Status of Financial Inclusion: A Comparative Study with respect to India and China

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Abstract

The term 'financial inclusion' has become a topic of indubitable importance since the onset of the 21st century, after it was identified that financial exclusion has a direct correlation with poverty in an economy. Since then, several countries around the world have introduced various measures to promote the spirit of financial inclusion in their economies. Financial inclusion refers to the act of imparting equal access and availability of financial products and services to all individuals and businesses, especially the lower-income and economically weaker sections of society. This study aims to highlight the significance, dimensions, policies, initiatives and challenges involved in the process of accomplishing financial inclusion in the developing countries of India and China. In addition to this, the study will also take a deep dive into understanding and analysing the progress as well as the current position of financial inclusion by undertaking a comparative study of the economies of India and China.

Keywords: Financial Inclusion, India, China, Economy

Introduction

The Reserve Bank of India introduced the term financial inclusion in India around 2005. Financial inclusion is "the process of ensuring access to appropriate financial products and services needed by all sections of the society in general and vulnerable groups such as weaker sections and low-income groups in particular at an affordable cost fairly and transparently by mainstream institutional players" (K.C. Chakrabarty, 2011). Financial inclusion is "the use of financial services by individuals and firms. Financial inclusion allows individuals and firms to take advantage of business opportunities, invest in education, save for retirement, and insure against risks" (Demirgüç-Kunt, Beck, and Honohan, 2009).

On comparing these two definitions, we see that on a global level, financial inclusion is mainly defined as the equal availability and accessibility to financial products and services (such as insurance, credit, equity, banking, etc.) for everyone. But, when it trickles down to India, a special emphasis has to be paid to the economically vulnerable population as financial support and access would further lead to income equality, employment generation, poverty alleviation, improved quality of life and socio-economic welfare. The exigency of providing such special attention is due to the history of exploitation, exclusion and neglect of the weaker sections in India.

A similar situation can be seen in the case of China, where more financial services are being provided to MSEs and other marginalized groups, due to the rapid advancement and development of the financial sector. The population of people having a bank account jumped from 63.3% in 2011 to 79.3% in 2017. India also caught up with China, as the number of adults having a bank account skyrocketed from 58.7% in 2011 to 80% in 2017.

If we look through the years, we notice how similar the origin of economic development has been for both the countries. India got independence in 1947 while People's Republic of China was formed in 1949, starting with their development plans in 1951 and 1953 respectively. Despite different efforts and strategies, till the 1980's, both the countries had almost similar growth rates and per capita incomes. Thus, when evaluating India, China becomes an efficient parameter for comparative assessment.

Objectives of the paper

1. To understand the imperativeness of financial inclusion in the growth and development of an economy.
2. To evaluate the progress made for inculcating financial inclusion by analysing the economies of India and China.
3. To evaluate the incorporation of digital technology in promoting financial inclusion in the two economies.

Research Methodology

This study is based on secondary data and sources collected from various research papers, reports and articles published by distinguished authors and reputable organizations like the Reserve Bank of India and World Bank. The potent data has been sourced from the official websites of the Government of India and China, their Central Banks, and the official pages of various schemes. The paper dives into the challenges to and initiatives taken for curbing financial exclusion in both the countries and analyses the progress reaped and the current status of financial inclusion in India as well as China. Further, the use of digital technology in promoting financial inclusion in the two countries has also been discussed in the comparative analysis.

Literature Review

As per United Nations, "financial access means access to a full suite of financial services, provided with quality, for everyone who can use financial services, thereby leading to an increase financial capability."

The State Council of the People's Republic of China defines financial inclusion as a "process by which individuals and groups access appropriate and effective financial services and products at affordable costs, based on equal opportunity and business sustainability."

Singh and Tandon (n.d.) give an insight into the economic gap that exists due to financial inclusion and analyse how the microfinance models can effectively solve the problem of financial inclusion in the country, leading to economic growth.

Siddique (2018) has created a link between religion and caste and bank account ownerships, studying the social impacts and the importance of education in eradicating bias.

Zhu et.al. (2018) have analysed the importance of financial inclusion for the sustainable growth and development of the Chinese economy and measured whether the development of financial inclusion in China is itself sustainable.

Omar and Inaba (2020) in their paper have displayed vital shreds of evidence that the poverty rates and income inequality prevalent in developing countries can be effectively solved by financial inclusion.

Advantages

Guruprasad et.al. (2019) have identified 9 potent benefits of financial inclusion. These benefits are the availability of credit to people further allowing them to invest and grow financially; availability of payment services to them; prevention of their exploitation under money lenders through formal loan facilities; inducing the practice of saving money for future emergencies and requirements; provision of insurance facilities for unforeseen incidents; aid in country's capital formation; implementation of subsidy and scholarship schemes designed by the government; country development and growth as well as economic ascension. Thus, financial inclusion proves to be of utmost significance as it provides the necessary thrust to the developing economies like that of India and China.

Initiatives Undertaken

Both the Governments of India and China recognized the vitality of ensuring financial inclusion in the economy. Therefore, to propel and ensure inclusivity, various schemes and policies were launched to aid this objective. Let us first look at the policies launched in India:

1. Indian Government Plans and Initiatives

The 11th Five Year Plan (2007-12) was the first to envision a "faster and more conclusive growth" of the country. Pradhan Mantri Jan Dhan Yojana (PMJDY), commenced in 2014, has proved to be the torchbearer of financial inclusion in the country. With six pillars: universal access to banking facilities; financial literacy program; micro-insurance; basic banking account with overdraft facilities; creation of Credit Guarantee Fund; and unorganized sector pension schemes, PMJDY has been a harbinger of prosperity and development. (Figure 1)

Other than PMJDY, the government has launched several other policies to spur financial inclusion in the country. Atal Pension Yojana (APY), launched in 2015, provides the people working in the unorganized sector with a pension of up to INR 5000 per month along with tax benefits. It renders security to the low-income senior citizens to provide them aid in cases of diseases, accidents, etc.

Pradhan Mantri Suraksha Bima Yojana (PMSBY) can be availed by all the subscribing bank account holders falling in the age range of 18-70 years. Under this scheme, the subscriber shall be provided with risk coverage of INR 2 lakh in the event of accidental death or full disability and INR 1 lakh in case of partial disability for a premium amount as meagre as INR 12 per annum per subscriber.

Furthermore, Pradhan Mantri Jeevan Jyoti Bima Yojana, introduced by the Government in 2015, provides a life cover of INR 2 lakh on the death of the insured (subscriber) in return of a premium of INR 330 per annum per subscriber. It is obtainable by bank account holders in the age group of 18-50 years, who have consented to join auto-debit. Some of the other Government initiatives include Pradhan Mantri Vaya Vandana Yojana (PMVVY), Pradhan Mantri Mudra Yojana (PMMY), Stand Up India Scheme among others.

2. Chinese Government Plans and Initiatives

The Communist Party of China, in 2013, announced the initiative to inculcate financial inclusion in the Third Plenary Session. Moreover, in December 2015, the State Council of China issued the 'Plan for Advancing the Development of Financial Inclusion' (2016–2020). The plan outlined the areas for improvement in availability, satisfaction and quality of financial products and services. The target customer segments were mainly the low-income groups, MSEs, rural residents, elderly, poor, and the disabled. The plan also highlighted the importance of incorporating digital technologies to enhance financial inclusion. Over 95% of the online population accesses internet through mobile phones.

Various policies like monetary, tax and supervision policies were also introduced to diminish the operational as well as communication cost of serving customers and to boost technology and innovation in the economy. In September 2016, the Chinese Ministry of Finance issued Administrative Rules for Earmarked Funds of Financial Inclusion. Earmarked funds can be used for purposes such as rewards for a progressive increase in agriculture-related loans by national financial institutions; providing subsidies to the rural financial institutions; and providing interest subsidies for guaranteed loans to business start-ups.

The Chinese government has also been actively working to develop government-owned guarantee companies. These companies will share the credit risk of MSEs and other underserved market segments. In Zhejiang province, these companies are providing a guarantee of 50% of the entire investment not surpassing RMB 10 million for growing technology firms.

The government also promotes agricultural insurance in the country by providing subsidies. In 2016, the central government apportioned RMB 15.8 billion for agricultural premium subsidies, which constituted 38% of the total agricultural insurance premiums. Various tax reduction measures were also undertaken. These include exemption of VAT on interest income of small loans provided to the farmers; exemption of stamp tax for loan contracts between financial institutes and MSEs; and raising the pre-tax deduction standard for loan loss reserves.

3. Reserve Bank of India Initiatives

The RBI suggested the concept of BSBD (Basic Saving Bank Deposit), previously under the no-frill accounts, requiring no minimum balance along with provisions of ATM, electronic payments and other facilities to the poor and financially excluded.

RBI also created the FIF (Financial Inclusion Fund), with an initial corpus of INR 2000 crore to fuel the process of financial inclusion in the country through capacity building and technology adoption. Additionally, it set up SFBs (Small Finance Banks) to provide a means of saving facilities and credit to the small business units, micro and small industries, marginal and small farmers, unorganized sectors and others at a lower cost.

The RBI has launched the Lead Bank Scheme, with special emphasis on suburban and rural areas, to support the development of small-scale industries, agriculture and other unorganized sectors. It also directed the banks to set up at least 25% of the total number of their branches in unbanked villages, along with relaxing KYC norms and banking charges.

To disseminate financial literacy, the RBI advised the scaling up of financial literacy programs in the FLCs (Financial Literacy Centres) to educate and encourage people to become financially included. As of December 2020, there were 1,478 FLCs in India. The RBI has also undertaken the "Project Financial Literacy" to promulgate the general information regarding RBI itself and basic banking concepts.

Construction of simple low-cost brick and mortar structure with BCs (Banking Correspondents) for cash management, grievance redressal, documentation, etc., with minimal but adequate facilities to enable smoother transactions and better services to the people. For systematic and effective acceleration of financial inclusion, the RBI has also put out the National Strategy for Financial Inclusion (2019-2024).

The following are the various policies and initiatives undertaken in China to enhance the inclusive growth of the country:

4. People's Bank of China Initiatives

Just like RBI, the People's Bank of China (PBC) has taken several cleverly fruitful measures for upscaling financial inclusion in China. The PBC incentivized the MSEs and rural industries by employing various strategies like differentiated required reserve ratios, refinancing of loans, and rediscounting of loans.

Since 2018, PBC has made efforts to reduce the required reserve ratios to be maintained by the commercial banks. In May 2020, the average reserve ratio was around 9.4% which is 5.2% lower from 2018. To curb the impact of COVID-19, the ratio was further reduced to 8.9% as of July 2021.

The PBC also prudently advanced pilot programs for mortgage loans in the villages by allowing "two rights" as collateral (i.e., management rights to contracted rural land and housing property rights to farmers); encouraged financial institutions to issue debt financing instruments to MSEs and encouraged MSEs to procure funds through financial bonds.

Challenges to Financial Inclusion

From socio-economic to political, there are multiple reasons why both of the countries still face financial exclusion. Kempson, Atkinson, and Pilley (2004) pointed out six major causes of financial exclusion (banking), varying from country to country, namely: refusal by banks themselves to provide services; absence of identity cards and proofs by the poor; restrictive terms and conditions imposed on the people; high bank charges, physical issues due to closure or non-availability of banking institutions; psychological and cultural barriers as well as social security payments. The aforementioned problems apply to both the countries under the study.

1. Challenges faced in India

One of the leading challenges to financial inclusion in India is the non-availability of banks and other financial institutions, especially in rural areas. Such remoteness of the financial service providers is a major discouragement to the already impoverished and unaware population, who would invest time in working a bit more than to learn of such opportunities. Even if there are financial institutions around, there is a good chance that the inadequacy of the services provided, along with high transactional and operational costs, would drive the underprivileged population away from the notion of financial inclusion.

The illiterate and uneducated population of the country may get unnerved by the complex and inflexible procedures required for availing the financial services. The requirement of extensive proof and documentation further adds to their reluctance. Moreover, sometimes people don't turn to these services simply because they don't possess the wealth to avail such services. There is hardly any surplus income left to be utilized for other purposes.

The masses may sometimes involuntarily choose to remain financially excluded due to preconceived notions and prejudice against the formal financial sector, either due to psychological preconception (brainwashing or fear induced by informal money lenders) or sociological bias.

The rampant red-tapism, corruption and other malpractices cultivate a lack of trust amongst the already exploited poor people. In addition to this, lack of financial education, literacy and awareness can count as some other major challenges to financial inclusion prevalent in the country.

2. Challenges faced in China

For many Chinese citizens, the concept of financial inclusion is still synonymous with credit subsidies, direct lending and charitable deeds. There is an urgent need for a transformation in the conceptualization of financial inclusion into a more evolved and widely accepted model. This will ensure that the vision of attaining full financial inclusion in China is attained in the future.

There is a high level of state interference in public sector commercial banks and state-affiliated financial services providers. This resulted in discouragement of competition and innovation and had a twisted impact on the market. The key challenge is to lay down the apt role of the government in the operations of these service providers.

In rural areas, problems like low per-capita income, lack of diversified economies, and underdeveloped infrastructure, hinder financial service providers from operating profitably. In urban areas, challenges like lack of information symmetry, scarcity of pledges or mortgages, insufficient credit data, and massive transactional costs are to be seen.

Achieving sustainable financial inclusion requires innovation especially in the digital upfront. But several risks are associated with digital technologies like operational or consumer risks. Chinese authorities face the challenge of balancing the two-fold objectives of developing an environment for innovation while simultaneously monitoring and controlling risks.

The Village and Town Banks (VTBs) and

Microcredit Companies (MCCs) face several challenges in the country. Major VTBs face problems like exorbitant operational and management costs and limited innovation; while MCCs face problems like a limited array of funding sources, huge costs, and heavy tax burdens.

The financial literacy and capability of consumers is an integral part of financial inclusion. But as per the reports of a survey conducted by PBC in 2017, there exists relatively low awareness regarding risks amongst consumers, lack of implementation on family expenditure plans, and incomplete understanding of contracts and statements of financial products.

Comparative Analysis

Despite the challenges faced by both countries, the diligent efforts of the central banks, financial institutions and governments of India and China have led to a remarkable improvement in the financial inclusion status of the country. Analysing the current progress and status of financial inclusion in both countries, we can deduce that the governments and central banks have indeed been successful.

As per the Global Findex 2017, the percentage of Indian adults possessing a bank account rose from an estimated 53% in 2014 to a whopping 80% in 2017. These figures when compared to those of China, whose 80% of the individuals and 96% of the enterprises have bank accounts, is quite similar. The same Findex reflected that 77% of the women in India had bank accounts as of 2017 as compared to 43% in 2014.

Moreover, India has achieved impressive conclusive progress in financial inclusion as derived from the RBI Annual Report of 2020-21. (Figure 2)

To accelerate financial inclusion, the RBI has released the National Strategy for Financial Inclusion (2019-2024), which "sets forth the vision and key objectives of the financial inclusion policies in India to help expand and sustain the financial inclusion process at the national level through a broad convergence of action involving all the stakeholders in the financial sector."

The RBI recently constructed a composite Financial Inclusion Index (FII) to capture the degree of financial inclusion across the country (RBI, 2021). The Reserve Bank of India released the FII for the period ended March 2021, which stood at 53.9 in comparison to the value of 43.4 for the period ending March 2017, reflecting a 10% improvement in the quality and quantity of financial inclusion in the country.

At the same time, China too has accomplished tremendous success in expanding the utilization of a vital financial instrument i.e., store-of-value transaction account. As per the 2014 Global Findex Survey, 79% of Chinese adults own at least one store-of-value transaction account. Financial infrastructure such as automated teller machines (ATMs) and point-of-sale (POS) has brilliantly increased in China over the past years, with 1.1 million ATMs and 31 million POS as of 2019. (Figure 3)

Started in 2006, the initiative of setting up VTBs has seen major progress. The number of VTBs has escalated rapidly and reached 1633 as of June 2019. More than 90% of loans from VTBs were made available to MSEs and the local farmers.

Apart from these, Fintech too has started playing a major role in accelerating financial inclusion. With a fintech adoption rate of 87%, India can foresee a fertile trajectory to viable financial inclusion in terms of lending, borrowing and financial management. Some of the fintech models that can catalyse financial inclusion in India are: IMT (Instant Money Transfer) Facility, e-KYC Incorporation, smart villages and panchayats with virile banking infrastructure, No-frills account, EBT schemes, etc.

China has also performed exceptionally well in terms of incorporating digital financial inclusion into the economy. The number of digital payments has significantly increased, many Internet banks like WeBank and MyBank have emerged along with massive growth in internet microfinance. Companies like Alibaba and JD are providing small loans to shop owners through their e-commerce platforms.

There also has been a significant increase in P2P networks since 2007 which not only suffice the needs of MSMEs but also lend to individuals. China's private fintech companies have made online purchases easier for citizens. Companies like AliPay and WeChatPay have over 475 million and 600 million subscribers respectively, who use these platforms for online purchases.

Limitations of the study

This study is entirely based on secondary data and relies on the sayings of eminent personalities. No statistical tool was used to analyse any primary data. The study only covers the countries of India and China and has not taken into consideration the rest of the countries.

Moreover, no comparison has been made between the two countries in terms of demographic, geographical and economical background.

FIGURES

Bank Name / Type	Number of Beneficiaries at rural/semiurban centre bank branches	Number of Beneficiaries at urban metro centre bank branches	No Of Rural-Urban Female Beneficiaries	Number of Total Beneficiaries
Public Sector Banks	21.65	13.02	19.12	34.67
Regional Rural Banks	7.00	1.00	4.62	8.00
Private Sector Banks	0.70	0.58	0.70	1.28
Grand Total	**29.35**	**14.60**	**24.45**	**43.94**

Figure 1: Pradhan Mantri Jan-Dhan Yojana, Progress Report 2021 (All figures in crore) (Beneficiaries as of 24 November 2021)

Particulars	March 2010	December 2019	December 2020
Banking Outlets in Villages-Branches	33,378	54,481	55,073
Banking Outlets in Villages >2000*-BCs	8,390	1,28,980	8,51,272
Banking Outlets in Villages <2000*-BCs	25,784	3,83,864	3,85,537
Total Banking Outlets in Villages-BCs	34,174	5,12,844	12,36,809
Banking Outlets in Villages-Other Modes	142	3,473	3,440
Banking Outlets in Villages-Total	**67,694**	**5,70,798**	**12,95,322**
Urban Locations Covered Through BCs	447	5,51,327	3,24,345
BSBDA - Through Branches (No. in Lakh)	600	2,558	2,891
BSBDA - Through Branches (Amount in Crore)	4,400	90,731	1,25,898
BSBDA - Through BCs (No. in Lakh)	130	3,409	3,601
BSBDA - Through BCs (Amount in Crore)	1,100	62,095	77,163
BSBDA - Total (No. in Lakh)	**735**	**5,967**	**6,492**
BSBDA - Total (Amount in Crore)	**5,500**	**1,52,826**	**2,03,061**

* Village Population
Source: Reserve Bank of India Annual Report 2020-21

Figure 2: Financial Inclusion Plan: A Progress Report

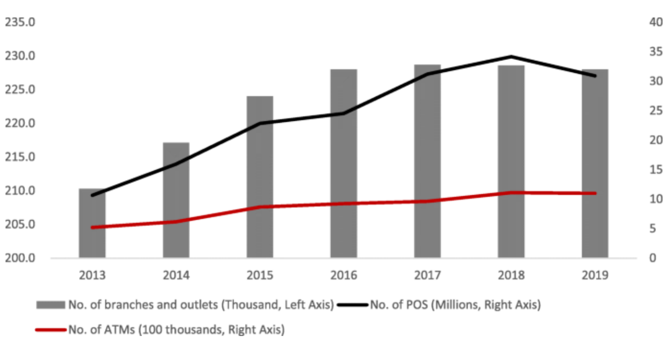

Figure 3: Physical reach of Chinese banking financial institutions

Conclusion

India and China, having gained Independence nearly at the same time, have come a long way in their ardent efforts to accelerate the inclusive growth of their economies as well as their residents. We can deduce that financial inclusion, though seems a vast concept, is just a domino, which when pushed, puts into action the significant drivers of economic and financial progression, eventually leading to greater social equality, better standard of living and mitigated poverty.

On analysing the current progress of India and China, it is clear that both governments are trying to ensure complete financial inclusion by introducing various schemes and setting up financial instruments in their respective economies. The policies and initiatives have been well-drafted and implemented by both countries, making the progress numbers so splendid.

However, there still remain certain challenges that inhibit the growth of financial inclusion. These challenges can be involuntary such as lack of financial literacy, income and awareness; belonging to remote areas; etc., or voluntary challenges like unwillingness to change, ignorance and distrust which are still prevalent in some parts of the countries.

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