

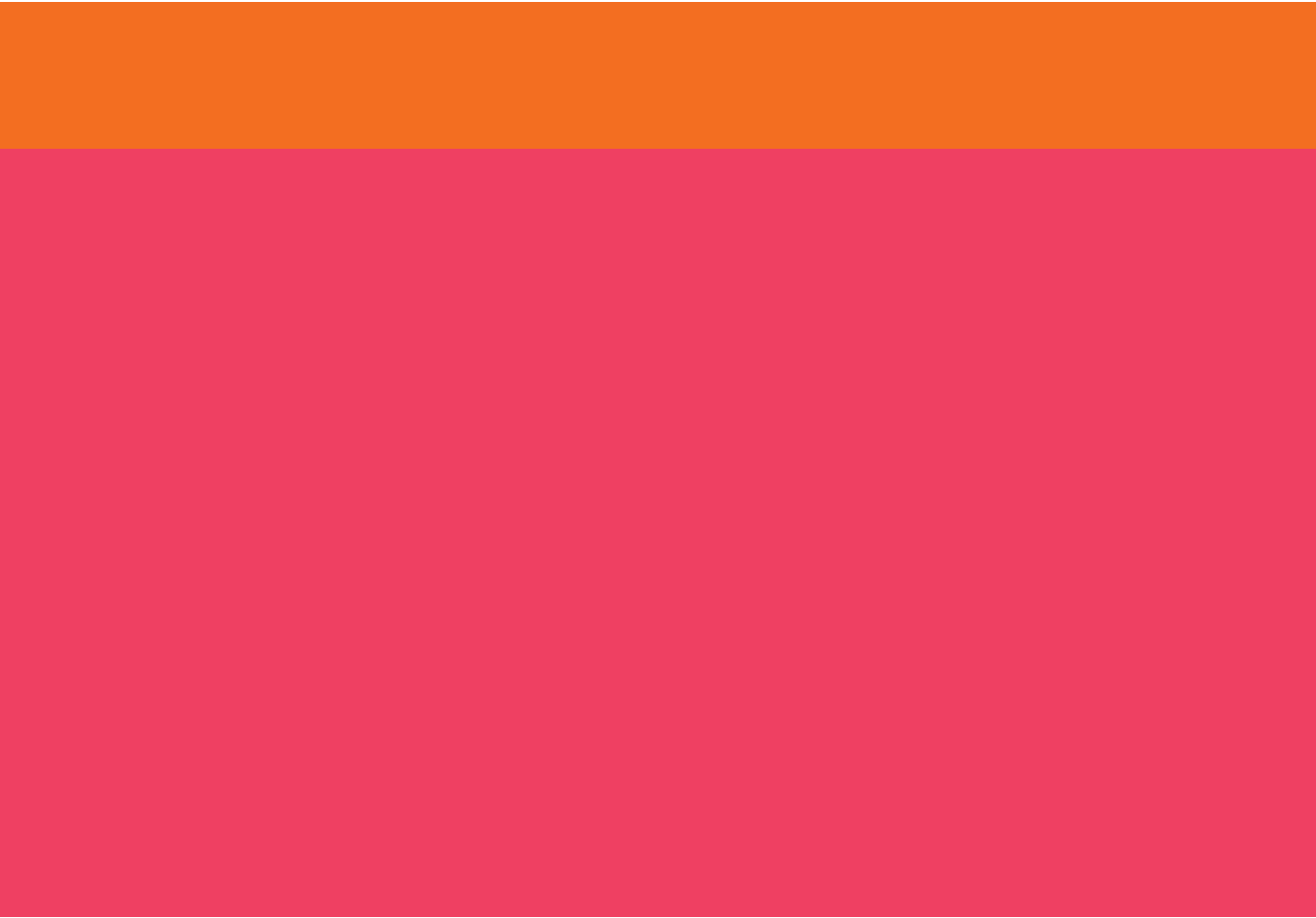
# ***The Next Decade***

How Financial Institutions can  
help the East grow



Confederation of Indian Industry





# *Executive summary*

The CII Banking Colloquium 2011 seeks to draw attention to the eastern region of India, which is all set to realise its latent potential and match the growth chart of more developed states. As the knowledge partner for this event, we take this opportunity to highlight some key elements that will assist the region in mapping its success story.

The report focuses on the importance of inclusive growth in the region. It also attempts a comparison between the eastern region and various other states on basic parameters such as employment statistics, infrastructure development and accessibility of financial institutions.

The report assesses how the eastern region has evolved to understand the key drivers for accelerating growth. Our analysis touches upon issues such as the current state of employment, while defining the vital role that small and medium enterprises (SMEs) need to play in generating it. Underlying this is the concern, shared with the other Indian states, of bringing more and more people within the ambit of basic financial services.

This paper, with the help of a few case studies, illustrates some best practices in the area of financial inclusion, infrastructure financing and SME operations. These practices have been rolled out more effectively in countries like China, Brazil, Indonesia, Malaysia and Kenya.

We have also drawn insights from our interactions with SMEs, leading financial intermediaries and policymakers. We hope you find this report useful and welcome your feedback on the subject.



# Contents

Page   Chapter

06   *Introduction*

07   *India on the global platform*

08   *Achieving sustainable inclusive growth*

15   *Employment: The SME perspective*

20   *Targeting the bottom of the pyramid: Financial inclusion*

25   *Infrastructure development and financing*

27   *Key research findings*

30   *Imperatives for inclusive growth in the Eastern region*

32   *Conclusion*

# Introduction

India's macro-economic indicators reflect a favourable and conducive growth environment. However, despite the growth trajectory, the benefits have not percolated to the under-privileged and poor sections of the society.

The Reserve Bank of India (RBI) recognises inclusive growth to be 'broad-based across sectors' and to include a large part of the country's labour force. Today inclusive growth has been renewed with a fresh vigour to ensure long-term and sustainable economic growth. Traditionally, financial services have always been skewed towards the richer sections of society. This has left the poor and less privileged sections without basic facilities like a bank account. This un-banked section accounts for nearly 60% of India's population. As a result of not having access to basic financial services, many rely heavily on the unorganised sector, family and friends for their need-based borrowing.

However, this has been changing over the last few years. The concept of micro-credit has found acceptance, establishing a profitable business model in the low-cost financial services sector.. The focus seems to have shifted from 'economies of scale' to 'economies of access'. With increased awareness the importance of saving and insurance products has gained ground.

As a crucial catalyst, the government has taken many policy decisions. These include creating a financial inclusion roadmap to cover villages with over 2,000 people by March 2012, mandatory opening of 25% new branches in un-banked rural centres, simplification of know your customer (KYC) norms, etc. These policies are focussed on reducing the gap between purveyors of financial products and their users and channelising the savings into long-term investments such as pensions and insurance.

Technology has further enhanced the access to financial services. The financial services sector has capitalised on the boom in mobile telephony to reach far-flung areas. Technology is a huge enabler and has facilitated new payment platforms and the use of electronic benefit transfer.

In this paper, we have attempted to assess the main ingredients of an inclusive growth model. We discuss the role of infrastructure development, availability of financial institutions, intermediaries and employment generation in accelerating the pace of inclusive growth in the eastern region of India which comprises states of West Bengal, Orissa, Bihar, Jharkhand.

# India on the global platform

India has shown resilience in the face of adverse economic conditions such as rising inflationary pressures and increasing crude oil prices. Despite the Indian economy growth rate dipping from its high levels of around 9% in 2008 to around 7% in the first quarter of 2011-12, India is fairly insulated from the global slowdown.

Over the last decade, per capita income has almost doubled with strategic reforms and continued investment in the economy increasing the country's growth potential. With continuous investment in infrastructure, it is most likely that India will tread on a sustainable growth path.

Country	Rank
Singapore	1
Japan	18
Mexico	35
China	79
Indonesia	121
Russia	123
Brazil	127
India	134

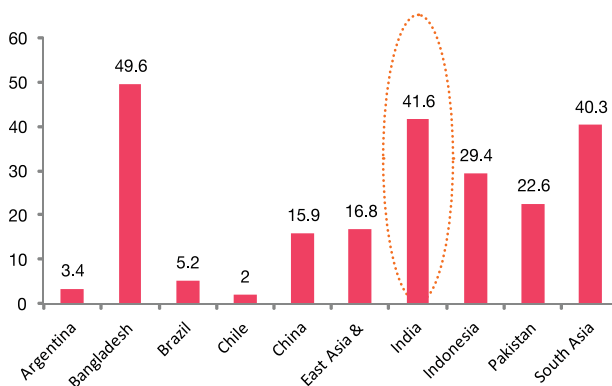
Source: World Bank Report, 2011

Undoubtedly, India is one of the most promising investment destinations in the world. However, as per global benchmarks, the country doesn't fare very well on some socio-economic indicators. The poverty-head count ratio shows that India stands a dismal second to Bangladesh. Even countries like Argentina and Brazil score better than the South-Asian economies including India.

In addition, in a 2010 World Bank report, India was ranked 134 out of 183 countries in terms of doing business, which indicates where India lies in terms of a business friendly environment.

- Around 80% of India's population subsists on less than \$2 a day.
- Only two-thirds of India's population is literate, as compared to 90% in China.
- Three-fifths of the labour force is employed in agriculture, producing less than one-fifth of the country's GDP.

**Poverty head-count ratio at \$1.25 (PPP)a day ( in %):  
India versus other economies**



Source: World Bank; reported at 2005 international prices

# Achieving sustainable inclusive growth

Inclusive growth ensures equal opportunities for all. India's poverty reduction at 0.8% every year is dismally low as compared to our neighbouring countries like Bangladesh and Nepal. Both these countries have seen poverty reduction of nearly 1.6% every year.

Although, poverty rates have declined in the last few years, they are still comparatively high. For the current government, this is a crucial issue that needs to be addressed. The essential pillars for inclusive growth are productivity, employment, financial inclusion and infrastructure development.

Undertaking measures and initiatives to strengthen each of these pillars will eventually lead to a holistic development of the economy.

*Gainful employment:* Creation of employment opportunities will automatically prepare the economy for inclusive growth. Generation of jobs and income for individuals, through new jobs or self-employment enables inclusive growth.

*Financial inclusion:* Without convenient access to financial institutions and services, the savings of those living in rural areas cannot be channelised into investment products. Further, the availability of credit facilities is also severely hindered.

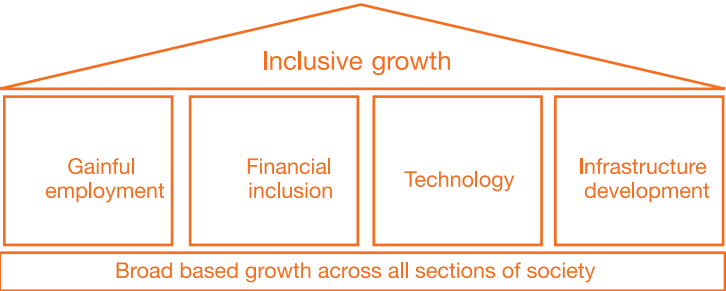
*Technology:* To keep pace with growth, technological support is essential. No kind of reform or development can actually take shape without the aid of technology.

*Infrastructure development:* A holistic economic development

cannot be complete without increasing infrastructure. Unless investments are made for better infrastructure facilities, that reach out to the people living in the far-flung regions, growth will remain slow-paced.

## What does the current situation in India look like?

- Around 30% of the population lies below the poverty line.
- Employment is dominated by jobs in the informal sector. There has not been much improvement in the employment scenario in the unorganised sector.
- There are 600,000 villages in India but only 32,919 rural bank branches in the country.
- Only 40% of the population in India has bank accounts.





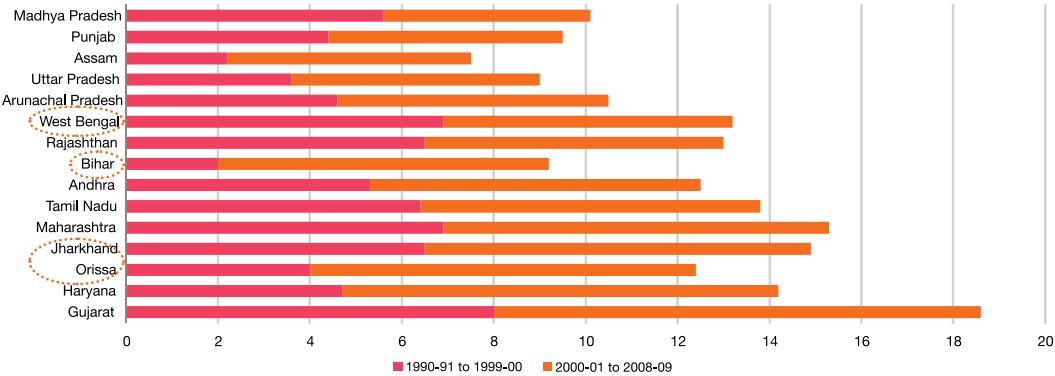
# Indian states: The growth story

Our country has its various regional disparities and challenges. To assess the growth seen in each individual state, a study of the economic progress over the last two decades is imperative.

Bengal lagged behind at 7.2% and 6.3%, respectively.

It is not enough to only look at the growth rates of different states to assess the levels of inclusive growth; Studying socio-economic indicators like poverty and

## Comparing growth across states

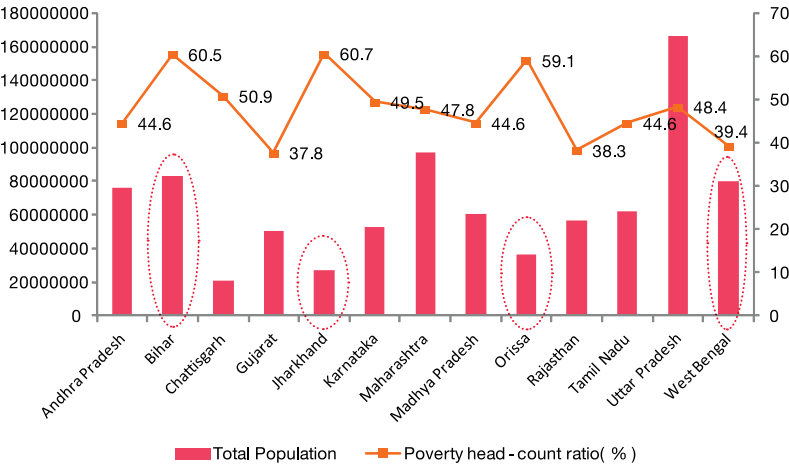


Source: RBI

As seen above, from 2000 to 2009, growth across all the states was considerably higher than in the 1990s. From 2000 to 2009, Gujarat, Haryana and Maharashtra showed exemplary growth rates of 10.6%, 9.5% and 8.4% respectively. However, in the same period, Bihar and West

unemployment, will also help draw a comparison across states on their pace and pattern of growth.

**Total population and poverty head-count ratio ( %): Comparison by state**



Source: Ministry of Rural Development, 2011

**Unemployment radar**

% of Regular Employment to Total Employment			
Less than 10%	10% -15%	15%-20%	Above 20%
Very Low	Low	Medium	High
Bihar	Rajasthan	Jammu & Kashmir	Maharashtra
Chhattisgarh	Madhya Pradesh	Gujarat	Tamil Nadu
Jharkhand	Assam	Kerala	Punjab
Orissa	Andhra Pradesh	Haryana	Delhi
Uttar Pradesh	Karnataka		
	Uttaranchal		
	Himachal Pradesh		
	West Bengal		

Source: NSSO Survey

The above chart indicates that the states with the highest number of poverty-stricken people are in the eastern region of the country, primarily, in Bihar, Jharkhand and Orissa.

Unemployment and under-employment are also factors that affect the backwardness of a region. Bihar, Jharkhand and Orissa end at the bottom of the list in terms of unemployment.

Allocation of credit is another factor that increases inequalities between states and impacts economic growth. Thus, it is important to assess the disbursement of business credit (funds for business activities) across regions.

Before looking at the details of funds sanctioned and actually released for each state, sector-wise allocation of funds for each region shows the complete picture.

**Allocation of credit: Sector and region-wise (%)**

	Northern	Southern	Western	Eastern
Agriculture	22.3	12.5	6.2	10.6
Industry	32.1	32.9	45	37.1
Service Sector	45.6	54.6	48.8	52.2

Source: RBI



The chart below shows the funds released for each state. Jharkhand and Orissa have been allocated lower funds in comparison to

other states. . Despite the fact that Bihar and West Bengal see considerable amount of funds allocated to rural households,

they still project high numbers below the poverty line. This can only imply that funds are not deployed efficiently.

### Allocation of funds by state

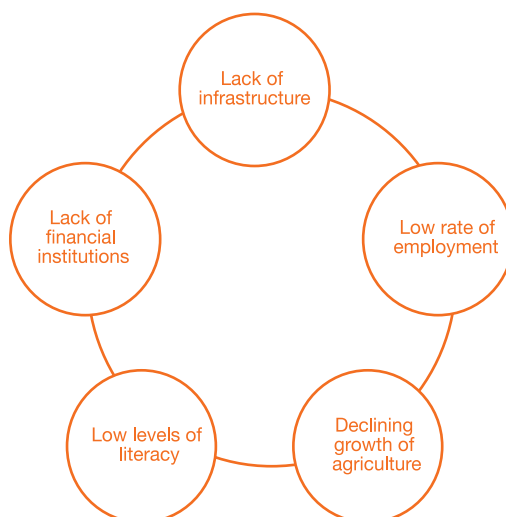
State	#Projected Rural population as on Mar-2010	Projected Rural households as on March 2010	Amt sanctioned based on per household scheduled cost (Rs)	Total Sanctioned amount	Amt released as 1st installment in 2009-10 (in Rs lakhs)
Andhra Pradesh	60726000	12145200	20	2429.04	1015.09
Arunachal Pradesh	851000	170200	30	51.06	35.28
Assam	25742000	5148400	30	1544.52	1067.06
Bihar	86255000	17251000	20	3450.2	1441.83
Chhattisgarh	18480000	3696000	20	739.2	308.91
Delhi	853000	170600	-	-	0
Gujarat	34922000	6984400	20	1396.88	583.76
Haryana	16727000	3345400	20	669.08	279.61
Himachal Pradesh	5994000	1198800	30	359.64	150.3
Jammu & Kashmir	8489000	1697800	30	509.34	212.86
Jharkhand	23844000	4768800	20	953.76	398.58
Karnataka	37127000	7425400	20	1485.08	620.62
Madhya Pradesh	51471000	10294200	20	2058.84	860.39
Maharashtra	60158000	12031600	20	2406.32	1005.6
Meghalaya	2059000	411800	30	123.54	85.36
Mizoram	469000	93800	30	28.14	19.45
Orissa	33693000	6738600	20	1347.72	563.21
Punjab	16938000	3387600	20	677.52	283.14
Rajasthan	50828000	10165600	20	2033.12	849.64
Tamil Nadu	31232000	6246400	20	1249.28	522.08
Tripura	2903000	580600	30	174.18	120.34
Uttar Pradesh	154211000	30842200	20	6168.44	2577.79
Uttaranchal	7048000	1409600	30	422.88	176.73
West Bengal	63462000	12692400	20	2538.48	1060.83

Source: Utilisation of Funds, Census 2011

## Eastern India: An Overview

Widespread poverty continues to be a humongous challenge, especially in Jharkhand, Bihar and Orissa. With limited scope and entrepreneurship skills, these state economies are battling for revival. The lack of basic infrastructure, reach of financial institutions and debt-ridden households do not create an entrepreneurship environment. Further, low levels of literacy only aggravate the situation, pulling the poor deeper into a debt trap.

Some of the challenges that hinder the development and growth of the eastern belt are shown here.



*More than 70% of the rural poor in the country are concentrated in Bihar, Orissa, Madhya Pradesh, Jharkhand, Rajasthan, Chattisgarh, Uttar Pradesh and Assam.*

All the data and statistics in the previous section indicate that the eastern region is lagging behind. But, it would be unfair to say that the region does not have the potential or resources to perform and sustain the growth rate.

The eastern region has diverse geography, culture and deals with its own set of challenges. It has been observed that initiatives and measures, which might have worked in other regions of the country, are yet to make a mark in this region.

### **Strengths of the eastern region**

- Cheap and skilled labour
- Huge potential for agri-business with fertile soils, favourable climate and aggressive land reform programmes
- Low cost of living
- High score on business confidence index

A well laid-out and implemented reform programme is required to haul the eastern belt out of poverty and economic inequality. Strong initiatives and measures need to be effectively implemented, to help push the region on a high growth trajectory

Looking at the gravity of the situation, even the World Bank is focussing on partnering with these low-income states to support structural reforms.

By the end of June 2010, the Bank had 75 active projects with a net commitment of about US\$ 21.4 billion.

**What should be the focus areas?**

- Self–employment programmes, enabling flow of credit
- Development of infrastructure, physical and social  
*Focus on agriculture*
- Enhance public expenditure on education and healthcare with participation of all stakeholders
- Policy support through government intervention to ensure balanced credit disbursements

Commitments	FY05	FY06	FY07	FY08	FY09	FY10
New lending to government (in US\$ billion)	2.9	1.4	3.7	2.1	2.3	9.3
Total commitments (active projects) (in US\$ billion)	12.8	11.3	14.3	13.8	14.9	21.4
Total number of active projects	64	56	67	60	61	75

Since SMEs play an integral role in generating employment opportunities, it is necessary to evaluate the measures which have been taken to give them a boost and also discuss some of the current challenges faced by them.

# Employment: The SME perspective

India is in a transition phase, undergoing demographic changes with an increasingly large number of people in the working age group of 15 to 59 years. As per a 2010 report by the Ministry of Labour and Employment, the proportion of unemployed is 49 persons per 1,000 persons in the working age group.

A report by the Census projects that by 2016, this working age group population will rise to 63.9% and by 2021 to 64.2%. The report also suggests that in absolute numbers, there will be approximately 63.5 million new entrants to the working age group between 2011 and 2016.

*In 2020, the average Indian will be only 29 years old, as compared to 37 in China and the US, 45 in west Europe and 48 in Japan.*

## Census Projection Report

It is important that India uses its demographic dividend to the best extent possible, in order to create a favourable employment scenario.

Providing gainful employment to every individual is an important component of inclusive growth. To attain this, we need to understand the peculiarities of the labour market. Some of the factors which play a critical role in determining the employment numbers in India include the following:

- Full-time or part-time workers
- Workers with multiple jobs
- Seasonal workers
- Migrant labours
- Social and cultural factors

Another observation is the low participation of women in the labour market. Only 15 to 18% of the labour market in the urban areas comprises women, whereas in the rural areas the range varies between 25 and 30%.

It is imperative for India to stress on the importance of creating skilled labour. This adds to the level of productivity, resulting in increased earnings and reduced levels of poverty. It is believed that the favourable demographic dividend

in India can be best influenced by upgrading worker skills.

## Important strategic initiatives

- *Provision of skill and training to women workers in rural areas*
- *Quality of training to ensure the credibility of training institutes*
- *'Learning the right skill' to match industry demands. Also, industry should participate in skill development, in order to impart the correct skill set to fulfil industry requirements.*
- *Development of skills and competency standards with proper qualifications at par with international standards*
- *Free flow of information regarding labour requirement, labour inventory, skill-development plans and labour training*



## *The SME perspective*

The small and medium enterprises (SME) sector is instrumental in generating employment opportunities, contributing around 45% of industrial production and 40% of exports in India. The sector employs 60 million people and creates 1.3 million jobs each year. The contribution of the SME sector to GDP is 17% in 2011 and is expected to increase to 22% by 2012. Presently, there are 30 million MSME units in India and it is likely that an additional 12 million people will be part of this workforce over the next three years.

The SME sector is characterised by high labour-capital ratio, shorter gestation periods, low investment requirements and concentration in smaller markets. It is a key link in supplying raw materials, finished parts, components, etc. to large industries. The SMEs boost local demand and consumption, and act as a growth engine of the economy.

Even though the development of micro, small and medium enterprises (MSMEs) is vital for more jobs and poverty alleviation, this sector faces policy and financial constraints. Combating

low levels of literacy and limited self-employed training, this sector needs the backing of government policies, increased access to finance and employment opportunities, etc.

Entrepreneurship needs focus and concentrated attention to bring improvements in the socio-economic status of India and reduce economic disparities. The SME sector differentiates itself by making use of local resources, trying to inject innovativeness in products and services, and by creating transformational change at each level.

On a broader level, the strategy of the SMEs is to provide a solution to under-employment and divert the surplus resources in the agricultural sector by deploying them in the SME sector. Encouraging agricultural labourers to turn entrepreneurs will yield an increase in agricultural productivity, increase income of the rural strata and provide a boost to industry growth.

However, due to its small size, the SME sector gets entangled in difficult situations, while trying to tap the right kind of markets, procuring raw materials, and accessing credit and consulting services.





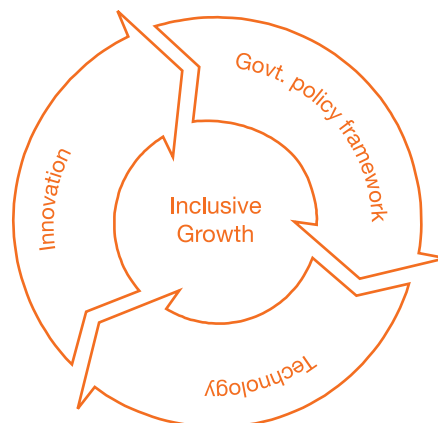


### **Prime challenges for the SME sector, especially in the eastern region**

- Absence of banking finance
- Limited capital and knowledge
- Limited use of technology
- Low production capacity
- Ineffective marketing strategy
- Identification of new markets
- Constraint on expansion
- Non-availability of high skilled labour at affordable cost

The above challenges have been discussed in further detail, supported by inputs gathered through interviews and interactions with SMEs and other stakeholders. Assessing most of these challenges leads us to believe that broad policy level changes are required to drive SMEs in the right direction.

- Socio-economic growth
- Generate employment
- Reduce economic disparities



Some policy changes that have been undertaken are as follows:

- *Provision of subsidies:* The government has on many occasions granted subsidies to industries for power, water, tax, land, etc. But more often, these do not really help small scale industries and are targeted towards larger industries.
- *Technology assistance:* Policies providing some degree of technology assistance works better for SMEs to upgrade their processes and operations. Support needs to be provided for increasing capacity, upgradation of processes, etc.

### **Recommendations for further development of SMEs**

- Conducive environment for investment through better policies
- Improved access to finance
- Alternative sources of investment for entrepreneurs
- Improved entrepreneurship skills

## Global overview

### **A study by IFC/World bank (2010)**

- In the 132 economies covered, there are 125 million formal MSMEs of which 89 million operate in emerging markets
- Formal MSMEs employ more than one-third of the global population, contributing around 33 percent of employment in developing economies
- Globally, the number of MSMEs per 1,000 people grew by 6 percent per year from 2000 to 2009; Europe and Central Asia experienced the biggest boom, with a growth of 15 percent
- East Asia and the Pacific have the highest ratio of MSME employment to total employment. This is mainly driven by China, where formal MSMEs account for 80 percent of total employment



# SME banking: Bridging the gap

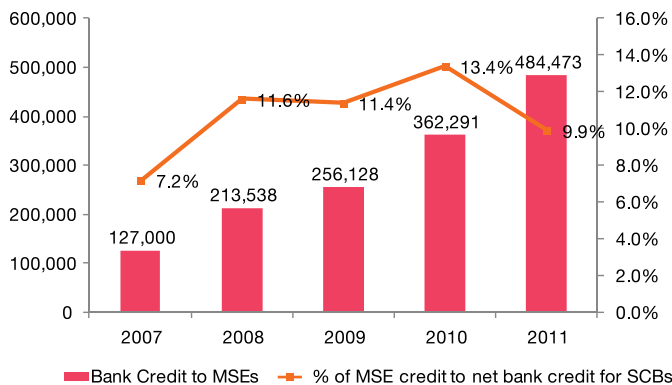
Realising the importance of medium- and small-scale enterprises, the credit rendered to this sector is treated as priority sector lending. It is mandatory for banks to provide at least 40% of their advances to this sector. The total credit outstanding to the SME sector as of March 2011 was Rs 4,84,473 crore, as compared to Rs 3,62,291 crore in March 2010 (an increase of 41.4%).

Even though the above data indicates that there has been an increase in lending credit to SMEs, there is a huge gap at the ground level, where SMEs observe that a large part of the funds are routed to large companies and only 4 to 5% of MSMEs have access to institutional funding.

Financial institutions need to look at financing the SMEs as an opportunity. They need to gradually increase their foothold in this segment. Moreover, emerging economies like India can draw upon the experiences of banks in developed economies to expand their SME operations and help them convert into viable business models.

Although traditionally, banks have been dealing in high-value and low-risk client bases, banks in developing economies are now consistent in thinking that SME financing can be a potential area of revenue generation. With microfinance institutions (MFIs) catering to the smallest of the SMEs and banks focussing on larger industries, the SME category falls into a grey area, which increases the problem of financing them.

## Bank credit to SMEs



Source: RBI

## Need for finance

- Lack of cash flow for SMEs to make investments
- Lack of access to financial markets

# Targeting the bottom of the pyramid: Financial inclusion

This chapter discusses the most crucial pillar of inclusive growth—financial inclusion.

- In India, only 55% of the population has deposit accounts and 9% has credit accounts with banks.
- India has the highest number of households (approximately 145) which remain excluded from the net of banking.
- There is only one bank branch per 14,000 people.
- Only 18% have debit cards and less than 2% have credit cards.
- Less than 20% of the population has any kind of life insurance.

The concept of financial inclusion may actually be interpreted in different ways in different countries. In developing economies, it speaks of access to financial products as well as the awareness about them. However, in developed nations, it is more about the knowledge of financial products and financial literacy.

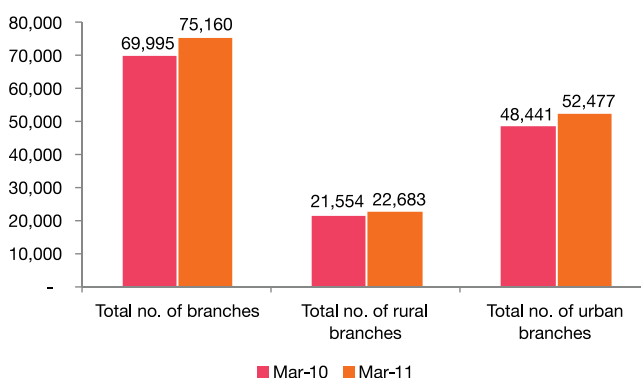
Facilitating access and reach for the low-income segment at an affordable cost is the prime objective of financial inclusion. The reason why it has taken such a long time to spread in India is because there is lack of an

adequate delivery mechanism, an elusive and suitable business model and skewed leverage of technology to give this initiative a boost.

Financial literacy lies at the foundation of any initiative towards financial inclusion. So, we need to build on the levels of financial literacy of the population before beginning to concentrate on other areas of boosting financial inclusion.

The progress of penetration by way of number of branches has been mentioned below:

## Growth of branches over the last two years



Source: RBI

Enumerated below are some of the achievements in financial inclusion over the past two years, with targets for the next two years.

Particulars	Mar-10	Mar-11	Mar-12	Mar-13
Total no. of BCs deployed	33042	58361	125988	187972
Villages covered through branches	21499	22684	24618	25694
Villages covered through BCs	33158	76801	197523	320441
Villages covered through other modes	100	355	1361	2177
Villages covered - Total	54757	99840	223502	348312
No-frills accounts (no. in lakh)	495.53	743.9	1096.24	1533.15
No-frills accounts (amt. in crore)	4895.19	6565.68	9311.02	11323.26
KCCS (no. in lakh)	195.24	224.89	322.59	407.33
KCCS (amt. in crore)	107518.8	143862.2	152113.6	179254.8
GCCS (no. in lakh)	6.37	9.5	46.89	81.13
GCCS (amt. in crore)	813.85	1307.76	3229.12	5669.73

Source: RBI; Note: BC- Business Facilitator; KCCS – Kisan Credit Cards; GCCS – General Credit Cards

Some of the broad challenges that act as roadblocks to the furtherance of financial inclusion are as follows:

- *Demographic spread*
- *Low income*
- *Literacy*
- *Physical connectivity*
- *Lack of savings*
- *High cost of operations*
- *Lack of technology*
- *No suitable distribution model*
- *Lack of infrastructure*
- *Looked upon as an obligation, not a business opportunity*

## *A snapshot of the eastern region*

Around 40% of rural households lack access to bank accounts. This aggregates to over 60% in the eastern and north-eastern regions of India.

- Farm households not accessing credit from formal sources as a proportion to total farm households is around 82%.
- The more economically backward the region, the higher the share of regional rural banks (RRBs). The east has 40% share of RRBs as compared to 56% share in the north-east.

The regional rural banks have been established to cater to agriculture and other rural sectors. They are focused on mobilising the savings from the rural and semi-urban areas and granting loans to small and

marginal farmers, labourers and rural artisans.

- Overall indebtedness to formal sources of finance is around 20% in this region.

To enable the success of the financial inclusion drive, some banks in that region have undertaken the following measures:

- Financial literacy programmes to increase awareness about financial products, debt counselling, savings, credit, etc.
- Complementing the brick-and-mortar model with technology to enhance reach to far-flung areas
- Tie-ups with micro-finance institutions and post offices
- Promotion of no-frills account among the low-income segment

## *Financial inclusion: Lessons for India*

- **M-Pesa in Kenya**

Launched in 2007, M-Pesa has leveraged mobile technology to the maximum. It signed up over 50% of the adults in less than four years to a mobile phone based retail payment system. It started with facilitating loan payments and repayments under the micro-credit schemes.

Gradually, the idea of the small savings scheme picked up. The system allows users to send or withdraw money from over 23,000 retail outlets, compared to about 1,000 bank branches before. At the same time, absolute amounts remain small, reflecting the income level of the users.

M-Pesa is a classic example of how mobile technology can help to address financial exclusion and become an integral part of the financial system

- **Financial inclusion in Malaysia**

The commitment to financial inclusion in Malaysia is reflected in the 3,300 deposit accounts per 1,000 adults and 1,100 loan accounts per 1,000 adults, among the highest in the world. They have followed the below-mentioned strategies:

- Creation of a business environment that allows a diverse range of financial service providers to thrive and compete
- Basic banking products and services made available at reasonable costs
- A diverse set of delivery channels introduced to ensure widespread access to financial services. In 2008, there were nine bank branches per 1,000 square kilometres and 24 ATMs per 1,000 square kilometres in Malaysia. In comparison, the global median is seven bank branches per 1,000 square kilometres and 15 ATMs per 1,000 square kilometres.

- Provision of greater financial literacy and awareness so that consumers do not fall prey to lending and investment scams

- **Financial inclusion in Indonesia**

Adopting a branchless banking strategy in Indonesia with the help of a biometric solution has helped reach out to the unbanked population. A leading bank in Indonesia used the branchless system to launch a new micro-finance business diversifying its current pension loan business. The bank saw a large increase in its loan activity and is poised to continue capturing more of the low-income market for growth. The biometric system led to greater reach, improved operating efficiency and reduction in operator error. The electronic data capture system also reduced the likelihood of fraud.

In India, financial inclusion is a bank-driven model unlike a telecom-driven model in other countries. Hence, for a successful financial inclusion drive, banks need to play a key role.

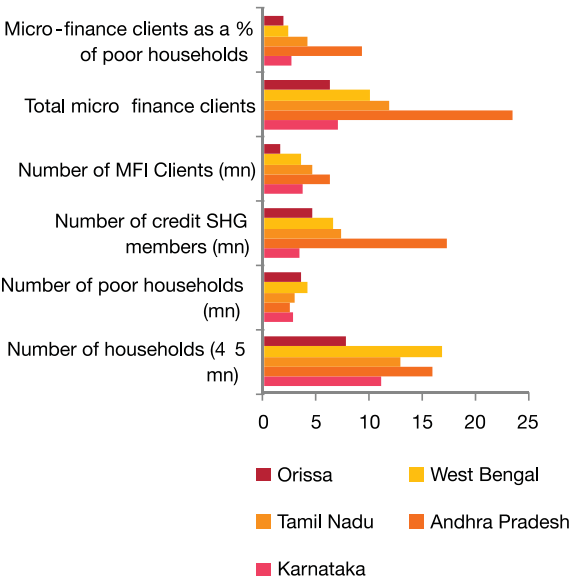
# Micro-financing: A comparison

The micro-finance sector comprises customers in need of small loans, members of co-operative credit societies and self-help group members. However, as with other things, micro-finance lending also varies across states, being heavily concentrated in the south as compared to the east. The chart below gives a comparison of micro-financing across states in India.

The number of poor households is seen to be concentrated in Orissa and West Bengal at 3.56 mn and 4.16 mn respectively, while Andhra Pradesh has 2.52 mn households. The number of credit self-help group (SHG) members and microfinance institution (MFI) clients are much higher in the southern states, especially in Andhra Pradesh, as compared to West Bengal and Orissa.

The self-help groups have been leveraged not only to provide financial services but also a means of livelihood. In Andhra Pradesh, the SHGs are very well networked, supported adequately by the banking system. As of March 2010, the number of SHGs with savings with the banking system was reported as Rs 6.81 mn, with savings of Rs 63,580 mn, as compared to Rs 55,456 mn in March 2009.

## Micro-finance financing across states (2010)



There has been a decline in the percentage share of SHGs with loans outstanding in the eastern region, whereas the central, western and southern regions showed an increase in 2010. A possible reason for the decline in the loans outstanding is that repeat loans are not available to SHGs after repayment of the earlier loans. In the southern states, however, there is a lot of pressure from state authorities for lending to SHGs.

Source: Report on micro-finance in India 2010



# Infrastructure development and financing

Emerging as one of the fastest growing economies in the world, India has seen a boost in its investment. Providing quality infrastructure is a key component to raising the growth potential in any economy. As a key driver of inclusive growth, infrastructure development, both in the rural areas and urban areas, needs attention.

India ranks very low on the parameter of infrastructure financing, spending only around 6% of its GDP on infrastructure, as compared to China which spends around 20%.

Traditionally, infrastructure financing was vested with the government, but with economic reforms, it has also been opened up to the private sector. Investment from the private sector is obtained only in those sectors where the user cost has been defined properly and is easy to recover. Irrigation, water supply, electricity, gas, etc have no transparency in user cost, a deterrent to secure private investment.

As per the 11th Five Year Plan (2007-2012), an investment of over US\$ 500 billion had been estimated.

Sectors	Tenth Plan (2002-2007)	Eleventh Plan (2007-2012)
Electricity, Roads & Bridges	436742	980677
Telecommunication	103365	258439
Railways, Irrigation, Water Supply and Sanitation	295964	658839
Ports & Airports	20842	118963
Storage & Gas	14532	39233
Total	871445	2056151

Source: Planning commission

As per the assessment of the Planning Commission, during the 12th Plan (2012-17) India may need infrastructure investments of over US\$ 1 trillion.

To meet the growing demand of infrastructure, financing needs to be facilitated through a well-developed debt market. Also, appropriate instruments for credit institutions should be provided while accounting for the risk. Banks have been the main source of financing in India. However, since the RBI is cautious about asset-liability mismatches and risk of concentration, it has not allowed too much focus on infrastructure financing.

## A recent study by IMF on infrastructure financing across four emerging countries - Chile, Korea, Brazil and China--presents some lessons for India.

- Chile and Korea have been particularly successful in developing their bond markets to support infrastructure requirements.
- The development of the pensions system in Chile went a long way in creating a market for local currency denominated long-term securities, minimising the need for bank finance.
- In China and Brazil, bank loans have played a major role in financing. In China, public banks have provided long-term financing, whereas in Brazil, BNDES the primary development bank, has provided the financing.
- Chile is the only country which has been successful in garnering the interest of institutional investors to buy into long-term bonds issued fully by private companies. Pension funds are able to invest only in investment grade securities. Private insurance companies have insured infrastructure bonds, which allow pension funds to buy into these markets.
- In Korea and Brazil, large public sector electricity companies are able to issue debt in international credit markets. Both countries have also been reasonably successful at encouraging foreign companies to invest in publicly guaranteed infrastructure funds (Korea) and in public-private partnerships (Brazil). This might be practical for some larger Indian corporates or public utilities, but the fiscal risks will have to be carefully monitored and managed.
- In China, foreign participation in infrastructure is minimal, while in Chile, a competitive electricity sector is operated to a large extent by foreign-owned multinationals. In Chile, foreign companies bid for and buy road construction and operation public-private partnerships (PPPs) along with domestically owned companies.
- Looking at these countries, India can aim to have a sound strategy to achieve better development of the infrastructure sector.

### ***Our recommendations:***

- *Involving the pension funds and insurance companies to fund long-term infrastructure projects*
- *Creating a well-developed corporate bond market for providing alternate sources of finance*
- *Leveraging the PPP model to improve services. For this model to be successful, it needs to be embedded in a strong regulatory framework which entails regular monitoring and transparency.*
- *Allowing tax benefits for bonds and flexibility in terms of tenure of long-term bonds issued by banks*
- *Securing private financing for a favourable business environment and transparency in policy administration*

# Key Research findings

Our survey was targeted towards interacting with banks, SMEs and other stakeholders to gain an understanding of some of the factors that affect the pace of the growth of the economy. In this case, the questions focused more on the eastern region, directed at the target segment to evaluate the progress made and what remains to be done.

We spoke with a few banks based in the east to understand their views on growth acceleration, banking on financial inclusion, SME development, infrastructure development, etc. We also managed to assess some of the roadblocks and constraints they face while conducting business.

Some of the highlights of the discussion were:

## ***On financial inclusion and growth***

- *Presently, with the new government in West Bengal, there is much discussion and deliberation on how best to improve the penetration of financial products and gain access to the masses.*
- *Some banks have tied up with SME rating agencies (SMERAs) to increase penetration, assisting in project kick-off and identifying viable sources of funding.*
- *It is not only important to reach out and open branches in remote rural areas, but also to stress on the sustainability of these branches.*
- *Presently, the role of BCs and BFes employed by banks lacks continuity. For instance, once the designated number of accounts have been opened in the rural branch and the agent has earned his/her commission from the institution, he/she requires a formal channel to continue this outreach.*
- *Gradually influencing the mindset of the rural segment, increasing financial literacy levels and promoting the usage of the products already in the market plays a significant role in growth.*
- *Presently, the recovery of loans mechanism faces multiple challenges with banks and MFIs.*

## On creation of jobs

- There is a need to create skilled labour in rural industries.
- Improved corporate financing will lead to job creation in the long run.
- Need for change in mindset in the east in order to adapt to technology
- Strict measures and governance to ensure the correct application of funds

## On the government

Banks firmly believe that the government needs to play a key role in catering to the infrastructure requirements of the eastern states. Some of the things high on the list of priorities are as follows:

- Road transport: Lack of 'all weather' connectivity between states
- Facilitating an uninterrupted supply chain, from the start to the end of projects
- Technology assistance and improvements
- Streamlining of the central registry process land registrations with the use of technology. Since the process is not computerised, the same piece of land/house/apartment is mortgaged multiple times to obtain finance, leading to defaults.
- Coordination between the government and financial institutions to attain the goals of financial inclusion
- A well-defined financial framework linking growth to the objective of financial inclusion

## Recommendations

- Need to promote financial literacy even in urban areas and urge the importance of financial planning
- A boost for infrastructure development with better road connectivity, employment opportunities and increased financial awareness
- The increasingly important role of SMEs, banks and MFIs in boosting access to finance. They need to gradually replace the unorganised sector in lending.

## Especially for SMEs

- *Training is required for SMEs as many lack marketing skills and the sector knowledge is unused.*
- *Skill-based or sector-specific micro-financing products could be rolled out to cover artisans in remote areas.*
- *Provision should be made to provide opportunities to SMEs for R&D. SMEs cannot fund R&D activities. At the grassroot level, they can conduct fruitful research, with the aid of the government.*

### Some of the measures undertaken by government bodies

- Financial literacy cum credit counselling centres (FLCC) have been set up in the backward districts of India for credit and technological counseling. NABARD is providing financial assistance upto 60% of the requirement or 10 lakh INR whichever is higher, for setting up FLCC.
- The farmers' club programme started by NABARD facilitates transfer of technology, capacity-building of members to act as business facilitators and business correspondents, formation of self-help groups, etc.
  - The region-wise distribution of clubs indicates that the central region has the major share (29.85%), followed by the south (24.47%), east (18.81%), west (13.03%) and north (10.82%).
- Documentaries on Doordarshan and distributing literature/newsletters and VCDs to the farmers' clubs helped in technology transfer.
- the Financial Inclusion Technology Fund (FITF) and Financial Inclusion Fund by NABARD are providing a boost to financial inclusion.
- The policy of preferential treatment to the states in the north-east and hilly regions was extended also to the states in the east in 2009-10. As a result, the financial institutions in Bihar, Jharkhand, Orissa and West Bengal have benefited.
- Concessions include 100% re-finance, concessional interest rates on re-finance and relaxation in eligibility criteria with respect to recovery and gross/net NPA.

### Recommendations

- Training of the BCs and BFIs and creating a sustainable environment for them
- Financial inclusion to cover not only no-frills accounts but also savings, pension, insurance, payments and remittance facilities
- New incentive scheme by the government for a mandate on local employment creation to ensure balanced regional growth
- Overall sustainability of industrialisation to depend on infrastructure. Single-window mechanism is being modified.
- Opportunities like HR development, skill development and R&D to be capitalised on for improved development

# Imperatives for inclusive growth in the Eastern region

- **Focus on infrastructure development**

Development of freight corridors in the east is of utmost necessity to upgrade the capacity of the system. The completion of these projects must be undertaken in a timebound manner and monitored carefully to avoid delays. Inadequate infrastructure also hinders private investment in this region.

- **Agriculture sector as key to development**

The agriculture sector has been neglected, with small and marginal farmers engaged in diversified subsistence farming. Government policies on a broader level need to be made more favourable for poor farmers. Also, credit facilities need to be made available to landless labourers and small and marginal farmers. Favourable agricultural programmes need to be introduced. It should be ensured that they do not get entangled in the bureaucratic shackles.

The Green Revolution needs to be extended to the low productivity areas in the east, where there is an abundance of ground water. This needs to be adequately supplemented by investments in power, logistics and marketing.

- **Improved governance in state**

For holistic development, the government needs to work with focused precision, to reach its goals of inclusive growth. Improved transparency in procedures, regular monitoring and better governance will help bring the goals closer. It will also help to involve the local people in land development, agriculture projects, etc.

- **Skill development for employment opportunities**

An important area for inclusive growth is the provision of employment opportunities. In order to provide employment, it is important to hone the right skill set in demand. Providing the opportunity for skill development and education will lead to higher incomes and improved conditions of livelihood, thereby benefiting economic growth.

- **Popularising technology**

Efforts need to be made to popularise technology within this section of society. A step-by-step process needs to be initiated where awareness needs to be created, the way needs to be shown to build capacity finally showing results.

- **Collection of data**

An important component that will lend direction to the strategy of inclusive growth is the availability of accurate data on the various socio-economic metrics in the east. An aggregation of this data will enable policymakers to formulate and implement appropriate policies in a more focused manner.

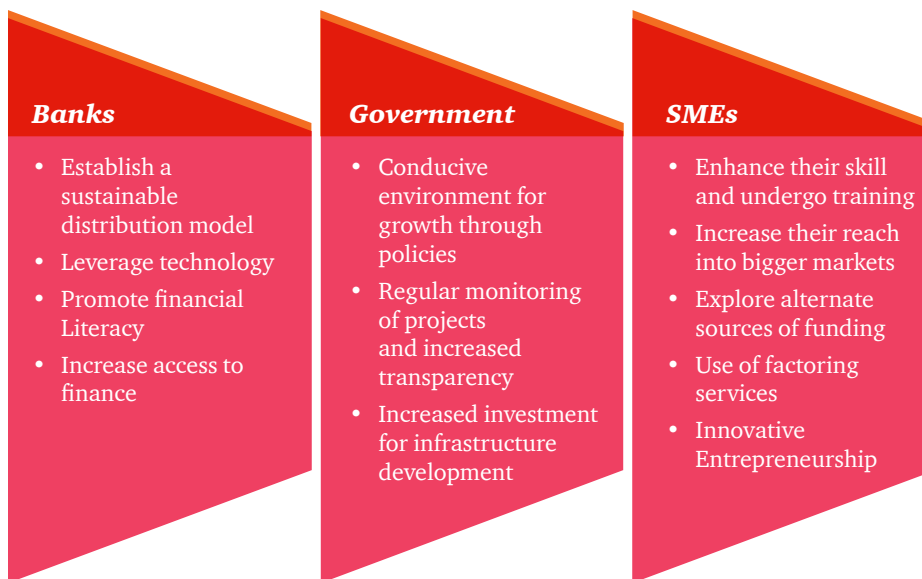
- **Education and literacy**

A very basic condition for inclusiveness at the grassroots is education and literacy of the weaker section of the society. Without basic education, any kind of development cannot take shape and the minds of the rural population cannot be influenced.

- **Need for a viable business model**

In order to spread the use of financial products and services, a resilient and viable business model is needed for the unbanked. Using technology, customised products need to be delivered to this population at an affordable cost. Only when this model is in place, can the savings of this strata of the population be channelised into the formal financial system.

### *Roadmap for the next decade*



The roadmap highlights some of the measures banks, the government and SMEs need to implement for accelerated growth in the next decade.

# Conclusion



To sum up, inclusive growth is a slow and steady process which needs focus on certain key aspects like infrastructure, accessibility to financial institutions, education, creation of jobs, etc. The XII Five Year Plan has continued the focus of the XI Five Year Plan to invest in building social infrastructure – education, public health, drinking water, creation of rural infrastructure so as to better position economic empowerment among the marginalised sections of the population in the east. The roll out of the ‘Adhar’ promises to further connect the economically backward sections of the eastern states into national economic mainstream.

Most importantly, the government alone cannot achieve

this objective. It needs support from various players in the nation’s tertiary / services sector, viz. the banks, other financial institutions and the financial industry sectors. All stakeholders need to contribute in equal measure to make the agenda of inclusive growth a success.

The east has remained behind because of numerous problems in public administration, policy implementation, slow decision-making, lack of adequate funding for projects and a slowdown in the development of an entrepreneurial environment. It is time the eastern states looked at the more developed states to pick up the best practices and trends to move to a more inclusive and sustainable growth model.



# *Notes*



# About PwC

PwC firms provide industry-focused assurance, tax and advisory services to enhance value for their clients. More than 161,000 people in 154 countries in firms across the PwC network share their thinking, experience and solutions to develop fresh perspectives and practical advice. See [pwc.com](http://pwc.com) for more information.

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# About CII

The Confederation of Indian Industry (CII) works to create and sustain an environment conducive to the growth of industry in India, partnering industry and government alike through advisory and consultative processes.

CII is a non-government, not-for-profit, industry led and industry managed organisation, playing a proactive role in India's development process. Founded over 116 years ago, it is India's premier business association, with a direct membership of over 8100 organisations from the private as well as public sectors, including SMEs and MNCs, and an indirect membership of over 90,000 companies from around 400 national and regional sectoral associations.

CII catalyses change by working closely with government on policy issues, enhancing efficiency, competitiveness and expanding business opportunities for industry through a range of specialised services and global linkages. It also provides a platform for sectoral consensus building and networking. Major emphasis is laid on projecting a positive image of business, assisting industry to identify and execute corporate citizenship programmes. Partnerships with over 120 NGOs across the country carry forward our initiatives in integrated and inclusive development, which include health, education, livelihood, diversity management, skill development and water, to name a few.

CII has taken up the agenda of "Business for Livelihood" for the year 2011-12. This converges the fundamental themes of spreading growth to disadvantaged sections of society, building skills for meeting emerging economic compulsions, and fostering a climate of good governance. In line with this, CII is placing increased focus on Affirmative Action, Skills Development and Governance during the year.

With 63 offices including 10 Centres of Excellence in India, and 7 overseas offices in Australia, China, France, Singapore, South Africa, UK, and USA, as well as institutional partnerships with 224 counterpart organisations in 90 countries, CII serves as a reference point for Indian industry and the international business community.

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