International Journal of Business Management
Available at www.ijbm.co.in
ISSN No.:2349-3402
Vol. 1(2), 2014

Inclusive Financial Services for Small Businesses and Low Income Households: An Overview of Mor Committee Recommendations

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Financial inclusion & financial deepening are required to be focused on to develop a robust financial system in a country. To achieve these twin objectives we have to provide the access to financial services to low-income households and small businesses. Many committees had been set up & extensive research had been done in the past to develop a mechanism to improve the accessibility of financial services. In the recent past Mor Committee was set up which came up with its recommendations to improve the status of financial services in the country. We in this present study focus on outlining some of the important recommendations.

Key-words: Financial Inclusion, Financial Deepening, Small Businesses, Financial Services.

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Introduction:

India is a developing country with a rapidly increasing economy. To sustain this economic development and growth a well-developed financial system is required.Financial markets and services play an important part in the effective functioning of an economy. Financial exclusion reduces the potential welfare of individuals and the productivity of enterprises in an economy. Access of disadvantaged groups to financial markets is thus of strategic importance for social and economic development and social inclusion.Financial inclusion mobilizes savings that promote economic growth through productive investment.Therefore increased financial access would be promoted by sound overall macroeconomic &financial sector policy and regulatory reforms to enable financial markets to function more smoothly. Moreover the unprivileged are required to be provided with much needed financial assistance in orderto take them out of their conditions of poverty.The banking Industry in India has recognized this imperative and has undergone certain fundamental changes through banking sector reforms by increasing competition, developing of new generation private sector banks, diverse financial products, services and delivery channels. Now Indian banks are one of the largest contributors of delivering financial services to the people of the country.

Financial Inclusion & Financial Depth:
Financial Inclusion is defined as the spread of financial institutions and financial services across the country and Financial Depth is defined as the percentage of credit to GDP at various levels of the economy. A World Bank report states, “Financial inclusion, or broad access to financial services, is defined as an absence of price or non-price barriers in the use of financial services.” So financial inclusion does not imply that all households and firms should be able to borrow unlimited amounts or transfer funds. The creditworthiness of the customer is also critical in

providing financial services. Moreover there is distinction between 'access to' which essentially refers to the supply of services, and 'use to'which is determined by demand as well as supply. The problem of financial inclusion addresses the 'involuntarily excluded' as they are the ones who, despite demanding financial services, do not have access to them.

Objectives of the Study:

The main objective of the study is to analyze the recent report on comprehensive financial services for small businesses and low income households by Mor Committee.

Literature Review:

Saladini,M (2005) found that the micro, small and medium enterprises (MSME) and the poor can benefit from dedicated microfinance facilities. In order to facilitate greater credit access for MSME, provincial governments had set up credit guarantee facilities. Kumar, Anjali (2005) concluded that a range of supporting institutions needed to be involved in the efforts of financial outreach. These included nonprofit agencies and community investment agencies who worked closely with target communities, such as the CDFIs of the United Kingdom and United States, which are distinct from commercial banks.The role of programs of financial education and literacy was also vital; inthis context, programs that offer incentives for family support to financialplanning were also interesting.Elliott et al. (2006) in their case study examinedSwisscontact's experience in stimulating a more conducive environment for small businesses in Indonesia and Russia and sought a departure from conventional approaches to making markets work for the poor approach.Mandira&Jesim(2009) found that level of human development and that of financial inclusion are strongly positively correlated.Income inequality, adult literacy, urbanization as measured by per capita GDP, physical and electronic connectivity and informationare important factors in explaining the level of financial inclusion in a country.Leaders of the G20 at the G20 summit in 2010 recognized financial inclusion as one of the main pillars of the global development agenda&endorsed a concrete Financial Inclusion Action Plan. Subsequently the Global Partnership for Financial Inclusion (GPFI) was established to institutionalize and continue the work begun by the Financial Inclusion Experts Group.Ehrbeck et al. (2010) established that despite sustained efforts, millions of rural and urban poor continue to lack opportunities to borrow, save, insure themselves, and access the numerous services of India's formal financial sector. The improved efficiency and greater penetration of an e-payment setup will likely encourage greater participation from poor rural citizens, and bring the central government closer to its cherished goal of reducing poverty and hunger through its welfare, food, and housing subsidy schemes.Radcliffe&Voorhies (2012) recognized that Payments are the connective tissue of an economic system& when these transactions are costly and inconvenient, economic activity is impeded. Arulmurugan et al. (2013) found that Access to financial servicesis extremely important for poverty alleviation and development. For total financial inclusion, policy makers, MFIs, NGOs and regulators have to work together. RBI took various inclusive steps including Opening of No – Frill Accounts (NFA), Relaxation of KYC norms, Engaging Business Correspondents (BCs), opening of branches in unbanked rural centers, Financial Literacy Programs etc. Faz&Moser (2013) sated that digital cash models (often called branchless banking, mobile banking, or mobile money) can increase financial access for unbanked segments by reducing the cost-to-serve for providers and making service more convenient for customers and can help accelerate the pace offinancial inclusion.

Mor Committee Recommendations:

The Committee on Comprehensive Financial Services for Small Businesses and Low Income Households, set up by the RBI in September 2013, was mandated with the task of framing a clear and detailed vision for financial inclusion and financial deepening in India. Committee found that overall situation is very poor and on sector/regional basis, very uneven. Close to 90% of small businesses have no links with formal financial institutions and 60% of the rural and urban population does not even have a functional bank account. Also credit to GDP ratio is modest 70% but in some states like Bihar it is as low as 16%. Savings as a proportion to GDP has fallen from 36.8% in 2007-08 to 30.8% in 2011-12 and the financial savings of households have declined from 11.6% of GDP to 8%.In its final report, the Committee outlined six vision statements for financial inclusion and financial deepening in India:

i) Universal Electronic Bank Account (UEBA): Each Indian resident, above the age of eighteen years, would have an individual, full-service, safe, and secure electronic bank account.

ii) Ubiquitous Access to Payment Services and Deposit Products at Reasonable Charges: The Committee envisions that every resident in India would be within a fifteen minute walking distance of a payment access point.

iii) Sufficient Access to Affordable Formal Credit: Each low-income household and small-business would have access to a formally regulated lender that is capable of assessing and meeting their credit needs. Such a lender must also be able to offer them a full-range of suitable credit products at an affordable price.

iv) Universal Access to a Range of Deposit and Investment Products at Reasonable Charges: Each low-income household and small-business would have access to providers that can offer them suitable investment and deposit products. Such services must be available to them at reasonable charges.

v) Universal Access to a Range of Insurance and Risk Management Products at Reasonable Charges: Each low-income household and small business would have access to providers that have the ability to offer them suitable insurance and risk management products. These products must at minimum allow them to manage risks related to: (a) commodity price movements; (b) longevity, disability, and death of human beings; (c) death of livestock; (d) rainfall; and (e) damage to property.

vi) Right to Suitability: Each low-income household and small-business would have a legally protected right to be offered only suitable financial services. She will have the right to seek legal redress if she feels that due process to establish Suitability was not followed or that there was gross negligence.

Aadhaar:Aadhar will be the key piece of infrastructure to enable a customer to be identified and authenticated so that repudiation and fraud risks are minimised and therefore should become the universal basis for authentication.

Payments Banks:Under the Banking Regulation Act, a set of banks may be licensed which may be referred to as Payments Banks. Their primary role is to provide payment services and deposit products to small businesses and low-income households, maximum balance of Rs. 50,000 per customer. CRR requirements will be as applicable to all the Scheduled Commercial Banks.They will be required to deposit the balance proceeds in approved SLR securities with duration of no more than three months and not permitted to assume any kind of credit risks.As they will have a near-zero risk of default, the minimum entry capital requirement for them will be Rs. 50 crore.

Investor Protection:RBI to issue regulations on Suitability, applicable specifically for individuals and small businesses, to all regulated entities within its purview, i.e., banks, NBFCs and payment; so that the violation of such regulations would result in penal action for the institution, including fines, cease-and-desist orders, & modification and cancellation of licenses.The firm would have to carry out a limited due diligence of the customer and put in place a process to assess the appropriateness of any product offered to a customer based on the results of the diligence. The firm must have internal grievance redressal mechanisms for non-compliance with process and this should be required to be communicated to customers as well.The Committee recommends that a unified Financial Redress Agency (FRA) be created by the Ministry of Finance as a unified agency for customer grievance redress across all financial products and services.

Financial Access & Usage Survey: In order to measure access, usage, and affordability of financial services, RBI should mandate two surveys of consumers to gain a more accurate picture of progress towards achieving the desired outcomes outlined by the vision statements

The Committee lays down a set of four design principles, namely Stability, Transparency, Neutrality, and Responsibility, that will guide the development of institutional frameworks and regulation for achieving the visions outlined. Any approach that seeks to achieve the goals of financial inclusion and deepening must be evaluated based on its impact on overall systemic risk and stability, and at no cost should the stability of the system be compromised. A well-functioning financial system must also mandate participants to build completely transparent balance sheets that are made visible in a high-frequency manner, accurately reflecting both the current status and the impact of stress situations on this status. In addition, the treatment of each participant in the financial system must be strictly neutral and entirely determined by the role it is expected to perform in the system and not its specific institutional character. At its core the Committee's recommendations argue that in order to achieve the vision of full financial inclusion and financial deepening in a manner that enhances systemic stability, there is a need to move away from a limited focus on any one model to an approach where multiple models and partnerships are allowed to emerge, particularly between national full-service banks, regional banks of various types, non-bank finance companies, and financial markets.

Conclusion:

In Indian context, the starting point for financial inclusion or deepening financial services is to discern prudently the profile of the excluded in the ' last mile' from demand side perspectives and design appropriate integrated products and services and appropriate means of delivery. The Mor Committee has touched in detail all the important aspects regarding improving financial services to small businesses and low income households. But the success of these recommendations will depend upon the successful execution in both letter and spirit.

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