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Marketing of Financial Services in Rural Sector : A Study of Public and Private Banks

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INTRODUCTION

Rural development occupies a significant place in the overall economic development of the country. Since independence, it has been constant endeavor of our policy-makers to give adequate thrust to rural development as the sector is directly related to agriculture. Rural banking in India started since the establishment of banking sector in India. Rural banks in those days mainly focused upon the agro-sector. Regional rural banks in India penetrated every corner of the country and extended a helping hand in the growth process of the country.

India's rural poor are overwhelmingly dependent on agriculture as their primary source of income; the majority is marginal or small farmers, and the poor house holds are landless. The financial needs of India's rural poor reflect the volatile, uncertain, and irregular income streams and expenditure patterns of these households. The recently completed World Bank NCAER Rural Finance Access Survey of 2003 (henceforth referred to as RFAS 2003) indicates that while rural families are predominantly multiple-income households, their two main sources of income include the sale of agricultural products and wage labor. Irregular employment is the most important source of income from wage labor. For households with more than one source of income, agricultural income is the most important secondary source, with sales of farm produce and dairy products being the most prominent. Clearly, rural households depend on one or both of two types of income : seasonal (post-harvest sale) or highly irregular, due to irregular or part-time wage labor, with the dependence on the latter being inversely proportional to the size of land holdings. The typical expenditure profile of the households is also of small, daily, or irregular expenses incurred throughout the month.

Moreover, the overwhelming majority of rural households report having to deal with at least one unusual expense each year, which they are forced to finance either from cash at home or through informal loans from family, friends, or moneylenders. Research shows that poor people value financial services and want these to be reliable, convenient, continuous, and flexible. They understand that financial services help them spend at one time the income they have earned at other times. And because those incomes tend to be small, irregular, and unreliable, they need the full armory of intermediating modes — saving up for future spending, taking advances against future savings, and building cash reserves that can be called on at any time. The poor need a wide range of financial services — from small advances to tide over consumption needs to loans for investment purposes to long-term savings that help them manage life-cycle needs.

RURAL FINANCE SERVICE PROVIDERS

India has a range of rural financial service providers, including formal sector financial institutions at one end of the spectrum, informal providers (mostly moneylenders) at the other end, and between these two extremes a number of semi-formal/microfinance providers. In terms of their sheer size and spread of operations, formal-sector financial institutions dominate the rural finance landscape: Commercial banks, mostly public sector banks (but also some private sector banks) and regional rural banks (RRBs) together have more than 32,000 rural branches. India also has a vast network of rural cooperative banks, with a three-tiered structure at the state, district, and village levels. There are some 14,000 branches of rural cooperative banks and more than 98,000 grassroot retail outlets of Primary Agricultural Credit Societies (PACS), which are used by the cooperative system as channels for fund flows. The post office system adds to the physical service point network of the country with more than 154,000 post office branches handling more than 110 million money orders and administering 114 million savings accounts Formal financial institutions are regulated by the Reserve Bank of India (RBI), although it has delegated the task of supervising rural cooperative banks and RRBs to the National Bank for Agriculture and Rural Development (NABARD). 14 Development Banks such as NABARD and the Small Industries Development Bank of India (SIDBI) provide support to both formal and semi-formal segments through funding refinancing arrangements. NABARD provides refinancing to banks' lending in rural areas and SIDBI funds and supports MFIs.

THE SEMI-FORMAL/MICROFINANCE SECTOR

While India is home to many microfinance innovations in terms of people reached and the scale of financing, microfinance in India is still a drop in the ocean. It reaches between 5 and 6 percent of the country's poor rural households, or about 30 percent of the rural poor, either directly or indirectly. Dominant among the microfinance models is Self-Help Group (SHG) – Bank Linkage, whereby women's SHGs are linked to the rural branches of commercial banks, RRBs, or cooperative banks, which often benefit from refinancing by NABARD. SHG-Bank Linkage has reached out to around 12 million family's interns of savings accounts. Credit outstanding remains low; disbursements in FY 2002–03 accounted for only 2 percent of the formal-sector credit outstanding in rural areas. The other model is specialized Microfinance Institutions (MFIs), which reach around 1 million clients. The total branches of MFIs are estimated to be in the range of a few thousand, compared to the vast numbers of bank branches. Recent developments have led to other inter-linkages between the formal both public and private sector banks and semi-formal sector initiatives, particularly in the context of SHG–Bank Linkage, as well as through lending by SIDBI and commercial banks to MFIs. Moreover, a few private-sector commercial banks, such as ICICI Bank, have tried innovative ways of incorporating lessons from microfinance into their operations, and have made inroads in using microfinance methodologies to deliver rural financial services. Informal providers, informal financiers include a range of actors-landlords, local shopkeepers, traders, professional moneylenders, etc. While there are no definite estimates of the number of informal-sector providers, these are spread very widely across the country. Survey data indicates that poor rural households rely heavily on informal finance to meet a range of financing needs: from consumption and emergency financing to investment loans.

REVIEW OF LITERATURE

RRBs, though operate with a rural focus, are primarily scheduled commercial banks with a commercial orientation. Beginning with the seminal contribution of Haslem (1968), the literature probing into factors influencing performance of banks recognizes two broad sets of factors, *i.e.*, internal factors and factors external to the bank. The internal determinants originate from the balance sheets and/or profit and loss accounts of the bank concerned and are often termed as micro or bank-specific determinants of profitability. The external determinants are systemic forces that reflect the economic environment which conditions the operation and performance of financial institutions. A number of explanatory variables have been suggested in the literature for both the internal and external determinants. The typical internal determinants employed are variables, such as, size and capital (Akhavein *et al.* (1997)) The literature on RRBs recognizes a host of reasons responsible for their poor financial health. According to the Narasimham Committee, RRBs have low earning capacity. They have not been able to earn much profit in view of their policy of restricting their operations to target groups. The recovery position of RRBs is not satisfactory. There are a large number of defaulters. Their cost of operation has been high on account of the increase in the salary scales of the employees in line with the salary structure of the employees of commercial banks. In most cases, these banks followed the same methods of operation and procedures as followed by commercial banks. Therefore, these procedures have not found favour with the rural masses. In many cases, banks have not been located at the right place. For instance, the sponsoring banks are also running their branches in the same areas where RRBs are operating. The issue, whether location matters for the performance, has been addressed in some detail by Malhotra (2002). Considering 22 different parameters that impact on the functioning of RRBs for the year 2000, Malhotra asserts that geographical location of RRBs is not the limiting factor for their performance. He further finds that it is the specific nourishment which each RRB receives from its sponsor bank, is cardinal to its performance. In other words, the umbilical cord had its effect on the performance of RRBs.

One of the prime arguments for the poor performance of the predominant small-holders in Africa is the inaccessibility to financial services (Collins *et al.,* 2009). This being the case (and as agriculture employs majority of people in developing economies), financial services provision to small-holders in most African countries attracted the attention of governments, researchers and development partners (Bikker and Haaf, 2002; Chen, 2009). For example, in efforts to deepen and widen provision of financial services to the wider community of Anzanians (majority of who are rural poor employed in Agriculture), the Government of Anzania has made important improvements in reforming its financial sector, dismantling the state-dominated banking and financial sector and allowing foreign investments (Simpasa, 2011; Cull and Spreng, 2011). Despite all this, the financial services provision to the poor rural farmers suffers a perceptual and condition mismatch between service renders (financial institutions) and the beneficiaries (small-holder farmers). To remedy the afore-mentioned mismatch, a number of individual and joint efforts of financial institutions, governments and private sector are put in place. One such effort includes the provision of innovative financial service to small-holders for agri-business growth (Abbas and Sobolev, 2008). The assumption with this tendency has usually been that innovative provision of financial services to rural small-holders improves their productivity and supports commercialization of agri-businesses (Yumkella *et al.,* 2011). Proponents of the Assumption (Bilton and Cummings, 2010; Edwards *et al.,* 2005) indicate that provision of innovative financial services in combination with other supportive aids to the rural farmers in developing countries enhances commercialization, growth and development of small-holders. Specially, Abbas and Sobolev, (2008); Bilton and Cummings (2010) emphasize the need for innovativeness in articulating financial services and modes of providing them to small-holder agriculturalists. According to Temu (2009), well-articulated rural financial services to small-holders and innovative financial mechanisms provide growth support to agricultural producers and value chains in which they operate. It is through innovation that we see new ways of doing things, better agri-business project operations, new success stories and overall growth and development both economic and social (Sorensen *et al.*, 2010; Sorensen, 2003). The concept of innovation has witnessed resurgence in the literature in recent years. It is one of the concepts that are widely defined and applied in different disciplines. According to Lundvall *et al.,* (2003), innovation is the creation, diffusion and use of new ideas applied in the economy. The application may take a form of production processes, new products, new forms of organization and new markets (Hotho and Champion 2011). In the case of this study, innovation can refer to new products, new markets and marketing techniques and/or new organizational or managerial structures (Mazzarol and Rebould, 2008). It is the key to sustenance and growth which, according to Temu *et al.*, (2011) has to happen at all levels of individual, organization, society and country if the community is to realize positive transformation. As demonstrated by Hotho and Champion (2011), innovation is a process - not a One-Time-Action. To innovate, organizations need operational models that don't constrain information flow but open space for information flow leading to learning and improvement.

FINANCIAL SERVICES IN RURAL MARKETS

Financial services are a form of services that provide solution to the financial needs of consumers. They are of various types like banking, insurance, mutual funds, securities financial transaction service etc. Provision of quality access to financial solutions is vital for development of people in rural areas. Low

–income households and micro enterprises can be extremely benefited from bank credit, savings, securities, mutual funds and insurance services. Investing in securities generates regular cash flow and also gives capital appreciation. Banking services enable people to take advantage of profitable business opportunities and increase their earnings potential. Insurance services can help all the stake-holders to manage the associated risk with life, business and agriculture. Attitude of rural people towards use of money and saving has changed after nineties. The age-old practice of keeping the savings in the form of cash or gold has given way to preference for bank accounts, mutual funds, securities and insurance. Recently self-help group concept has got tremendous success in rural areas. This study concentrates on rural insurance.

Chakravarthi (2006) reported that health insurance schemes are more complex and because of various demand and supply side-imperfections, there are inherent problems in the health insurance market. He also says that most of the perspective population is unaware of the pros and cons of the different schemes of health insurance.

Ratna and Sarkar (2007) reported that rural population treat health as an important aspect and are interested in a health insurance scheme. They reported that high costs of hospitalization and surgery is not posing financial risks for poor households. They also reported that poor rural people are able to take judicious decisions regarding the composition of a health insurance benefit packages.

Naveen and Veerashekhrappa (2009) reported that Micro-insurance is entirely a new financial product for the rural poor in the study villages. All respondents heard about the micro health insurance for the first time through the SHGs and the NGO staff. They say that large numbers of the SHG members cover their health insurance through micro-health insurance program. They also reported that the accessibility of micro health insurance is more skewed towards the income group of very poor and moderately poor households.

Vinod and Saharan (2007) reported that general public is slowly becoming aware about the benefits of the health insurance and its importance in today's world. They say that the premium level and index of growth of health insurance business is continuously rising up in India. They also reported that public sector players are declining with their market-share in health portfolio whereas the private sector players are on the rise in their contribution level.

Charkravarti (2006) reported that below-poverty-line population is not capable of paying health insurance premium and the insurance agents are not properly informed about the policy. He says that general public takes financial help from the neighbours/community to bear the financial burden of medical expenses. He reports that a large section of the rural poor in West Bengal simply avoid health implications due to their poverty; as they are unable to bear the cost of treatment.

The rural banking system in India has an essential role in the rural development of the country. Beginning with co-operative credit structure followed by rural branches of commercial banks and then RRBs, the institution structure has grown and expanded during the last three to four decades. In spite of these expansion programmers, a large segment of rural economy is still beyond the reach. The success of any bank depends on the facility what they provide to their customers.

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