

**FINANCIAL INCLUSION, ACCESS TO CREDIT:  
IMPLICATIONS FOR ECONOMIC DEVELOPMENT IN  
ARUNACHAL PRADESH**

Policy Conclave December 8-9, 2017

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Theme: Economy and Development  
Sub Theme: Expanding the Role of Institutional Credit in  
Arunachal Pradesh

# **FINANCIAL INCLUSION, ACCESS TO CREDIT: IMPLICATIONS FOR ECONOMIC DEVELOPMENT IN ARUNACHAL PRADESH**

## **1. INTRODUCTION**

The challenge of enhancing financial inclusion has gained serious attention of policy makers globally. Absence of access to institutional credit is not only detrimental to economic growth, but also creates vulnerabilities amongst the poor and marginalized sections of society. Financial inclusion is a crucial instrument of poverty reduction, while creating a buffer to manage risks. In the Indian context, this is a far more crucial imperative, especially in times of economic distress for the poor, who are mostly employed in the informal sectors. Globally, 2 billion people did not have a bank account in 2014 (Demiguc-Kunt et al 2015). In 2014, only 42% of all adults reported borrowing in the last one year (excluding the usage of credit cards). In a study of towns in Mexico where bank branches were opened rapidly, it was demonstrated that increased access to financial services leads to an increase in incomes for poor families and creating an overall increase in employment (Bruhn and Love 2014). Empirical data also suggests that financial inclusion helps poor households to improve their standard of living, paving the way for higher economic growth. (Rajan and Zingales 1998. Bitten court 2012).

This paper seeks to understand the recent changes of government policy at the national level in India for expanding financial inclusion and access to formal credit. It then specifically examines the presence of banks and access to institutional credit in the north eastern region, with specific reference to the state of Arunachal Pradesh. It tries to draw policy learnings on the challenges and implications for economic development of the state.

## **2. FINANCIAL INCLUSION IN INDIA**

The Rangarajan Committee on Financial inclusion in India, 2008 defined financial inclusion as the “process of ensuring access to financial services and timely and adequate credit where needed by vulnerable groups such as weaker sections and low income groups at an affordable cost.” Clearly, this definition goes beyond a simplistic approach of having the ability of opening a bank account as sufficient indicator for financial inclusion. It clearly spelt out that if any deserving and genuine claimant of access to credit and financial services is denied the same, it is clearly a case of financial exclusion. At the national level, several strategies have been rolled out over the years by RBI and Government of India including establishment of Regional Rural Banks(RRBs), mandatory priority sector lending norms, introduction of no frills accounts, kisan credit cards for farm loans, introduction of Banking correspondent model as an alternate to brick and mortar service delivery. In spite of these policy interventions, as per 2011 census, only 58.7% of households availed banking services in India. In 2014, only 53% of India’s adult population had an account as per World Banks Financial Inclusion Index Findex. (Demigurc-Kunt et al 2014).

An empirical study sought to compute a Financial Inclusion Index at a pan India level for 2013 using three basic dimensions: (i) proportion of adults having access to bank accounts (ii) usage of bank accounts measured by adults who ever used the account for any financial activity (iii) availability measured by access to bank branch/ATM/others within a kilometer of place of stay. (Mukhopadhyay 2016). Huge regional variations were apparent with 48% adults having access to bank accounts nationally, the lowest proportion being in the North Eastern region at 30%. A similar result was revealed in the ranking of states done by CRISIL(2015) based on Inclusix, where in North Eastern region was ranked at the bottom of the heap with an index of 38.6 on a scale of 100, in sharp contrast to Goa which had the highest at 76.1. The north eastern region is the worst performer both from a demand side and supply side perspective of financial inclusion. In terms of access to credit, data revealed that amongst the poor, nearly 22.15% of the poor and 44.29% of the non poor borrowed from the money lender. Borrowing from the banks stood at 48.44% for the poor and 55.71% for the non-poor. (Mukhopadhyay, 2016).

The biggest policy disruptor in the financial inclusion space was the launch of Pradhan Mantri Jan Dhan Yojana (PMJDY) on August 28, 2014, which set an ambitious agenda of universal banking coverage. It allows opening of zero balance accounts, with an overdraft facility of upto Rs 5000 and an accident insurance coverage of Rs 1 lakh, life insurance cover of Rs 30,000. It also has a facility of RuPAY debit card. As on November 8, 2017, more than 300 million accounts have been opened under this scheme with deposits of over Rs 676 billion. This has been coupled with a policy push for enhanced transfers of public entitlements through Direct Benefit Transfers (DBT) using the Aadhar payment bridge and the Public Financial Management System. In popular policy parlance a new acronym of JAM trinity (Jandhan, Aadhar, Mobile) has found acceptance as the government pushes for greater cashless transactions.

A study from raw data of 135147 individuals across India between 2013 and 2015 showed that nearly 20% of the PMJDY accounts were opened through Business correspondents. However, less than one percent of the bank account holders used them for financial transactions. (Gunther, 2017). The same study revealed an asymmetry in state wise bank account ownerships and that between 2013 and 2015, the north eastern region witnessed the highest growth of 36%. One of the key underlying motives to open a bank account was to receive government payments. Opening of bank accounts has however not translated to a similar rise in credit offtake. It was brought out that in the two year period, the ATM usage increased from 24% to 35%.

Acknowledging that there are nearly 5.77 crore small businesses, mostly sole proprietorships which don't have access to formal credit, the Government of India launched the Pradhan Mantri Mudra Yojana which offers three tiered loans : Shishu for start ups with finance of uptoRs 50,000, Kishore uptoRs 5 lakhs and Tarun upto Rs 10 lakhs for business expansion. MUDRA bank was established simultaneously to provide refinance facility to banks which offer such loans. In 2017-18 so far more than 2 crore loans have been sanctioned and a sum of nearly Rs 1 lakh crore has been disbursed. In 2016-17, more than 3.9 crore loans were sanctioned under this scheme with a total disbursement

of Rs 1.75 lakh crores.

### 3. THE SPECIAL CONTEXT OF THE NORTH EASTERN REGION

As per the 2011 census, the states of the North eastern region(NER) account for 8% of geographical area. The percentage of poor as a proportion of population in the region stood at 30.57% as compared to national average of 21.92%. In Arunachal Pradesh, 34.67% of the people were below poverty line. In March 2016, the CD ratio for the NE region was 38.4 as compared to the national average of 78.3. In Arunachal Pradesh the CD ratio was amongst the lowest at 29 (RBI 2016). The average credit per adult in the North Eastern region was Rs 15,877 way below the national average of Rs 56,298 (Table 1, Column 5). The amount outstanding per account in priority sector lending in the region is also far lower than national average. (Table 2) Within the north eastern region, the average credit offtake is the highest in Sikkim. This can perhaps be explained by the fact that Sikkim has the highest density of bank branches, highest share of manufacturing, highest per capita income in the region. (Sangwan: 2016).

**Table 1. Outstanding credit of Scheduled commercial banks in NER**

State/Region	Number of Accounts	Amount outstanding(Rs million)	Amount per account (Rs)	Credit per adult (Rs)
1	2	3	4	5
Arunachal Pradesh	71401	16320	22,857	17,125
Assam	1,787,055	268,523	15,026	12,504
Manipur	92,537	13,495	14,583	7,197
Meghalaya	143,681	31,194	21,711	15276
Mizoram	82112	14066	17130	18705
Sikkim	38468	23225	20029	65265
Nagaland	136529	27346	60375	17014
Tripura	339014	33038	9745	13064
NER	2690797	427027	13601	15877
All India	130881297	48032669	36,699	56,298

Source: RBI Statistical Return table 4.9, 22 July 2013

**TABLE 2.**

Annual Statement on Priority Sector Advances and Sectoral Deployment of Credit (2016)									
State	Total Priority Sector			Agriculture			Loans to Weaker Section (Priority Sector)		
	No. of A/cs	Balance O/s (Rs million)	O/s per A/c (Rs)	No. of A/cs	Balance O/s (Rs million)	O/s per A/c (Rs)	No. of A/cs	Balance O/s (Rs million)	O/s per A/c (Rs)
Arunachal Pradesh	26555	7774	292751	15551	1671	107453	24217	4735	195524
Assam	2299460	225378	98013	1606550	82591	51409	1932215	82746	42824
Manipur	65456	12141	185483	38828	3823	98460	48560	5063	104263

Meghalaya	104945	15808	150631	73978	4613	62356	99729	7066	70852
Mizoram	36748	8442	229727	20202	1422	70389	29467	3599	122137
Nagaland	56751	9095	160261	44299	3014	68038	51409	5473	106460
Tripura	467478	32437	69387	324407	12183	37555	422279	14555	34468
<b>NORTH EASTER N REGION</b>	<b>3057393</b>	<b>311074</b>	101745	<b>2123815</b>	<b>109318</b>	51472	<b>2607876</b>	<b>123238</b>	47256
<b>ALL INDIA</b>	<b>99552720</b>	<b>27514662</b>	<b>276383</b>	<b>69258672</b>	<b>1173098 2</b>	<b>169379</b>	<b>71783964</b>	<b>6999904</b>	<b>97513</b>
Source: Statistical Tables relating to Banking in India, <a href="https://dbie.rbi.org.in/DBIE/dbie.rbi?site=publications">https://dbie.rbi.org.in/DBIE/dbie.rbi?site=publications</a> , Accessed as on 13 Nov 2017									

An assessment of the microfinance activity in the region also shows a bleak performance as compared to the rest of the country. In 2016-17, the total loan disbursal to 28961 self help groups in the north eastern region was Rs 284.2 crores and in Arunachal Pradesh, credit of Rs 1.2 crores was disbursed to 102 SHGs. (NABARD 2017). So the average loan disbursal per SHG in the region was less than Rs 1 lakh as against the national average of Rs 2.04 lakhs. This also must be juxtaposed with the status of non performing assets (NPAs) on the loans sanctioned so far. As against a national NPA level of 6.5%, the NPA in NER was 20.64% and in Arunachal Pradesh it was 35.63%. (NABARD 2017) . Clearly the institution of self help groups is yet to take roots in this part of the country.

The RBI Committee on Financial Sector plan for the North Eastern Region gave its report in July 2006. It noted that “The banking outreach in the NER, particularly in the rural districts, is significantly low. Many outreach indicators for the region like average population covered per bank branch, deposit and credit growth, etc. are generally lower than the national average. The position is so on account of several impediments in penetration of banking/financial services in the region, which include difficult terrain, sparsely distributed population in hill regions, poor infrastructure, difficulties in obtaining land as collateral, insurgency/law and order problems, complicated systems/procedures of banks, shortage of suitably skilled staff, lack of awareness amongst large segments of the population about formal banking transactions and the general preference for grants rather than loans.”(RBI 2006).

#### 4. BANKING AND CREDIT PROFILE OF ARUNACHAL PRADESH

The report of the Lead Bank to the State Level Bankers Committee for the quarter ending March 2017 brings out the profile of banking and credit offtake in Arunachal Pradesh. A total of 26 scheduled commercial banks operate in the state, having 187 brick and mortar establishments, which makes it 1.35 branches per 10000 population. However the distribution of banks is very uneven and there is a large concentration in the urban and semi urban settlements. There are 79 branches in semi urban/urban areas and of the 108 rural branches, 47 are rural/cooperative bank branches and 45 of SBI. There are 155 Customer Service Points (CSPs) which supplement these brick and

mortar banks. However, even now there are 44 block headquarters across the state which neither have a bank nor a CSP, indicating a skewed concentration of branches. Across the state, over 2.1 lakh PMJDY accounts have been opened and RuPay cards have been issued to 1.69 lakh customers. On the whole, there are more than 13 lakh operative saving bank accounts in the state.

The state of lending in a state is captured in the Credit Deposit Ratio (CD Ratio). CD ratio of banks witnessed a decline from 36.4% in September 2016 to 30.13% in March 2017. This was sought to be explained by the fact that the banks receive a large number of government deposits in March end which presents a false picture of inflated deposits. Nonetheless, the CD ratio is well below the RBI minimum threshold of 60. A more detailed analysis reveals that CD ratio in respect of scheduled commercial banks is only 24.08%. A district wise analysis of CD ratio in the state also shows sharp variations : from a low of 8.04% in Tawang to a high of more than 46% in Kurung kumey and Kra Dadi districts and 47.86% in Lower Subansiri district. It would be instructive to study the reasons for such wide disparity.

Priority sector lending of scheduled commercial banks in the state was 31.26%, which was well below the minimum 40% norm. The gross NPA of banks in the priority sector was 23.51% but the NPA levels of the Arunachal Pradesh State Apex Cooperative bank was abnormally high at 59.62%. The priority sector advances of all banks in the last financial year were of Rs 201.14 crores. Within this the crop loan offtake was very low – only Rs 12.66 crores. There are 16175 Kisan Credit card holders who have a total outstanding amount of Rs 87.57 crores. In order to encourage farm loan, the government of Arunachal Pradesh has launched a new scheme : Chief Ministers Krishi Rinn Yojana under which the state would provide additional 4% interest subvention to be channelized through NABARD which would effectively bring down the interest rates to zero in case of timely repayment (since 3% subsidy is provided by Government of India). In 2016-17, Rs 30.98 lakhs loans were disbursed to 41 weaver credit card holders for their working capital requirement. A new scheme of providing interest subvention to weavers for their working capital loans has been launched by the state government which would give interest subsidy of 7% for working capital loan requirements of upto Rs 2 lakhs.

In the non priority sector, NPA of scheduled commercial banks was 1.5%, but even here the cooperative bank NPA level stands at 72.18%. For industry, new loans of Rs 16.12 crores were sanctioned last year. In the MSME sector, 1454 loans of Rs 146.48 crores were sanctioned. The MUDRA scheme has shown encouraging results in the state with a total of 6109 loans being sanctioned for a sum of Rs 81.46 crores.

In order to infuse a culture of entrepreneurship, the state government has launched the Deen Dayal Upadhyay Swalamban Yojana which provides a back ended 30% back ended capital subsidy for educated unemployed entrepreneurs who venture into four select areas: Eco tourism, agro processing, textiles and manufacturing.

## 5. BARRIERS TO INSTITUTIONAL CREDIT AND IMPLICATIONS FOR ECONOMIC DEVELOPMENT

There are several barriers for smooth credit offtake in Arunachal Pradesh, some of which are common to the North Eastern region, while others are peculiar to the state. Some of the key challenges for smooth credit flow are as under:

- a) **Lack of Land ownership documents.** Land ownership rights in Arunachal Pradesh are still governed by customary law and vest in tribal communities, clans, or individuals belonging to those communities. There is no codification of customary law in the state. While The Arunachal Pradesh (Land settlement and Records) Act 2000 and The Balipara/Sadiya/Tirap Jhum Land regulation 1947 acknowledge the ownership rights of the individual, in absence of cadastral survey, there is no formal conferment of ownership rights. The state has so far demonstrated ambivalence on conducting this exercise and individuals are only granted "Land Possession Certificates". From the standpoint of a financial institution, land ownership documents and mortgage of property serve as useful collaterals in case of defaults. The absence of formal ownership documents has also restricted the flow of private investment from outside the state, which in any case is limited on account of the Bengal Eastern Frontier Regulation, 1873 which bars any outsider from acquiring any interest in land unless so allowed by government.
- b) **Low Agricultural Credit offtake:** Most farmers in the state follow single cropping pattern which is confined to local consumption requirement. The banks view the viability of long term lending with skepticism in absence of market linkages and adequate surplus production for sale. The institutional credit flow to agriculture in Arunachal Pradesh remained almost same during the last three years and crop loan disbursement has declined substantially during this period. Without capital formation in agriculture, in which the role of institutional credit is of paramount importance, sustainable increase in production and productivity is not possible. (NABARD 2017).
- c) **Trade license:** For doing business in the state, an entrepreneur must have a valid trade license, which is issued only to local tribal people. In real terms, the local tribal citizen obtains a trade license for multiple business verticals and then on a power of attorney enters into an informal agreement with a non tribal person who becomes de facto owner of the establishment. This has several implications; One it creates a fuzzy framework of taxation liability and secondly from the standpoint of a lender for an SME enterprise, the banks view this arrangement negatively as it confuses the liability of repayment. The large NPA of cooperative bank in this segment could perhaps be an indication of this reality
- d) **Challenges of loan recovery:** The process of recovery under the Bengal Public Demand Recovery Act 1913 under which Bakijai Officers appointed by the state enforce action for recovery of defaulters. The number of Bakijai Officers in the state is limited and they in any case are burdened with additional responsibilities. In the quarter ending march 2017, there were 7128 Bakijai cases pending in the state. The other legal recourse for

recourse available to the banks is the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, which is a much quicker settlement and can be used for wilful defaulters, but for some inexplicable reasons has not been invoked in the state by the banks at all. Apart from this there is also the challenge of disposing the property through auction. By the very nature, tribal societies are closely knit and if a kin or a clan member purchases land of a brethren it is taken amiss.

- e) **Prevalence of Moneylenders:** There is a substantial informal credit market where lending is available at usurious rates and in absence of any regulatory check on moneylending in the state, people find it much easier to borrow informally even at much higher rates than the banks
- f) **Lack of adequate Financial literacy:** While there is a clear mandate to the banks from RBI to hold Financial literacy camps across the states at regular intervals, the banks mostly end up concentrating on district headquarters for such camps and the really deserving people end up being denied this right.
- g) **Limited bank penetration:** As has been pointed out earlier that the number of brick and mortar branches at the sub district level are few and banking correspondents don't inspire confidence amongst people for financial transactions.
- h) **Poor connectivity:** Arunachal Pradesh has huge challenges of road and digital connectivity. It also has the largest number of unelectrified villages in the country. This poses challenge to start formal banking operations and also inhibit technology driven net banking solutions which are dependent on robust data connectivity.

Absence of adequate credit poses huge challenges to the economic development of the state. Out of a total population of 13.1 lakh, nearly 1 lakh people are dependent on government employment. The work participation rate as per 2011 census was 42.47%. The number of people registered on the employment exchange rose rapidly from 39611 in 2013 to 64705 in 2016 as per data maintained by Directorate of Employment and Training, Itanagar. There is hardly any industrial activity in the state and the limited private investment has direct implications for the states fiscal position.

## 6. POLICY IMPLICATIONS

There are clear lessons from a pragmatic policy perspective which can be drawn from the above analysis.

- a) The first step is to create mass financial literacy. The Deputy Commissioners should spearhead the program along with NABARD and the Lead Bank for rolling out such programs at each block headquarter. This should be used as an enrollment drive as well as loan facilitation drive
- b) Establish CSPs in the shadow blocks of the state. The government can identify credible local people with a minimum cash turnover who can be provided some additional incentive to act as CSP
- c) Reform the land ownership Law and confer ownership rights. State wide cadastral survey may take time but the state can well begin a process for those people who for purposes of business or otherwise are interested to secure ownership rights by making appropriate payments. If it warrants change in regulatory regime, it may also be done.



- d) Government should appoint multiple Bakijai officers : at the block level and the provisions of the SARFESI Act should be invoked where warranted
- e) Certain select sectors where the state has a comparative advantage should be taken up as focus areas for credit facilitation and the state should seed entrepreneurs. Entrepreneurship development centres should be established at the regional level in partnership with Banks or NEDFI to provide handholding support to budding start ups for preparing bankable projects at limited cost.
- f) The regime of administering trade license must be made more transparent and the relationship between the actual proprietor and landowner be brought out clearly so that banks develop the confidence to lend
- g) A law banning Money lending on the lines of Bombay Money Lenders Act which has penal provisions
- h) Robust loan appraisal mechanism by the banks should be adopted and perhaps a monitoring mechanism in partnership with district administration for oversight of projects would be useful, especially given the remote geography of the state.

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