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A study on the problems faced in the financial sector of rural India

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ABSTRACT

Rural India is one of the sectors that have to develop for the increase in GDP of India. The rural sector includes the agricultural sector. The financial services provided in the rural sector are NABARD and MSMEs'. These are the facilities that provide credit and loans to the public. There is a requirement of credit in the rural sector due to fewer quantities being produced by the agricultural sector. This research paper shows an overview of all the problems being faced in the financial sector of rural India. The paper also provided details of the initiatives taken by the government towards the public in rural areas and shows statistical data of the growth in rural credit.

Keywords— *Rural India, Financial service, Agriculture*

1. INTRODUCTION

(D. Subbarao, the Governor of RBI, 2012) India has a diversified financial sector undergoing rapid expansion, both in terms of strong growth of existing financial services firms and new entities entering the market. The sector comprises commercial banks, insurance companies, non-banking financial companies, co-operatives, pension funds, mutual funds and other smaller financial entities. The banking regulator has allowed new entities such as payments banks to be created recently thereby adding to the types of entities operating in the sector. However, the financial sector in India is predominantly a banking sector with commercial banks accounting for more than 64 per cent of the total assets held by the financial system.

The Government of India has introduced several reforms to liberalize, regulate and enhance this industry. The Government and Reserve Bank of India (RBI) have taken various measures to facilitate easy access to finance for Micro, Small and Medium Enterprises (MSMEs).

(Gagan Bihari Sahu, 2004) The Financial sector of a country causes a huge indirect influence on its growth and development. The financial sector mobilizes savings and allocates credit across space and time. It provides not only payment services but also enables firms and households to cope with economic uncertainties by hedging, pooling, sharing and pricing risks. An efficient financial sector reduces the cost and risk of producing and trading goods and services and thus makes an important contribution to raising the standard of living.

Although the Indian Financial Sector is one of the fastest growing sectors in the world, it faces huge problems. Most of these problems are concentrated in rural India. The government along with the RBI has taken steps to improve the condition of the financial sector in rural India but the results are not satisfactory.

The main reason why it is so difficult to penetrate and establish the financial services in rural India is that of illiteracy, traditional mindset of the people and trust issues. Most of the people don't understand the benefits that they can get by contributing towards the success of these financial institutions. Another main problem that the financial sector faces is that the technology used to establish these services are outdated and not efficient. There is no availability of technological resources, which would make things easier for both the parties.

Rural India is so important to the financial sector as almost 68.84% of India's population stay in rural areas. The fact that the majority of India's population does not have access to proper and efficient financial services is both saddening and frightening at the same time. Although it is very important for the financial sector to tap into rural India, it will not be easy.

The Indian government has continuously strived to improve the condition and the framework of the financial sector in rural India but have failed time and again. Although the state of the financial sector is improving on a daily basis, the results are not satisfactory. There are more problems than solutions to this issue.

In this research paper, our aim is to analyze all the problems that the financial sector faces in rural India and also provide certain solutions to overcome these problems and make our country a better place to live in.

2. LITERATURE REVIEW

(Richi Sidana, 2013) In India over 65% of the population resides in villages. 70% of them do not have bank accounts. Moneylenders are sources of funds. Moneylenders control 1/3rd of all rural loans

(Anjani Kumar, K.M. Singh and Shradhanjali Sinha, 2010) Rural Finance has always been a hurdle since the government legalized commercial banks. Indira Gandhi had nationalized private banks with an exception that there will be a deposit base of 50cr to provide aid to the poor sector of India in the year 1969. In the 1990s self-help Group Bank Linkage (SBL) was created to motivate farmers, therefore, attempting to reduce suicides amongst farmers.

Central Banking Enquiry Committee (CBEC) in the year 1929 and Madras Provincial Banking Committee (MPBEC) are classic mechanisms that show the mechanism of debt.

(Balakrishnama Naidu, A. Siva Sankar and P. Surya Kumar, 2013)Regional Rural Banks were also assigned by the RBI for compensating rural credit and for getting rural development. In the year 1991 Narasimham Committee focused on the poor financial aids provided by RRBs to the rural areas.
(Valentina Hartarska, 2015) Most of the hardworking farmers are forced to take money from moneylenders due to illness in the family or not enough harvests. Due to the lack of importance given to farmers, there is not enough income due to which they are unable to repay the money taken and leads to suicides.

(S. Cole, 2009) The RRB's have faced obstacles in deposit mobilization. Due to their restrictive lending policies, potential depositors show no interest in depositing money in banks. Due to this the pace of growth of RRB's is low and leads to limiting the scope of direct lending by RRB's in their operations. There is also a difficulty in recognizing potential buyers due to their backward thinking of not liking formalities and dealing with money in an informal manner.

Initially, the rural people have a misconception of credit being required for agricultural production in the 1960s and '70s. There was also a fear in the people due to collateral being asked by private sector lenders. Once the misconception was identified and cleared, there is an increase in demand for credit in the rural sector of India.

2. STATEMENT OF THE PROBLEM

The problem at hand is the lack of development in the financial sectors in rural India. If you take a look at the urban areas there are multiple private and public players which provide multiple financial services, but whereas in the rural areas the people are not even aware of such services or financial products. This study aims to provide information on the key areas in which the financial industry can be developed in rural India.

3. NEED OF THE STUDY

The need of such a kind of study is because of the lack of focus on the development of this industry in rural India. This is a huge opportunity for various financial institutions to bridge the gap that currently exists between urban India and rural India. The study would help in understanding the key areas to focus and analyze the scope of development.

4. OBJECTIVE OF THE STUDY

The main objective of the study is to analyze the various areas of lack of development of the financial industry in rural India.

5. RESEARCH METHODOLOGY

Secondary data has been used for this study. Data published by various institutions such as the government of India, reserve bank of India, world bank and several other authors. The data has been taken from various articles and websites which talk about the various issues, challenges and faced by rural India and hence used for the purpose of this research paper.

6. DATA ANALYSIS AND INTERPRETATION

6.1 Financial services in rural India

The availability of quality financial services in rural areas is extremely important for the growth of the economy as this will enable a large number of rural households to fund the growth of their livelihoods. The growth of the economy is dependent on the growth of the rural market in the country. Therefore greater financial inclusion in these segments is imperative. Rural finance is about providing financial services – secure savings, credit, money transfer and insurance – in rural areas. Indeed, financial services can play an important role in rural development. Savings and insurance schemes assist the rural population in reducing vulnerability to risks, planning more reliably for the future 4 and saving for upcoming investments, as well as smoothing out irregular income flows and covering unexpected expenses. The latter is particularly important in rural areas where income depends on agricultural cycles. Loans for investments and working capital are crucial elements that enable rural entrepreneurs to make investments, seize economic opportunities, and purchase agricultural inputs and working capital. Short-term consumption or emergency loans can help households to avoid difficult situations that might have forced them to sell an asset.

However, loans are not always favourable: some poor borrowers experience difficulties in repaying their debts, due either to circumstances beyond their control (e.g. sickness, theft, natural disasters) or to a lack of knowledge and wrong investment strategies. Money transfer services make it possible for people who leave rural areas to work in cities or abroad to send home their remittances safely and at reasonable costs. In addition to fostering rural development, rural finance is increasingly used as an incentive to promote sustainable use of natural resources, use of alternative energies, and environmentally sound behaviour. In recent years, several banks and microfinance institutions have attempted to achieve not only financial and social but also environmental sustainability, which has been dubbed the “triple bottom line”.

Despite the significant demand for financial services in rural areas, institutions offering financial services – such as banks, credit unions, microfinance institutions (MFI) or insurance companies – are typically reluctant to serve rural areas. As a result, the majority of the developing world’s rural population does not have access to the formal financial system.

Confronted with this lack of access, households, farmers and small entrepreneurs rely on informal ways of accessing financial services. Entrepreneurs usually rely on family savings or borrow money from friends to make small investments, and in emergency situations, people tend to borrow from acquaintances. Such loans are usually repaid without interest. Also, people typically rely on moneylenders to obtain loans. Moneylenders often ask for usurious interest rates and sometimes try to recover the loans by violent means. On the other hand, moneylenders can provide loans rapidly in an emergency, and they do not ask for collateral. Community self-help schemes such as self-help groups (SHG), rotating savings and credit associations (ROSCAs), community-based savings and credit mechanisms are useful instruments to encourage savings, provide small-scale insurance and avoid debt at exorbitant interest rates. Formal institutions can offer a broader range of financial products. Formal services such as microfinance cannot replace loans from friends and family, but they do complement them and enable the rural population to access a wider range of 5 services. Moreover, formal financial institutions belong to the economic infrastructure of a country or region and can thus help to foster economic development.
(Sources: www.iosrjournals.org)

6.2 Challenges in rural India regarding financial services
Rural households and entrepreneurs still face a number of obstacles that make it difficult to access financial services. Following are a broad array of challenges faced by service users as well as financial institutions

- Higher transaction cost
- Higher risk
- Higher rates of illiteracy

From a survey conducted it shows that the people in rural India are not completely aware of the various financial services available.

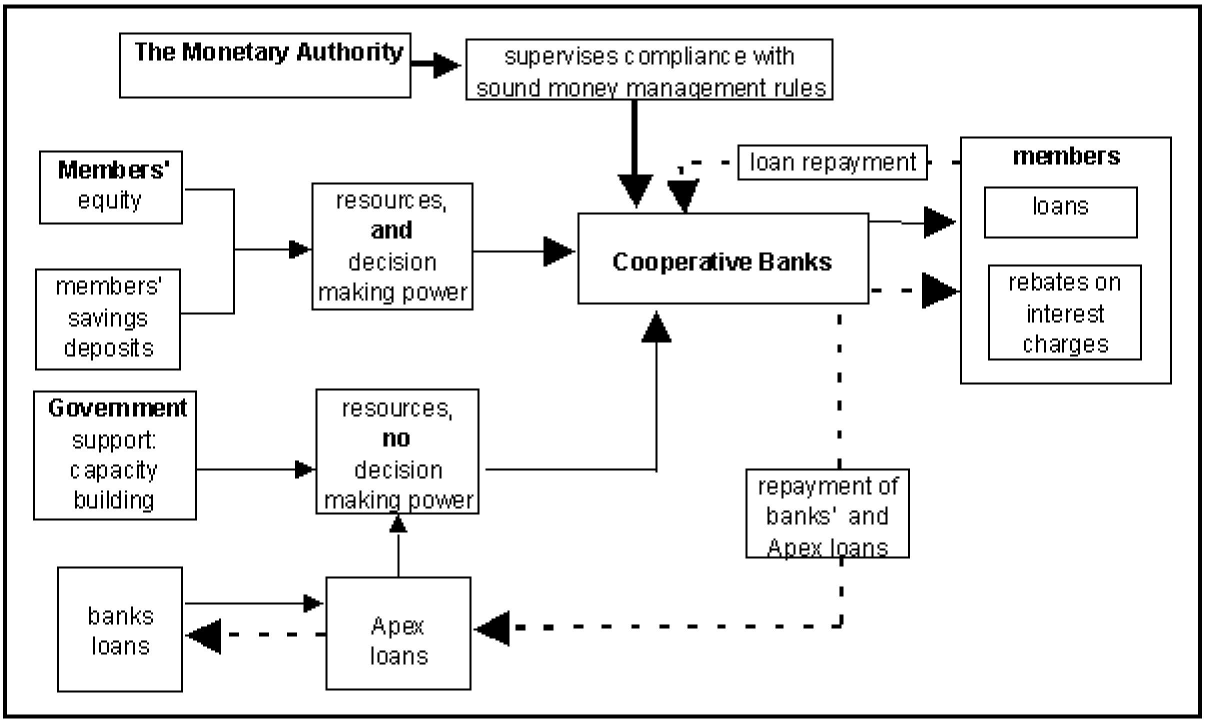

Fig. 1: The flow of cooperative banks and shows the relationship between the public and the banks
Source: http://www.fao.org/docrep/005/y2006e/y2006e0c.htm

The above diagram shows the flow of cooperative banks and shows the relationship between the public and the banks. It also shows how the government provides aid to the public by spreading awareness of the credit systems being introduced to the public.

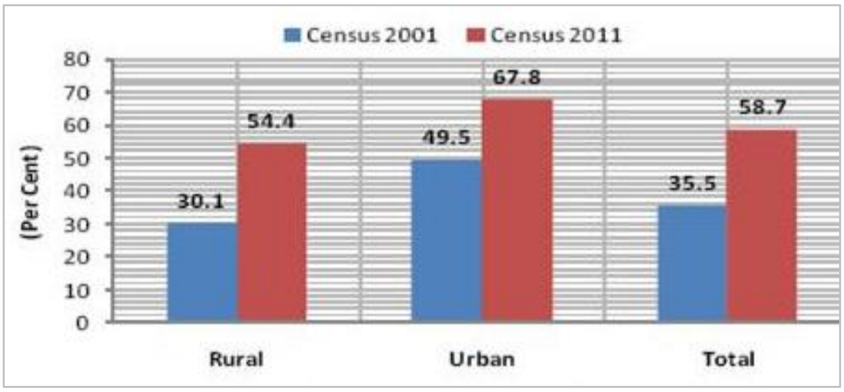

Fig. 2: The census survey conducted in the rural areas and urban areas
Source: Department of Financial Services.

The above graph shows the census survey conducted in the rural areas and urban areas. The rate of credit has risen in 10 years by 24.3% which is a positive boost that shows that the percentage of rural credit. The government have been hosting campaigns and spreading awareness amongst the rural population, explaining how it will benefit them and help them in their daily lives. This boost has also helped the Indian economy in terms of development and literacy rates are slowly rising due to the availability of funds to the public in the rural sector.

7. CONCLUSION

NABARD and MSMEs' introduced by the government have led to an increase in the percentage of rural credit being used by the public in the rural sector. The FMCG market is slowly rising in the rural sector and there is a prediction of the market to cross 100 US dollars. The financial sector has also had development once it was decentralized. Earlier the rural could not repay loans they borrowed due to having insufficient funds. Now that the credit provisions are available to the public, it had raised their standard of living and there is an increase in agricultural production.

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