International Journal of Scientific Research in Science and Technology
© 2019 IJSRST | Volume 6 | Issue 1 | Print ISSN: 2395-6011 | Online ISSN: 2395-602X
doi : https://doi.org/10.32628/IJSRST19699

# Financial Inclusion and Economic Development In India

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## ABSTRACT

Financial inclusion represents a complex and varied concept, with diverse perspectives existing worldwide. The principle of financial inclusion aims to ensure that affordable financial services are accessible to every segment of society, thereby enhancing their quality of life. This plays a crucial role in economic growth, ensuring the development of the financial sector while also providing affordable financial services for the improvement of all segments of society. The process involves distributing financial services to the underprivileged segments of society at a cost that is manageable for them. This system ensures the secure management of savings, provides access to loans for various needs, allows for risk diversification through investments in multiple avenues, and offers risk coverage through a range of insurance products, all of which contribute to enhancing the ease and comfort of people's lives. Consequently, inclusive finance fosters prosperity and economic growth by addressing poverty, reducing income inequality, and mitigating the influence of local banking monopolies. Financial inclusion is not a singular goal that can be attained directly; instead, it is a multifaceted process that culminates after various aspects, such as access to and utilization of financial services and the extent of banking penetration, have been successfully addressed.

Financial inclusion refers to the effort to guarantee that individuals and businesses can access suitable financial products and services at reasonable costs. In a diverse and populous nation such as India, financial inclusion serves as a fundamental requirement for economic advancement and acts as a crucial catalyst for equitable growth. This study examines the progression, present condition, obstacles, and influence of financial inclusion in India on its economic growth.

**Keywords :** Finance condition, banking, economic growth, GDP

## Introduction

It is generally recognized that two essential factors driving economic growth are progress in the financial sector and innovations in the information and communication technology (ICT) sector. The financial sector contributes to economic development in various ways, such as efficiently allocating resources for productive activities, supplying credit and insurance, facilitating savings for a broad segment of the population, and offering risk management for investors [1,2,3,4,5]. The services offered by financial institutions are essential for enhancing investment return rates, and they also significantly contribute to the execution of financial inclusion initiatives. The World Bank defines financial inclusion as a scenario in which both businesses and individuals can access appropriate and affordable financial services and products. This access allows them to obtain credit and insurance, conduct financial transactions, make payments, and accumulate savings. It is essential that these services are provided in an efficient and sustainable manner (World Bank, 2017). Financial inclusion initiatives aim to provide marginalized and vulnerable communities with essential services, including savings accounts, microfinance, home and personal loans, insurance, financial literacy, and market intelligence on investment opportunities. These services are intended to enhance their quality of life and contribute to broader economic growth.

Banking and financial services are essential for the growth and development of an economy. Studies indicate that an effective and inclusive financial system is associated with more rapid and equitable growth. A diverse array of personal finance options exists for the higher and upper middle-income groups, featuring financially engineered and innovative products. In contrast, a substantial portion of the population continues to lack access to fundamental banking services, such as holding a bank account. This phenomenon is referred to as “financial exclusion,” which subsequently results in social exclusion. It is essential to offer individuals accessible and cost-effective institutional financial products or services, commonly referred to as “financial inclusion”. It is widely acknowledged that the aim of financial inclusion is to broaden the range of activities of the organized financial system to encompass individuals with low incomes. In India, coordinated action among banks, the government, and related agencies is essential to enhance access to bank accounts for those who are financially excluded. Given the necessity for enhanced financial deepening within the country to stimulate economic development, there is an urgent requirement to broaden financial inclusion.

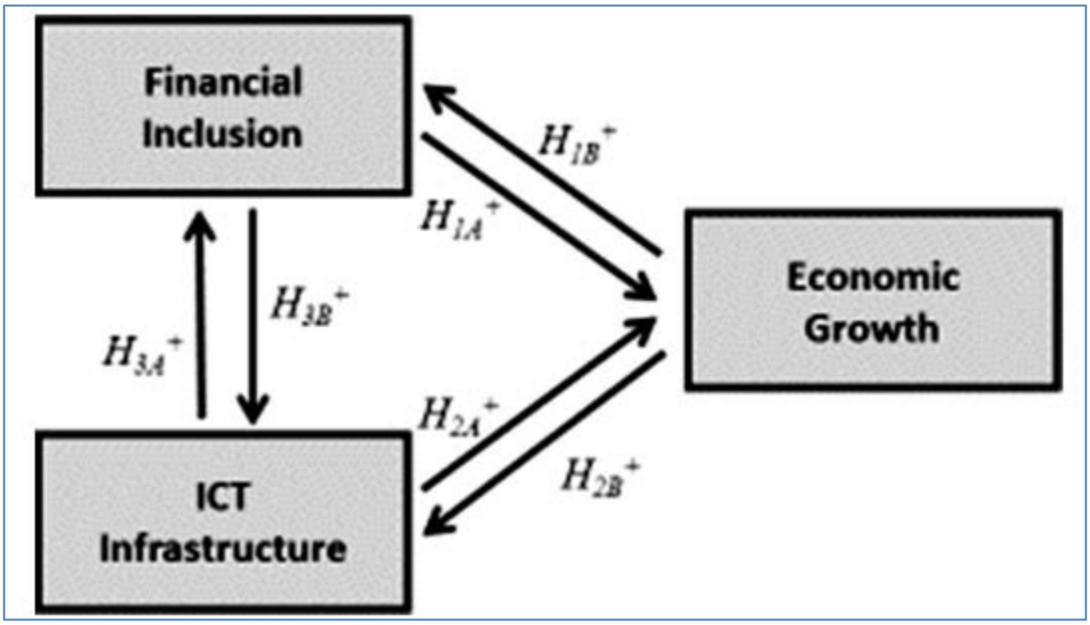


**Fig.1 Possible endogenous links between financial inclusion, ICT infrastructure, and economic growth [6]**

Although numerous studies have explored the separate impacts of financial inclusion and ICT on economic growth, there is a scarcity of research examining the interplay between ICT and financial inclusion initiatives and their collective influence on enhancing economic growth. The main aim of our investigation is to examine the connection between ICT, financial inclusion, and economic growth within the framework of a developing nation, specifically India.

## 1. Objectives and Need of Study

For developing nations such as India, it is essential to integrate the entire segment of society under a unified framework of financial services. The rural credit markets in India continue to be primarily influenced by money lenders. In these areas, individuals are not well-informed about the full spectrum of financial services, including the process of opening bank accounts and obtaining credit, among others [7]. In light of the previously discussed context, this study aims to develop a Financial Inclusion Index (FII) to assess financial inclusion in India. To achieve this objective, the discussion begins with the significance of financial inclusion in fostering inclusive growth. Secondly, the key indicators for establishing a FII in India have been identified. Third, this study develops and proposes an Index for measuring financial inclusion in terms of direction, degree, and intensity within the Indian context.

This study outlines the primary objectives listed below.

- ✓ Here to examine the concept and development of financial inclusion in India by exploring how it has advanced through different policy initiatives and technological advancements.
- ✓ The objective is to analyse the connection between financial inclusion and economic development by assessing how enhanced access to financial services impacts GDP growth, reduces poverty, fosters employment, and stimulates entrepreneurship.
- ✓ To evaluate the impact of significant government programs including PMJDY, MUDRA, and digital payment systems.
- ✓ Furthermore, recognizing their contribution to enhancing financial access and utilization.
- ✓ The aim is to pinpoint the obstacles to financial inclusion in India, emphasizing challenges like the digital divide, insufficient financial literacy, and the exclusion of marginalized communities.

Financial inclusion has become an essential mechanism for fostering inclusive development in contemporary economies. Despite notable advancements, a substantial segment of India's population continues to experience limited access to formal financial systems, particularly in rural and semi-urban areas. Some necessity of the financial inclusion study is described as below.

**Inclusive Growth Imperative:** To attain equitable and sustainable economic development in India, it is essential for the financial system to cater to all segments of society, particularly the underserved and marginalized.

**Policy Relevance:** Numerous government initiatives have sought to improve financial inclusion, yet there is an increasing necessity to assess their efficacy and propose enhancements grounded in data analysis.

**Addressing the Urban-Rural Divide:** Rural communities continue to encounter challenges related to infrastructure, technology, and access to information when it comes to banking and financial services.

**Digitalization:** The swift digitization of financial services presents opportunities for enhanced access, yet it simultaneously brings forth issues related to digital literacy, cybersecurity, and the quality of services provided.

## 1.Rise of Financial Inclusion in India

The evolution of financial inclusion in India has unfolded over many years, influenced by shifting socio-economic demands and policy focuses. This period featured financial reforms driven by the state, focusing on broadening banking access in rural regions.

### Pre-Liberalization Phase (Before 1991):

Bank Nationalization (1969 and 1980) intended to enhance banking accessibility in rural and underserved regions. This led to a notable rise in the quantity of rural bank branches. The Lead Bank Scheme, introduced in 1969, designated a lead bank for each district with the responsibility of ensuring sufficient banking coverage and equitable credit distribution. Regional Rural Banks (RRBs) were established in 1975 to offer credit and financial services specifically aimed at supporting rural and agricultural sectors.

### Post-Liberalization Phase (1991–2005):

The economic reforms of 1991 initiated financial sector liberalization; however, the inclusion of rural and low-income populations has not kept pace. The shift towards profitability in banks has resulted in the closure of certain rural branches and a diminished emphasis on financial inclusion. Self-Help Groups (SHGs) and the Microfinance Movement: Non-governmental organizations and microfinance institutions have been instrumental in delivering microcredit to women and the rural impoverished population.

### Institutional Push for Inclusion (2005–2013):

Throughout this time, the emphasis on financial inclusion emerged as a key national objective, with the Reserve Bank of India actively engaging in initiatives. In 2005, the Reserve Bank of India acknowledged financial inclusion as a crucial policy objective, urging banks to establish "no-frills" accounts. The Business Correspondent (BC) Model, introduced in 2006, enabled banks to designate agents to deliver banking services in remote locations lacking a physical branch.

### Digital and Policy-Driven Inclusion (2014–Present):

This phase signifies a significant shift driven by assertive governmental actions and advancements in digital infrastructure. Prime Minister Jan Dhan Yojana (PMJDY) – 2014 which was established more than 500 million bank accounts with zero-balance options. Facilitated Direct Benefit Transfers (DBTs), enhancing transparency and efficiency in the distribution of subsidies. The Unified Payments Interface (UPI), introduced by the National Payments Corporation of India (NPCI) in 2016, transformed the landscape of digital transactions by facilitating swift and convenient mobile-based payments. The Micro Units Development and Refinance Agency (MUDRA), established in 2015, offers collateral-free loans to small businesses and informal entrepreneurs through the Pradhan Mantri Mudra Yojana (PMMY). The Digital India Campaign and the JAM Trinity (Jan Dhan, Aadhaar, Mobile) have facilitated the provision of identity-linked financial services and promoted cashless transactions.

The progression of financial inclusion in India showcases a shift from traditional branch-based banking to digitally empowered, citizen-centric financial systems. Every phase has played a distinct role in enhancing access, affordability, and utilization of financial services. Despite significant advancements, realizing genuine financial inclusion necessitates ongoing innovation, strong regulatory frameworks, and comprehensive digital infrastructure.

## 2. Indicators of Financial Inclusion

Various indicators are employed to assess the scope and impact of financial inclusion in India. These indicators demonstrate not only access to financial services but also their usage and quality. These can be classified into three main dimensions: access, usage, and quality.

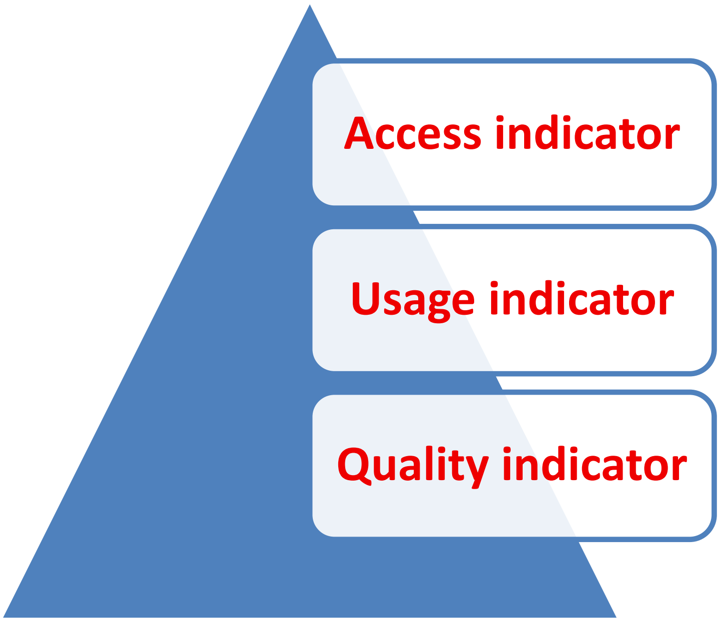


**Fig.2 Indicators of financial inclusion in India**

➢ **Access indicator**

- **Ownership of Bank Accounts:**

The World Bank's Global Findex Report 2021 indicates that more than 80% of Indian adults now have access to a formal bank account, a significant increase from 35% in 2011. By 2024, over 500 million accounts have been established nder the PMJDY initiative.

- **Distribution of Bank Branches and ATMs:**

According to RBI data from 2023, there are around 14.5 bank branches for every 100,000 adults. The concentration of ATMs is greater in urban settings, yet there is a notable increase in rural areas facilitated by the introduction of micro-ATMs.

- **Business Correspondents (BCs):**

There are currently more than 1.4 million active BCs, providing services to unbanked regions that lack physical branches.

➢ **Usage Indicators**

- **Active Bank Accounts:**

Approximately 78% of PMJDY accounts demonstrate activity, as evidenced by transactions occurring within the last 90 days.

- **Financial Reserves and Accounts:**

Total deposits under PMJDY surpassed ₹2.3 lakh crore by early 2025, reflecting a notable shift towards enhanced saving practices.

- **Access to and Utilization of Credit:**

The credit-to-GDP ratio continues to be lower in rural regions. Since their inception, microfinance institutions and MUDRA loans have collectively disbursed more than ₹20 lakh crore.

- **Electronic Exchanges:**

By 2025, UPI transactions exceeded ₹14 trillion each month. The rise of digital payments in rural areas can be attributed to initiatives from both government and fintech sectors. This analysis evaluates the frequency and effectiveness of financial service utilization in India.

➢ **Quality indicator**

This emphasizes the dependability, cost-effectiveness, and client contentment elements of financial services.

- **Dormancy Rate:**

Even with improved access, approximately 20–25% of accounts continue to be inactive, particularly among women and users in rural areas.

- **Coverage for Insurance and Pensions:**

More than 30 crore individuals have benefited from the Pradhan Mantri Suraksha Bima Yojana and the Jeevan Jyoti Bima Yojana. As of 2024, over 40 million individuals have registered for the Atal Pension Yojana.

- **Understanding Financial Concepts:**

While there have been advancements in financial literacy, it continues to be inadequate in rural regions and among specific demographics such as the elderly, women, and those with lower educational attainment.

## 3. Economic Development

Economic development signifies the ongoing enhancement of living standards, income levels, health, education, and the overall well-being of a nation's populace. This concept encompasses more than just economic growth, which is limited to the rise in national income or GDP. In the context of India, the trajectory of economic development is intricately linked to factors such as social inclusion, the creation of employment opportunities, the upliftment of rural areas, and the accessibility of financial resources. Financial inclusion serves as both a catalyst and a measure of economic development. This initiative enhances individual capabilities, fosters entrepreneurial ventures, optimizes resource distribution, and mitigates income disparities. The influence of financial inclusion on economic development can be analysed through various essential dimensions.

- **Reducing Poverty:**

Providing access to savings accounts, credit, and insurance enables low-income households to effectively manage risks, accumulate assets, and steer clear of reliance on informal moneylenders. Direct Benefit Transfers (DBT) implemented through initiatives such as PM-KISAN, MNREGA, and various subsidy programs provide essential income support to disadvantaged populations, effectively minimizing leakage and corruption. The World Bank indicates that access to financial resources can alleviate extreme poverty by facilitating more efficient consumption and enhancing financial planning capabilities.

- **Employment Generation and Entrepreneurship:**

The Pradhan Mantri MUDRA Yojana (PMMY) offers collateral-free loans to small and micro-entrepreneurs, fostering self-employment and facilitating job creation. Financial inclusion fosters development in the informal sector, which engages more than 80% of India's workforce.

- **Inclusive Economic Growth:**

Ensuring financial inclusion allows the advantages of economic growth to extend to marginalized groups, including women, small farmers, SC/ST communities, and rural populations. The advent of mobile banking, UPI, and fintech innovations enables individuals in remote regions to engage in formal economic activities.

- **Enhanced Savings and Investment:**

Broader financial access results in higher savings via formal banking systems, which can be utilized for national development initiatives. Financial intermediation effectively channels funds from surplus to deficit sectors, thereby fostering industrial and infrastructural development.

- **Human Capital Development:**

Insurance and pension schemes within financial inclusion initiatives offer financial security, promoting investments in education, health, and skill enhancement. Households that have access to financial services tend to invest more in education, which enhances literacy and increases long-term income potential.

## 4. Challenges

While there has been considerable advancement in broadening access to financial services, India still encounters substantial obstacles in realizing thorough and enduring financial inclusion. The challenges at hand are complex and encompass a range of dimensions, including economic, infrastructural, social, and technological aspects.

**Digital hindrance:**

Numerous rural and remote regions continue to experience deficiencies in dependable internet connectivity and digital infrastructure, which restricts access to mobile banking and digital financial services. A considerable segment of the population, particularly among the elderly and those with lower levels of education, faces challenges in effectively utilizing digital platforms.

**Inactive Accounts:**

Despite the opening of millions of bank accounts through initiatives such as PMJDY, a significant proportion remain inactive or hold minimal balances. Inactivity frequently stems from insufficient awareness, trust issues, or limited economic capacity to engage in transactions consistently. A significant segment of the population demonstrates a deficiency in fundamental financial understanding, including the utilization of bank accounts, comprehension of interest rates, effective savings management, and responsible credit use. This results in a lack of engagement with financial services and an increased risk of fraud.

**Gender Inequality:**

Women, particularly in rural and conservative areas, encounter significant social and economic obstacles in obtaining financial services. Barriers such as cultural norms, limited literacy, and insufficient documentation frequently hinder women's ability to independently own or manage bank accounts.

**Operational and Infrastructure Constraints:** Numerous tribal and hilly areas continue to be underserved by bank branches, resulting in limited economic development.

## Conclusion

Financial inclusion has become a fundamental element in the pursuit of inclusive and sustainable economic development in India. In the last twenty years, notable advancements have been achieved through strategic policy initiatives, technological advancements, and cooperative efforts among government entities, regulatory agencies, and financial institutions. Initiatives such as Pradhan Mantri Jan Dhan Yojana, MUDRA, UPI, and the JAM Trinity have successfully integrated millions of individuals who were previously unbanked into the formal financial system. Nonetheless, despite significant advancements in access to financial services, the challenges of meaningful usage and achieving long-term financial empowerment persist. Challenges like digital illiteracy, dormant accounts, restricted access to credit, and gender-based financial exclusion persist in obstructing the complete achievement of financial inclusion's potential.

Financial inclusion serves as a significant catalyst for economic transformation rather than being a goal in its own right. This plays a significant role in alleviating poverty, generating employment, fostering entrepreneurship, enhancing social security, and strengthening the economy's overall resilience. As India aims to achieve a $5 trillion economy, it is essential to prioritize the enhancement of financial inclusion, particularly for underserved rural and vulnerable communities.

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