

[Financial inclusion]

Banking the rural poor

In the Indian State of Karnataka, public sector banks and various other government agencies are working on making financial services available in the villages. Progress has been made, but far too often farmers still depend on traditional moneylenders.

[By Laura Ceresna]

In the Indian State of Karnataka, 535 farmers have committed suicide from January 2008 to November 2009. Typically, they were suffering from overburdening debt to traditional moneylenders who demand exorbitant interest rates. India's formal banking system needs to reach out include farmers and provide an alternative to informal loan sharks.

The majority of Indians live in rural areas; most of them do not have access to regular banks. At the turn of the century, the Reserve Bank of India reckons, almost half of the urban population made use of bank services, but the share was below one third among rural people. Farmers are among the most disadvantaged groups in regard to financial exclusion. There is only one rural bank branch per every 18 villages. Just to visit a bank branch, villagers sometimes have to travel up to a day and bear transport costs as well as daily wage loss.

To improve matters, the National Bank for Agriculture and Rural Development (NABARD) initiated a programme to link banks to self-help groups as early as 1992. This programme is quite successful. By March 2008, NABARD was in touch with 3.4 million self-help groups and reached 55.5 million poor households. In Karnataka alone, NABARD set the goal of promoting another 30,000 self-help groups in the fiscal year 2008-2009. Moreover, income generation measures were included in the programme. Women are the main target group.

In 2005, the Indian government and the Reserve Bank of India started their own financial inclusion programme. The objective is to achieve 50 % inclusion by 2012 and 100 % inclusion by 2015. The idea is to expand low-cost access to no-frills bank services. A differential rate of interest was introduced, allowing banks to grant credit at 4 % interest to those who need it. The programme also involves strengthening rural cooperatives and restructuring regional rural banks.

At the state level, there is action too. Each of Karnataka's rural districts has appointed a "lead bank" to coordinate local banks and implement the financial inclusion programme. The lead banks have declared all districts of Karnataka to be 100 % financially inclusive. Such rhetoric is exaggerated, however.

Some banks work through business correspondents and local facilitators. Business partners such as NGOs or local government agencies like post offices, for instance, act as agents on behalf of banks. Using this model Syndicate Bank, the convenor of the Karnataka's state-level bankers' committee, opened 3 million zero-balance accounts in the course of two years. Modern technology is used, including portable terminals, mobile telephones, biometric fingerprint authentication and voice-guided transaction systems. Transactions are thus even possible in remote areas.

It is also important to educate the rural poor about the availability and functions of banking services and to encourage usage. The Government of Karnataka has introduced relief measures for districts with high debt burdens. It has also established centres for financial literacy, credit and farmer training. Farmers' clubs help by providing credit counselling and information on technology and production-enhancing skills.

Lasting challenges

Nonetheless, the rural people still struggle with many problems. That was the result of research done by the NGO Cividep in two rural districts of Karnataka. The majority of the farmers interviewed said they use formal-sector banks' services. Most had applied for agriculture loans. However, they complained that banks did not respond

to other urgent credit needs, for instance, in cases of medical emergencies or major family events like weddings or funerals. Therefore, many farmers were still turning to traditional moneylenders. Other reasons for doing so included

- geographical disadvantages,
- existing debt to moneylenders,
- the lack of knowledge about loan procedures and
- difficulties of documentation.

In Karnataka, traditional moneylenders charge interest rates of around three percent per month. That adds up to more than 40 % per year. Such loans are hard to service and pay back, and indeed, many farmers are unable to do so. Crop failures are major business disasters for farmers who lack insurance coverage. Farmers who default on bank loans are not eligible for new ones, thereby forcing them to seek non-institutional credit sources.

Moneylenders who are not repaid exert massive pressure, sometimes threatening the lives of farmers and their families. On the other hand, the social stigma attached to defaulting on loans is taxing, with farmers mentioning low self-esteem and mental stress as a consequence. These are the reasons for most suicides among Indian farmers.

Financial inclusion in rural Karnataka is no mission accomplished. To improve matters, governmental and non-state actors must cooperate. Farmers' access to banks must go beyond agricultural credit. Public-sector banks must become more reliable and deliver services faster than in the past. In Karnataka, only one private-sector bank was offering services to the rural poor in 2009. Most private-sector banks shy from becoming active in the villages because of low profitability. The NABARD approach of cooperating closely with self-help groups is commendable and should be copied by others.

In the past, various Indian governments have forgiven outstanding debt to public-sector banks. That policy was destructive because it undermined people's willingness to repay the money public-sector banks had lent them. What is needed, however, is a

debt-swap system that would enable farmers to escape their dependence on traditional moneylenders.

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