed banking from the tradi-

(406 million) are having Bank accounts. Hence proliferating mobile phones open another delivery channel for basic financial services to poor people. This technology drastically reduces the costs of convenient and real-time financial transactions, expands access points, lessens the need to carry cash and attracts previously unbanked customers. Several country cases illustrate the promise of mobile payments for financial inclusion.

### ROAD MAP

Many a times, the poor, migrants, disadvantaged and marginalised people, struggle to open a bank account in the absence of a proper identification or address proof. Even the onus of proving identity has been transferred to the individual. Hence they are cut off from the formal chain of financial services.

Hence a key facilitator for enabling the country's banking system to spread its reach in the coming days can be the unique identification (*UID*) number. UIDAI (*Unique Identity Authority of India*), targets to provide unique identity to 600 million residents in next five years, which will address many of the current challenges faced by the banks in delivery of financial services. UIDAI have identified financial inclusion as the main driver for *UID* and enabling e-governance.

The concept of 'bank account number portability', which is in practice in some countries, is that consumers would own their identity reference and could move it between Banks. It is the same way mobile phone numbers are portable and would further stimulate competition within the banking industry. Once again momentum this would be a dramatic shift forward for consumers of financial services. [\(IER\)](#)

## INFORMATION ASYMMETRY BETWEEN CONSUMERS AND BANKS PUTS CUSTOMERS OF FINANCIAL SERVICES AT DISADVANTAGE

bank branches are in the rural areas. More importantly, rural India accounts for just nine percent of total deposits, seven percent of total credit, 10 percent of life insurance and 0.6 percent of non-life insurance business. In rural areas 39 percent of the population is banked against 59 percent in urban areas.

In addition, information asymmetry between consumers and banks regarding financial products and services puts customers of financial services at a disadvantage. This imbalance is greatest when customers are less experienced and the

tional brick-and-mortar infrastructure to a system supplemented by other channels like automated teller machines (*ATM*), credit/debit cards, internet banking, online money transfers, etc. Globally, about four billion mobile phone subscriptions were reported in 2009, well over half of them in the developing world. Mobile phone penetration in developing countries has almost tripled in the past five years, with Asia in particular showing high growth rates. As on February 2011, India alone accounts for 752 million mobile users. Out of this only 54 percent

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*The views expressed in the article are personal and do not reflect the official policy or position of the organisation.)*