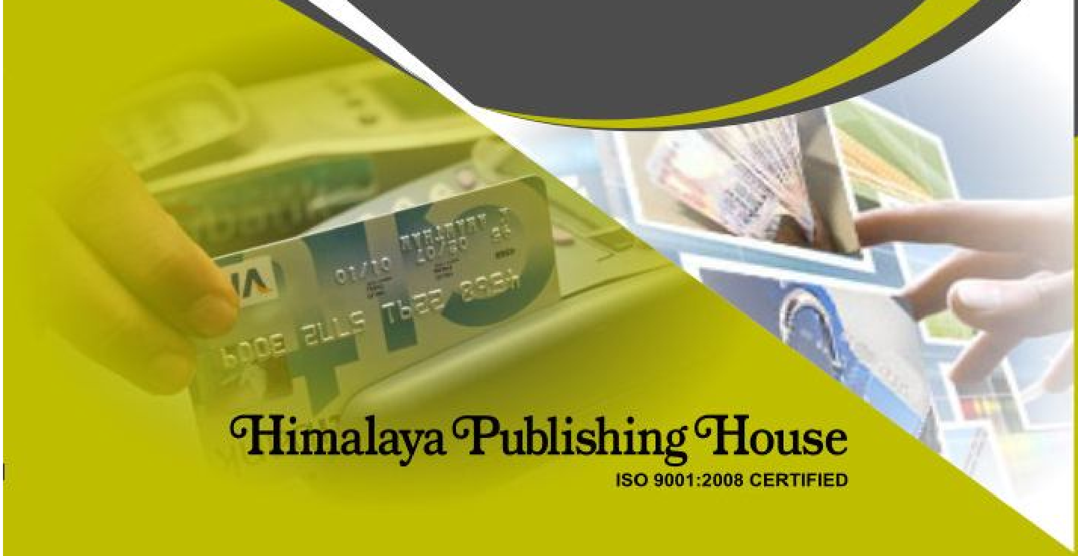
Emerging Trends in Finance and Banking

Pavnesh Kumar



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Dedicated to my Parents who bestowed on me the inspiration and strength to take up this work

Preface

The fast changing volatile and dynamic financial landscape is creating a new set of environment for the companies and forcing the practitioners and researchers to develop new insights adopt the changes at a fast pace than before. This book discusses some of the emerging trends in the area of finance and banking.

This current book entitled ***Emerging Trends in Finance and Banking*** discusses various emerging trends in finance and banking. The book contains sixteen articles and is divided into four parts.

The first part is **Emerging Trends in Financial Inclusion** contains five chapters covering the discussions on financial inclusion, role of NGOs in financial inclusion and rural economy and financial inclusion in Indian perspective.

The second part of the book **Emerging Trends in Banking** contains six chapters covering the discussion on performance evaluation of Indian banks, Islamic banking, rural banking and comparative study of public and private banks.

The third part of the book contains two chapters on **Emerging Trends in Microfinance** covering the discussion on microfinance and role of technology in microfinance

The fourth part of the book contains three chapters on **Emerging Trends in Insurance and Accounting** covering discussions on process design of health insurance, post office role in microfinance and XBRL.

All the chapters contained in the book are application-oriented and therefore will provide useful guidance to the practitioners as much as thy will to the researchers

Dr. Pavnesh Kumar

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Like others, I owe much to many. I am particularly grateful to Prof. Y.P. Singh and Prof. S.K. Singh (FMS-BHU) (the latter being the Ex-Professor Delhi School of Economics) of University of Delhi. They are my source of inspiration and strength. I am also grateful to Prof. G.S. Rathore my Research Supervisor who helped me in several ways – all the time.

Editing this book has been an enriching experience in itself. I express my sincere thanks and gratitude to all those who extend a helping hand in the completion of this book. My main motivator is, of course, the publishers Himalaya Publishing House Pvt. Ltd.

I am also grateful to my seniors, colleagues, friends and students for being a continuous motivator during editing of this book.

Coming to my home, my wife Pooja Singh have continuously helped me to meet my minor errands. I am grateful to her.

Dr. Pavnesh Kumar

Contents

Financial Inclusion: Emerging Trends

Umesh Kumar Singh*

Though the Indian Banking industry has performed double digit since the past 10 years, but still there remains some unmet customer needs, and most important among these is to extend its arms to every realm of the society. In other words, the Financial Inclusion. Although there are challenges to address this, but these challenges make way for opportunity if dealt with significant innovation and specialized skills. *In a fast growing economy like India, today's poor is the middle class of tomorrow and banks could, therefore, ill-afford to ignore this segment.*

In our country, almost half of the populace is unbanked with over 50% of the population not having deposit account. Less than one-fourth of the India's population has debit cards and less than 2% has credit cards. These sections of the society just need access to the financial services. There cannot be any instance where an agrarian economy can transform into a developed one without broad-based financial inclusion. The economy prospers when its people prosper. Lots of attempt has been made in this regard, and lot more is required to stand out as a powerful Indian economy. Some of the significant steps were cooperative movement, nationalization of banks, establishment of RRBs and financial inclusion the next step ahead.

"Financial Inclusion" was formally articulated by Dr. Y.V. Reddy, the then Governor, RBI in the Annual Policy Statement of 2005-06, while recognizing the concerns in regard to the banking practices that tend to exclude rather than attract vast sections of population, urged banks to review their existing practices to rethink them looking into the objective of financial inclusion. The main features of the approach involve 'connecting' people with the banking system and not just credit. Financial exclusion is mainly in two ways — one is exclusion from the payments system, i.e., not having access to a bank account and the second type of exclusion is from formal credit markets.

THE JOURNEY SO FAR

Since then, a several mile journey has been made by the coordinated effort of all the channel partners such as banks, financial institutions, technical service providers etc. The various steps taken in this regard include:

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No-frill Accounts: The first step to bring the poor unbanked people starts with their bank accounts, and the main hindrance to this is the complicated KYC documentary requirements and maintenance of minimum balance which cannot be expected from this section of the society. No-frill accounts which requires nil or very low minimum balance requirement and with simplified KYC norms created a milestone in implementation of Financial Inclusion. 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.

Business Correspondent/Business Facilitator Model with Use of Technology: The next step is the accessibility of this population to the banking services. Very often, the nearest bank branch is quite a distance from the village where the person resides. Travel to the branch could mean loss of a day's earnings. Technology helps us provide banking at the doorstep of the customer. And what could change the way banking done in rural areas is the RBI's decision to allow banks to use or build a network of banking correspondents (BCs). It is the BC who is the umbilical cord between the customer and the bank. The BC is provided with a hand-held device that can store and transmit data pertaining to a customer. To secure the transaction, the customer is usually provided with a smart card (which has a micro-chip storing his personal details). The BC Model allows banks to provide doorstep delivery of services especially to do 'cash in – cash out' transactions, thus addressing the 'last mile' problem.

Relaxations in KYC Norms: To facilitate easy opening of accounts especially for small customers, RBI has simplified the Know Your Customer (KYC) norms to such an extent that small accounts can be opened without any documentation by just giving a self-certification in the presence of bank officials. Further, in order to leverage upon the initiative of UIDAI, RBI has allowed 'Aadhaar', the unique identification number being issued to all citizens of India, to be used as one of the eligible document for meeting the KYC requirement for opening a bank account. Recently, in September 2013, RBI has allowed banks to provide e-KYC services based on Aadhaar, thus paving the way for account opening of all the people.

Simplified Branch Authorization Policy and to Open Branches in Rural Unbanked Areas: To address the issue of uneven spread of bank branches, in December 2009, domestic scheduled commercial banks were permitted to freely open branches in Tier 3 to Tier 6 centers with population of less than 50,000 under general permission, subject to reporting. In the second quarter review of Monetary Policy, Branch authorization has been relaxed to the extent that banks do not require prior permission to open branches even in Tier I centres, subject to reporting. Further steps to this banks have been mandated to open at least 25% of the branches in unbanked rural areas.

Roadmap for Providing Banking Services in Unbanked Villages with Population More and Less than 2000 by RBI: A phase-wise approach to provide banking services in all unbanked villages in the country was adopted. Under the Financial Inclusion Programme 'Swabhiman' on completion of the first phase, 74,194 villages with population more than 2,000 were provided with a banking outlet, and now in the second phase the remaining unbanked villages with population less than 2000, numbering close to 4,90,000 are identified and allocated to banks, for opening of banking outlets by March 2016.

Sub-service Area Concept: As per the directives of Ministry of Finance, Government of India, it shall be the endeavor to ensure that there is at least one bank branch/Business Correspondent Agent (BCA) in every Gram Panchayat(s). Since the population of Gram Panchayat varies across the States, banks need to ensure that about 1,000 to 1,500 households are available in the sub-service area of BCA for effective implementation of DBT.

Financial Literacy: Financial Literacy is an important adjunct for promoting financial inclusion. RBI has designed a mass-scale Financial Literacy Programme with an objective to integrate the financially excluded population having low level of income and low literacy level with the formal financial system. Financial Literacy Centres organize Outdoor Literacy camps in their respective Districts wherein along with creating awareness, accounts are also opened in the Literacy camps. The programme has been received well on the ground as an integrated approach of financial inclusion through creating awareness and providing access simultaneously.

Financial Inclusion Plan of Banks: The first phase of FIPs was implemented over the period 2010-2013. The Reserve Bank has used the FIPs to gauge the performance of banks under their FI initiatives. A snapshot of the progress made by banks under the three-year Financial Inclusion Plan (April 10 to March 13) for key parameters during the three-year period indicates that banking outlets increased to nearly 2,68,000 banking as on March 13 as against 67,694 banking outlets in villages in March 2010. 7,400 rural branches have been opened during this period of three years. Nearly 109 million Basic Savings Bank Deposit Accounts (BSBDAs) have been added, making the total number of BSBDA to 182 million. Share of ICT-based accounts have increased substantially. Percentage of ICT accounts to total BSBDAs has increased from 25% in March 10 to 45% in March 13. About 4,904 lakh transactions have been carried out in ICT-based accounts through BCs during the three-year period.

THE WAY FORWARD

Although large network has been created with these efforts and a lot of unbanked population have came into the formal banking system through the services of BCs and by opening bank accounts, however simply creating the banking infrastructure and opening banking accounts will not fulfill our objectives of achieving total Financial Inclusion. There is a need to have more and more transactions in these accounts and to deliver micro-credit, small value asset products and micro insurance through this platform to make the business viable. Some of the current programmes of the government and banks which may lead to a great revolution in this field and proper utilization of the infrastructure are:

Direct Benefit Transfer: The introduction of direct benefit transfer validating identity through Aadhaar will facilitate delivery of social welfare benefits by direct credit to the bank accounts of beneficiaries. Government proposes to route all social security payments through the banking network using the Aadhaar-based platform. It has been rolled out in 121 Districts in two phases and expected to cover all over the country in future. Under DBT-LPG Scheme, LPG consumers can get their gas subsidy directly credited in their Bank accounts. As on 30th September, the scheme has been implemented in 54 districts and it has been targeted to implement in 289 Districts of the country by 1st January 2014.

USSD-based Mobile Banking Services: TRAI has come out with guidelines and tariff on unstructured supplementary service data (USSD)-based mobile banking services. USSD technology is used by telecom operators to send alerts to their users. It can be used for prepaid call-back service, location-based content services and menu-based information services. TRAI has come out with a framework to help bank agents to interface with service providers for the use of SMS, USSD and IVR channels to provide mobile banking services. The authority wants to utilize the benefits of mobile banking for “financial inclusion”. The Mobile Banking (Quality of Service) (Amendment) Regulations, 2013 have come into immediate effect and the Telecommunication Tariff (56th Amendment) Order, 2013 shall come into force on January 1, 2014. On September 30, 2013, there were about 87 crore mobile subscribers in the country of which about 35 crore were in the rural areas. The fact that large number of mobile subscribers in rural areas does not have access to banking facilities presents an opportunity for leveraging the mobile telephone to achieve the goal of "financial inclusion." (*Source: Press Release of TRAI, Chairman, Rahul Khullar, Dated 27.11.13)

Aadhaar-enabled Payment System or **AePS:** Developed by National Payments Corporation of India, its working is based on unique identification number for individuals called Aadhaar. The system allows an Aadhaar holder to carry out financial transaction on a micro-ATM provided by the banking correspondent. It is an initiative towards providing improved social security benefits and financial inclusion of the underprivileged people. AePS was launched in March 2011. The pilot project was launched in Jharkhand state in association with three banks – Bank of India, Union Bank of India and ICICI Bank. The AePS is being used in many districts from 1st January 2013 for payment of social security pensions, scholarships, NREGA wages, subsidies on LPG and PDS by various state governments and the Union government. The government is implementing the AePS in a phased manner – to cover all districts of India. Andhra Pradesh is the first one to use it on pilot-basis for PDS subsidy in the East Godavari district from September 2012. AePS allows balance inquiry, cash withdrawal, cash deposit and Aadhaar-to-Aadhaar funds transfer. All that a customer needs for availing of the AePS services is an Aadhaar number. These transactions are biometric-based transactions in which routing of authentication request to UIDAI is done by NPCI. It is a real-time payment system; the account gets debited/credited instantly upon successful authentication. It also includes transactions like best finger detection, E-KYC and demographic authentication. All the banks participating in AePS comply to interface specification published by NPCI.

WHAT ELSE CAN BE THE PACE MAKER?

The Right Direction for Greater Reach: In a country like India, where there is a great diversity of demography as well as geography, ranging from densely populated areas like UP to sparsely populated States like Madhya Pradesh, and Arunachal Pradesh, Costal plain areas like West Bengal and Gujarat to Hilly and remote areas like North Eastern States. Accordingly, the challenges for Financial Inclusion are different in different places. The present model of Financial Inclusion mainly targets to cover the villages having population more than 2000 and less than 2000 or through SSA approach where one BC/Branch should cover 1000-1500 households, both of these models are focusing on Demography but not Geography and very much suits the places which are densely populated. But in case of the sparsely populated and hilly areas, where there are very small villages lying in the remote places having miles of distance in between them, coverage of 1000-1500 households through a single BC may not be feasible. In that case, we have to go away from the population-based approach and to cover the villages keeping in mind the distance as the criteria, say one BC/CSP to cover the unbanked villages within a radical distance of 4-5 km. The model has already been adopted by Government of MP successfully.

Banks May be Subsidized by the States: The Break-even point for the banks' business through BC model under financial inclusion is normally 4-5 years and banks need to invest a lot of capital for enrollment and issuing Biometric smart cards. If State governments can subsidize the banks for this activity, the model can break-even earlier and the Financial Inclusion Project can be more viable for the banks and they will show a greater interest in this.

There should be a Rating model for the BCAs and the Best Performing BCAs should be incentivized to boost up their morale and to bring a competitive environment among them.

FI Index for Every District: There is a need for an FI index for every District, based on the level of penetration of FI activity, level of infrastructure available etc. so that the District administration will be more proactive in better implementation of FI activity in their Districts.

Mobile vs. Static Model of Banking Outlets: In the mindsets of the villagers, there is an inclination towards the static banking outlets. Their level of confidence is more for the Branch rather than the mobile BCs. Hence, more focus should be given to the static model of BC outlets and the BCs should be made a part of the banks' human resources through a separate vertical.

Government has to play a major role to build up the supply side of financial inclusion through financial literacy and making all the payment of the social schemes through the banking channel to make the model viable.

Successful implementation of financial inclusion will be a win-win opportunity for the poor, the bank and for the country. By bringing the poor to the mainstream, financial system will improve thereby decreasing the rich-poor gap which is the root cause of development of anti-social activities by the poor population. For the bank, it will be a lucrative business opportunity in the long run and all will help in the overall economic development of our country.

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