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PAPER

The Policy of Financial Inclusion in India
The Paradox of Inclusive Governance

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Abstract The idea of inclusive development has acquired a new dimension in recent times, with rising emphasis of the state policy on resolving socio-economic exclusion through the mechanism of the market, as evidenced by the rise of the 'semi-formal sector' and NGO/ private sector-led microfinance initiatives in countries like Brazil, Bangladesh and India.
In India, this has produced a consolidated discourse of the policy of Financial Inclusion. The main aim of this paper is to study the wider social and political contradictions implicit in the idea of Financial Inclusion in the specificity of the Indian context.

Given the manner in which the initiatives to achieve socio-economic inclusion through the formal financial system are being undertaken, the policy of inclusive finance has become an instrument for the accommodation of socially-inclusive development within the neo-liberal paradigm of individual enterprise, thereby subverting the very rationale of development.

While inclusive development through the formal financial system was a core area of the state policy since the 1950s and was subsumed under the wider imperative of social inclusion, the current policy reveals itself to be more inclined towards accommodative inclusion under a neoliberal financial system, with the consensus that the merits of the 'strategy' of Financial Inclusion lie in that it will hike the profitability of banks if they are able to tap the potential 'market' of the rural poor. This has led to a proliferation of the norm of developmental self-reliance based on entrepreneurship rather than the realization of well-being as an important developmental outcome.

Keywords Development - Financial inclusion - Neo-liberalism - Well-being
Individual entrepreneurship

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Development through inclusive finance: Changing patterns in Indian policy development

The evolving issue of financial inclusion represents an important dimension in the changing approaches to international development issues. The Global Financial Development Report 2014 has defined Financial Inclusion in terms of the "proportion of individuals and firms that

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use financial services"[1] . In the language of international development discourses, this translates into an understanding of financial inclusion as the expansion of public policy to cover the 'unbanked' sections of society or to increase the credit access of low-income and disadvantaged socio-economic groups. According to the Rangarajan Committee report, financial inclusion refers to, "the process of ensuring access to financial services and timely and adequate credit where needed by vulnerable groups…at an affordable cost."[2]

While the provision of financial inclusion entails policy action at the national level, the issue is characterized by an important affirmation of some of the key aspects of the global policy discourse. The concept of financial inclusion combines four major imperatives which makes it relevant to the international development discourse viz. poverty reduction, socio-economic development, individual-centric social self-sufficiency and promoting the role of market mechanisms in accelerating inclusion. While entailing significant internal differences, the idea of financial inclusion seeks to combine the apparently disparate objectives of social development and market intermediation in social policy. Thus, at both the global and national levels, the policy of financial inclusion is reflective of the politics of development in providing a legitimate discursive ground for the World Bank's neo-liberal programmes in national policy.

The policy of financial inclusion in India has followed a complex pattern that has widely reflected the larger patterns of politics of development in India. While financial inclusion gained political and policy currency during the last decade, especially with the debacle of the microfinance industry in Andhra Pradesh (Ananth and Oncu 2013), the government has been playing a steady role in expanding the public access to financial services since Independence. Over the years the government has formed a series of committees to deal specifically with this issue, such as the Vaidyanathan Committee, Thorat Committee, Rangarajan Committee and Raghuram Rajan Committee. Moreover, the efforts of the government to reform the country's financial sector, especially in the wake of the Global Financial Crisis, in the past two years, have also been primarily underpinned by the rationale of accelerating the goal of financial inclusion.

While the broad commitment to financial inclusion, since Independence, affirms the state's institutionalization of financial inclusion within the larger paradigm of development as social welfare, the trajectories followed by the policy of financial inclusion since Independence are reflective of a change in the development thinking from the norm of well-being as the responsibility of the state to the attempts to foster an individualistic culture of self-help. The post-Independence period saw an institutionalization of a large number of initiatives by the government to expand people's access to credit as well as a highly interventionist and political role of the government in the functioning of banks and financial institutions (Basu 2005). The Nehruvian period of the Indian political economic development is distinctive for its focus on the formation of village cooperatives. The creation of a 'cooperative credit network' cemented through cooperative banks and Regional Rural Banks has been one of the major modes through which the government has pushed the policy of financial inclusion (Chavan 2005). The subsequent period, under the government of Mrs. Gandhi, saw the large-scale nationalization of commercial banks in order to direct the flow of credit to priority sectors like agriculture. While the period after the 1991 liberalization and globalization saw a tentative opening up of the banking sector through the distribution of new banking licenses and emergence of new initiatives like the SHG-Bank linkage programme initiated by the NABARD, the regulatory oversight continued to predominate.

1 World Bank. 2014. Global Financial Development Report 2014: Financial Inclusion. Washington, DC: World Bank. doi:10.1596/978-0-8213-9985-9. License: Creative Commons Attribution CC BY 3.0.

2 Report of the Committee on Financial Inclusion. 2008: http://sksindia.com/downloads/Report_Committee_Financial_Inclusion.pdf

This early period of active state intervention in banking policies was, despite the goals it was oriented towards, not the same as the financial inclusion policy of the government that is in evidence today. It was based on the principle of 'social banking' or development banking rather than inclusion Basu (2005; Dev 2006). Under the principle of social banking, the underlying principles were two-fold: the poor are not 'bankable' (Chavan 2005) and the financial institutions have to be subsumed to the imperative of social development. This essentially translates into the policy discourse whereby the poor or the unbanked cannot be treated as a potential market which can be leveraged for long-term gains. Therefore, most importantly, there was little focus on self-help or promoting individual entrepreneurship among the rural poor and more on the idea of providing access to credit through state intervention, framed by a rights-based discourse.

The current policy of financial inclusion, on the other hand, as it has been articulated since 2005 and implemented rigorously since 2010, is based on completely polar principles. It has closer linkages with the microfinance model of administering access to credit, whereby the target population is not treated centrally as the beneficiary of a public good, but simply as one of the stake-holders among multiple other players like banks, government and private sector actors seeking to leverage their own interest through the policy of inclusion or accommodation within the neo-liberal framework of governance. The implicit assumption underlying such a model is that the deregulation of controls would allow banks greater operational freedom in achieving their financial inclusion objectives (Ramachandran and Swaminathan 2005). The new policy is premised on a dual rationale: on the one hand, the objective of financial inclusion will form an important part of the social welfare policy of the government as an important developmental goal, while, from the point of view of supply-side mechanisms, the new policy would also provide incentives to the new actors in a deregulated policy environment to exploit incentives available to them. Accordingly, the new policy has close parallels with the microfinance model, whereby the target groups are treated as consisting of responsible individuals who can interact with the formal financial system through the new culture of viewing the poor as entrepreneurs. This constitutes a neo-liberal discourse which is completely removed from the rights-based framework of social banking under which the early financial development initiatives proceeded. Financial responsibility is no longer defined in terms of the distributive justice idea of 'right to credit' (Hudon 2009) which formed the tenet of the early financial development policy, but rather in terms of individual responsibility to ensure one's own growth in income and assets and pay back the government. This change in the role of the state in development policy heralds implications for the wider notion of well-being in the development discourse.

Socio-economic development under changing financial inclusion policy in India: Factors and implications

In accordance with the theoretical framework that has been laid out in this paper which seeks to understand how the changing policy of financial inclusion in a neo-liberal policy environment implicates the development policy discourse in the country, an assessment of financial inclusion in India needs to be undertaken through an evaluation of two concerns:

First, how effective has the institutionalization of the financial inclusion policies in India been? An evaluation of this factor needs to assess not merely the empirical data on financial inclusion indices, but also question whether macro level effectiveness always translate into micro level effectiveness.

Second, given the discursive developmental foundation within which it is embedded, does this effectiveness translate into substantive developmental outcomes in terms of well-being and how this well-being constructed?

Implementing financial inclusion: Macro and Micro level translation

According to a recent report on financial inclusion, India ranks 29th globally on the Index of Financial Inclusion (IFI) with an IFI value of about 0.198[3] . This is despite the fact that, since 2010, the RBI and the central government has consistently encouraged a number of rigorous supply-side mechanisms to promote financial inclusion for the rural poor. The primary mode through which the RBI has done this is by encouraging Priority Sector Lending (PSL), which consists of agriculture and allied activities and small and medium enterprises, to which the banks have to mandatorily contribute 40% of their total credit, with 18% going to the agricultural sector (Bhunia 2014). The most prominent broad policy goal in this regard has been the systematic and phased implementation of Financial Inclusion Plans (FIPs), the first of which was implemented during the 2010-13 period and the banks have been directed to implement the second phase during the 2013-16 period.

The RBI's assessment of the FIP in its latest Annual Report (Reserve Bank of India Annual Report 2013-14 2014) is significant, as it recaps the huge bulk of financial inclusion initiatives undertaken since 2010 and provides a clear picture of the supply side initiatives taken by the policymakers at the macro level. According to the RBI's performance evaluation of the FIP, there has been a substantial increase in major parameters for assessing the FIP. A computation of the numbers given in the RBI Annual Report yields interesting results in terms of percentage increase from 2009 to 2013. There is nearly a 466% increase in the number of banking outlets in villages. The Business Correspondent (BC) model, whereby banks appoints intermediaries to promote more effective financial inclusion in remote rural and urban areas, has also shown signs of improvement. The number of urban locations covered through BCs has increased from 447 to 60,730, between the year ended March 2010 and year ended March 2014. While the number of basic Savings Bank Accounts (SBAs) has more than doubled, yet there has been far greater growth in the number of SBAs opened through the BCs which have increased nearly ten-fold during this period. However, it is interesting to note that the credit growth and transactions in the BC-opened bank accounts has not been commensurate, even though it tripled during this period. This shows that the supply side policy initiatives are still struggling to create commensurate demand among the unbanked sections of the population.

This is clearly indicative of a discrepancy between the macro and micro level policy coherence and effective translation. While the government reports show impressive supply side numbers, the micro level reality does not always complement them.

More significantly, from a political economy perspective, we need to ask what are the mechanisms and underlying principles through which such demand is being created, how these processes incorporate the target sections of population within the new model of development and how is this indicative of the new development policy discourses. In order to assess these problems, we need to re-contextualize the central rubric of state-led development policy, that is, the idea of ensuring well-being and how that has transformed in the new thinking on financial inclusion.

Reimagining well-being and development

As we have seen, the model of development that underpins the policy discourse of financial inclusion in India has undergone several changes since Independence. The

3 IFI is an index of measuring financial inclusion on a scale of 0 to 1, with 0 indicating complete financial exclusion and 1 indicating complete financial inclusion. The index uses several parameters to measure the coefficient of financial inclusion, based mainly on an assessment of banking penetration in rural areas.

policy trajectory that this discourse has historically followed demonstrates a shift from rights-based social inclusion in the financial system to market-based model that relies on individual enterprise to promote developmental outcomes.

While this shift has not been explicit and the policy of financial inclusion continues to be perceived as broadly lying within the paradigm of state-led social welfare and development, more deep-rooted departures from the welfarist model of development are visible in the principles underpinning the organizational structures of the new policy and the manner in which the policy discourse of financial inclusion has constructed alternative notions of well-being within the recipient population.

This section will look at how the discourse on well-being has transformed within the policy of financial inclusion by assessing three indicative areas: principles of organization and mechanisms of demand creation.

1. Principles of organization

Principles of organization are an important reflection of the policy ideology and discourse. They mark the independent functioning of the government and the private sector by reflecting the prioritizing and operational practices according to wider goals to be achieved. There are several features of the new organizational structure that need to be delineated in this regard:

Partnership model: In order to facilitate smooth implementation, the new structure of the financial inclusion policy envisages the provision of right incentives to the implementing agencies viz. the banks. In a departure from the early institutional norms governing the banking system in which the central government kept the Public Sector Banks (PSBs) firmly subsumed within tight regulatory institutions, the recent years, coinciding with India's economic downturn since 2012, have witnessed a dismantling of these state controls. Two major factors have contributed to this change in regulatory policy vis-à-vis PSBs.

First, the mounting debt or Non-Performing Assets (NPAs) in the public sector banking system in India has significantly exacerbated their dire institutional condition. According to the latest report on asset quality, the net NPAs have doubled from 2.83% a year ago to 5.17% now.[4] Second, on the external front, the Global Financial Crisis of 2008 and the slow and skewed global recovery thereafter, has led to the institutionalization of stringent banking conditions applicable to developed and emerging markets alike. Notable in this regard have been the latest Basel banking requirements that stipulate a high capital adequacy ratio for banks, which is particularly difficult for an emerging market like India to achieve (Foundation 2007). Already caught in the prolonged trap of low growth, high inflation and high fiscal deficit, a uniform implementation of the Basel requirements are difficult for a country like India to achieve, as compared to more advanced economies.

With this background of a crisis and flux in the banking system, the government and the RBI are moving towards a gradual dilution of regulatory oversight. This has been done by encouraging the greater involvement of commercial private banks and private sector financial institutions in achieving the government's financial inclusion objectives, as will be discussed. As a result of this diffusion of new actors, the realization of financial inclusion objectives has come to be framed in the nature of a partnership between different actors. Thus, the PSBs, and the government, are no longer the sole providers of the good of financial inclusion.

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4 Reference link: http://www.moneycontrol.com/news/result-analysis/asset-quality-remainsniggling-worry-for-indian-banks_1216229.html

Rise of new private actors: While the traditional mode of ensuring commercial banks' cooperation in promoting financial inclusion included mandating the fulfilment of priority-sector lending requirements, in recent times, the politics surrounding the implementation of these requirements has become more significant as the policy of financial inclusion has gained ascendancy as one of the primary objectives of the RBI. To foster greater private sector involvement in promoting financial inclusion, the government and the RBI distributed new banking licenses to select private banks. The fact that there had also been intensive lobbying by private sector financial institutions over the months leading up to the distribution of new bank licenses shows that, despite various regulatory and social bottlenecks, shows that the private sector views financial inclusion as a space that can be exploited for high returns.

Thus, more than being an obligation which the banks need to fulfil, there has also been recognition –albeit without successful practice or implementation –of the fact that the vast population of the rural poor or unbanked sections of society can be exploited as a market for potential long-term financial gains. This was clearly visible in the exploitative practices institutionalized by the Micro Finance Institutions (MFIs) in India, which led to a number of suicides by the indebted borrowers in Andhra Pradesh and became the cause of the downfall of the MFI industry.

Changing structure of internal accountability: Mechanisms of ensuring internal accountability form an important part of the function of regulatory oversight. The relationship between the government and the banks in this arena is also indicative of the market-determined institutional underpinnings of the policy of financial inclusion. Apart from the structure of coercion to ensure that the banks fulfil their minimum priority sector lending requirements, there are also provisions for individual-level benefits that provide incentives to the banking personnel to fulfil the financial inclusion requirements. As Shetty and Deokar (2014) note, with reference to the policies mandated by the RBI, the policy of financial inclusion is meant to be a part of the 'business strategies' and 'corporate plans' of the banks, as advised by the RBI to the banks. It is as a part of this wider management approach that the banks have to establish both mechanisms of coercion and incentives. These, for instance, include periodic performance reviews of the banking practices by the RBI, such as a review of the BC model for delivering financial inclusion. The key words in these performance reviews become both efficiency and effectivity. The supply side parameters that they focus on shows little preoccupation with delivering developmental welfare outcomes and concentrate more, in the spirit of corporate organization, on meeting the targets. The fact that the RBI reports show that private and foreign banks perform better in meeting their priority sector requirements would only further cement a management approach to public policy.

2. Mechanisms of demand creation

Creation of demand as a way of widespread legitimization and effectualisation of policy forms an important manner through which the policy is shown to be discursively embedded within larger ideational structures. The effectiveness of the institutions and principles of organization highlighted above depends upon the incentive factor of creating a market that can foster a neo-liberal policy regime of financial inclusion. Thus, in this respect, the creation of demand, within the target population, for the policy of financial inclusion, becomes a key mechanism of institutionalizing the 'market' for financial inclusion. More than creating a market for financial inclusion, this fostering of demand should be viewed within the larger framework of grounding the legitimacy of market mechanisms through the instrument of financial inclusion and the notions of well-being that such a process constructs within the development policy discourse. The central premise is based on the creation of need among the rural poor (Schwittay 2011).

What is particularly significant is that despite the stringent priority sector lending requirements and the difficulty of tapping the potential market that can be offered by the rural unbanked sections of the population, there is no dearth of policy initiatives to realize this goal. The creation of a market in the space of financial inclusion can be substantiated by the key initiatives taken by the RBI to generate demand among the rural poor. The promotion of Financial Literacy forms an important initiative and has informed the new development thinking which realizes the importance of incorporating the target population, as a way of soft mobilization, to legitimize the value, especially the market value, of financial inclusion. In this context, the Nachiket Mor Committee (Committee on Comprehensive Financial Services for Small Businesses and Low Income Households 2014), formed by the government in 2013 clearly recognized the fact that perpetuation of institutional structures will do little to achieve financial inclusion, as the experience of Regional Rural Banks, cooperative banks, Non-Banking Financial Companies, Business Correspondents and Self-Help Groups has shown. They have failed to create the requisite rural market which can be leveraged for promoting financial inclusion in a mutually profitable manner.

Thus, the promotion of financial literacy initiative provides a landmark discursive break in this regard, representing an active mode and a crucial building block through which the rural population can be accommodated within the new policy discourse. The government's major effort in this regard has been the institutionalization of the National Strategy for Financial Education prepared by the Financial Stability and Development Council, through the National Centre for Financial Education. Interestingly, it is not just the government, but also various private actors, such as ICICI bank and the FLAME initiative by IIFL (India Infoline Limited) that are actively intervening to promote financial literacy initiatives.

The new emphasis on financial literacy initiatives as a part of the financial inclusion policy marks a new approach in the government's development thinking. Having moved from social banking to financial inclusion premised on market intermediation, the new emphasis is now on institutionalizing various discursive structures through which a market out of the rural poor can actually be created. The necessity for this has begun to be realized in the government and corporate decision-making centres, as the private sector and PSBs alike perceive the various regulations like lending requirements as a hindrance in face of the fact that they do not yield long term returns on lending to the unbanked population. The rural poor are seen to be afflicted by the double factors of a lack of sustained demand and a lack of capacity which makes the repayment of loan through asset-creation particularly difficult, as has amply been seen in the debacle of the Microfinance industry. This constitutes a severe block in the profits that can otherwise be leveraged through the promotion of financial inclusion, and literacy initiatives constitute an important discursive mode through which the rural poor can be implicitly mobilized to participate in the current model of neo-liberal financial governance.

Conclusion

In this paper, it has been argued that the current policy of financial inclusion in India constitutes a new phase in the development discourse. An analysis of the evolution of financial inclusion since Independence shows the broader neo-liberal line of transformation that has shaped it. Under the current policy, this can be substantiated by looking at the principles of organization and construction of well-being that underlie the current financial inclusion policy. An analysis of both these factors is reflective of the new governance and development discourse that is taking place through the avowedly social objective of financial inclusion.

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