



FINANCIAL INCLUSION FOR INTEGRATED DEVELOPMENT

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'Freedom has a thousand charms to show,
That slaves, howe'er contented, never know'
- *William Cowper (1731-1800)*

Introduction

In a world recovering from one of the history's darkest recessions and in a country freed from the clutches of terrorism, thousands of people are yet to know the 'charms of freedom'. They are not technically slaves, but they are denied elementary freedom and remain imprisoned in one way or the other by economic poverty and social exclusion. They are tied down by economic manacles. The main purpose of development should be to spread the freedom and its 'thousand charms' to the unfree segments of society; or more specifically, development should result in individual freedom and general welfare to the extent that our collective economic wealth positively and absolutely correlates with individual freedom.

Poverty, according to the Indian Nobel laureate Amartya Sen, is 'the deprivation of basic capabilities rather than merely lowness of income' and what is implied by Sen is that poverty is the outcome of disparity in wealth distribution. The 'basic capabilities' referred to by Sen include social infrastructure, access to health, education, water, roads, banking, establishment of industries, employment opportunities, social inclusion and many more factors, the totality of which form the integrated development of a country. A major issue in poverty is the lack of access to financial markets and limited or no access to financial instruments like savings, credit, insurance, education loans, etc. and financial inclusion serves as a driver of economic growth and poverty alleviation as it seeks to make financial services accessible to the un-banked and the under-banked on a meaningful and sustained basis.

Despite the established relationship between financial inclusion and integrated development, their causality is arguable. Financial inclusion forms an integral part or an antecedent of integrated development through alleviation of poverty, which is one of the primary development objectives. However, one may also argue that financial inclusion is a consequent of development rather than an antecedent, in the sense that financial inclusion would be possible only in the presence of 'basic capabilities' as Amartya Sen points out. People can be persuaded into engagement with formal banking only if they have certain social conditions in place such as social infrastructure, access to health, education, water, roads, employment opportunities etc. In either case, the fact



that needs to be emphasized is the need for achieving 100% financial inclusion aligned with the development activities of the country.

The objective of this article is to discuss the need for adopting an integrated approach towards development and the importance of financial inclusion of the un-banked and the under-banked segments in society in this endeavour in bringing about a poverty-free Sri Lanka.

Why Integrated Development?

The integrated strategic development approach is predicated on the assumption that certain sectors can play the lead role in the development process. According to theoretical principles, lead sectors are those which exert the greatest influence on growth in other secondary areas of the economy such as infrastructure, IT, education, agriculture and food processing and financial services. The greater the degree of integration between lead sectors and other primary economic areas, the larger will be the multiplier effect.

There are four areas that we need to focus on as the primary development objectives as being most relevant for attaining the integrated development consistent with sustainable output and export growth:

- Increased domestic production
- Employment maximization
- Poverty reduction
- Productivity enhancement

The achievement of those objectives will undoubtedly impact all citizens and will result in a more prosperous and peaceable nation. It is required to put best efforts in pursuit of the optimal development policies and strategic interventions that can be implemented for the realization of those objectives. It is essential that the private sector must also play a profound role in the integrated development process.

It is my view that in the present dynamic economic environment nothing less than an integrated development planning approach will produce the desired results. Such an approach is mandated by the comprehensive scope of economic and social parameters required to produce the desired changes. It is also essential for ensuring effective distribution of development benefits among the people from the top to the bottom of the pyramid.

Need for Sustainable Integrated Economic Development

The introduction of the integrated development strategy must be effected over time and on the basis of sound analysis. There are four fundamental guiding principles that permeate sustainable economic development.



- **Competitiveness:** It is clear that competitiveness is a fundamental component of sustainable development. All businesses – not just those involved in manufacturing – are threatened by sweeping regional and global changes.
- **Innovation:** it is essential that we recognize the imminent economic ascendancy of knowledge-intensive industries and the crucial importance of innovation as a process affecting almost all areas of economic activity. The businesses, communities and individuals need to adapt to and exploit the advantages of a knowledge-based society.
- **Focused Action:** Given inevitable constraints on finances and time resources there is a need for a pragmatic approach to implementation, implying a need for hard choices about priorities and what should be tackled first. There is, therefore, a need for focused action. It is also acknowledged, however, that implementation must be flexible; circumstances can change, and the strategy must be responsive to events and unexpected challenges and opportunities.
- **Partnership:** Partners recognize that much more can be achieved by adopting a joint, collaborative approach to addressing socio-economic needs and realizing opportunities.

These general principles are relevant to any country that seeks to promote sustainable economic development; however, as far as formulating and implementing integrated development strategies are concerned, Sri Lanka being a country emerging from decades long civil conflict, needs to carry out an in-depth analysis of its current position and future prospects.

Integrated Development in the context of Sri Lanka

Analysis of the country's current position and expected future trends indicates that there are a number of key developmental themes confronting Sri Lanka that together must inform future actions and priorities in implementing integrated development, such as,

- To generate additional high-value business activity in the country, and in particular to develop higher value service sector activity through FDI, greater exploitation of the country's knowledge assets, and by encouraging local entrepreneurship and business transformation.
- To enable local people to capture more fully existing and emerging employment opportunities, by providing improved access to skills development and training opportunities, and thereby helping to create a more flexible and productive workforce.
- To radically improve the image and appeal of the conurbation by maximizing the contribution of commercial functions, especially retailing, leisure, entertainment and cultural activities and attractions.



- To create more responsive and productive business infrastructure and to realize development opportunities and environmental enhancements available in both the urban centres and gateway areas of the country.

Having realized the challenges ahead Sri Lanka in implementing integrated development, needs to formulate growth strategies and prioritize strategic actions. Well thought-out short-term and long-term planning in view of the possible threats and opportunities will ensure successful implementation of sustainable integrated development.

What should be done?

Consistent with the view that Sri Lanka must give priority to dealing with its internal development constraints, certain issues need to be recognized as the principal challenges that must be confronted in the pursuit of sustainable integrated development. They are the rigidities in the structure of the economy that affect business growth and international competitiveness, weaknesses and/or inadequacies in the national institutional framework, including areas such as economic management, strategic planning and information management and the generally unproductive social attitudes, poor work ethic and moral values.

In addition, it is of paramount importance that in order to achieve short term development, we must examine glaring concerns not addressed by the existing development programmes and policies and provide practical and sound recommendations where prevailing strategies appear to fall short of achieving desired results. For example, strategic actions need to be focused on six primary sectors of the economy, namely Tourism, Agriculture, Fisheries, Manufacturing and Export, Information Communication Technology and Cultural Industries.

The following measures are presented as the most relevant actions that should immediately be initiated in order to stimulate growth and stability of output.

- Undertake a comprehensive revision and harmonization of all business incentives, programmes and schemes to focus on the achievement of specific development objectives. The incentives revision should cover all sectors of the economy and take account of the production and export of both goods and services.
- Prepare and adopt an integrated export development strategy that would effectively integrate trade and investment promotion and enhance international competitiveness in the evolving regional and international trade regimes (WTO, SAFTA, CEPA etc.)
- Place greater emphasis on economic projects that are directly income generating.
- Align education curricula to focus on national economic and social goals and introducing Entrepreneurial and Self-Sufficiency Training throughout the school system.



- Spearhead programmes to develop value added agri-products and agro-linkages
- Develop cottage industries for export/import substitution with targeted incentives (especially in non-traditional areas such as culture and services).
- Introduce ICT in areas that improve human performance, reduce time and save cost with instant reporting and communications, access to relevant databases where currently deficient.

It is essential that priority be given to implementation of above suggestions and where feasible, donor support and financing should be sought from relevant agencies, including the private sector for the implementation of those initiatives.

In addition to the priority actions indicated above, it is also important to focus on short term growth strategies and actions most pertinent to the role and function of the private sector. It is essential that the private sector spearheads the implementation of these initiatives and contributes to their financing.

Challenges of Integrated Development

Without exception, these consultations confirm the existence of numerous reports and recommendations relating to most sectors of the economy that are still awaiting further analysis, rationalization and prioritization. At the same time, there also appears to be a lack of information regarding existing sector policies, incentives and initiatives. This suggests a general laxity on the part of people to acquaint themselves with existing information and reports. As a result, most economic agents are ill-equipped to deal with the challenges of development, and the institutional infrastructure needed to create and support economic transformation remains weak and incapable of delivering desired growth rates. In the interim, the critical objective in the short term needs to be to achieve an increase in the rate of economic growth.

The measures for increased economic growth are relying on three strategic areas:

- Private Sector: Private Sector development expands production of goods and services and increases employment
- Public Sector: Restructuring of Public Sector enhances its effectiveness in supporting private sector activities and reducing cost of government.
- Labour Efficiency and Productivity: Increased efficiency and international competitiveness in all segments of the economy

Private Sector development - Growth and development are driven as much by public sector action as by private sector response to commercial opportunities that government policy serves to create. In illustrating this point, the World Bank in its Development Report says, '*Private*



firms are at the heart of the development process. Driven by the quest for profits, firms of all types - from farmers and micro-entrepreneurs to local manufacturing companies and multinational enterprises - invest in new ideas and new facilities that strengthen the foundation of economic growth and prosperity'.

In the current international economic context both large and small businesses need to restructure and become more aggressive about their own future if they are to successfully contend in the fierce international competitive environment. A process of re-education would serve consumers and entrepreneurs alike to assist them in acquiring the aggressive perspective towards excellence and productivity that are essential for success.

Joint venturing, equity pooling and other alternatives to traditional debt financing need to be adopted as part of the growth strategy and business must become adept in the employment of those mechanisms. To the extent that development strategies in the other primary economic areas stimulate and or strengthen private sector development, there would be a direct positive impact on the overall development goals and international competitiveness.

In an evolving international trade environment characterized by rapidly expanding trade in services and rigidly standardized goods trade, international competitiveness is increasingly determined by the quality of the national trade support network and production efficiencies. The latter hinges on supply side concerns such as technological innovation, productivity enhancement and cost of factor inputs, utilities etc.

It must be noted that there will be occasions where investment opportunities will materialize, which our private companies will not have the capacity to engage. Government will therefore be required to support such initiatives.

Public Sector Reforms - In a small country like ours, the government is expected to exert significant influence on the economy both as a primary producer, consumer and facilitator of the development efforts of other economic agents. The government's roles in those areas are indeed the tripod upon which the economy rests. The private sector may well be the engine of growth but the public sector is most definitely the fuel that makes the engine go. We may well extend the analogy to say that the pace at which the engine goes may be a reflection of the quality of the fuel that is injected.

Reform of the public sector will impact the development process across the board and given the current state of public affairs, this constitutes an essential criterion for economic advancement. Consequently, the public sector reform process needs to achieve targeted objectives that in turn conform to the national development vision and goals; specifically increasing productivity and output.



Productivity Management - The objective of increasing the rate of economic growth implies the expansion in the quantity and quality of the goods and services produced by domestic economic agents. Unfortunately entrenched in the social and cultural norms of the country are many practices and attitudes that impede maximum efficiency and productivity in a commercial production setting. These practices and attitudes have persisted throughout the decades and today pose a severe threat to the economic survival of the nation. Some of the more obvious reflections of these negative practices are observed in the general poor output and service quality in the major economic sectors, the limited daily hours worked in some sectors such as agriculture, and the disproportional wage rates among different sectors for comparable work. Clearly potential benefits of the available development opportunities and the current capacity for undertaking these development pursuits cannot be harnessed unless there is a profound adjustment in work ethics and output. Essentially any measure that is introduced in the primary economic areas that results in increased productivity will automatically impact the national development goals and should produce a positive demonstration effect in other economic areas.

It is my strong opinion that the quality of the education imparted to individuals during the formative years within the formal education system is of primary importance and determines their productivity or usefulness in the advancement of the country's goals. The education reforms must consequently be viewed as an essential component of productivity enhancement and public sector reforms and the education system must be refocused to ensure that individuals since their formative years are knowledgeable about the country's development goals and that they have the requisite skills to effectively participate in the development process and to perpetuate sound social values (that are reinforced at all levels of the system). It is commendable that the government is promoting skill-based, professional education and educating the masses about the country's development goals and equipping them with the required skills to actively participate in the economy.

Integrated development is a challenging but amply rewarding project which requires the complete involvement and engagement of both the public and private sector in integrating the lead sectors with the secondary and other primary economic activities to develop the country in terms of increased production, maximized employment, reduced poverty and enhanced productivity.

The Role of Banking in Integrated Development

If the banking system of a country is effective, efficient and disciplined, it brings about a rapid growth in the various sectors of the economy through activities like promoting capital formation, investing in new enterprises, promoting trade and industry, developing agriculture, balancing regional development, influencing economic activity by its influence on credit creation and interest rates and implementing monetary policy.

From an individual, social point of view, banks have to play the role of a responsible partner in the community. Banks are expected to facilitate social entrepreneurs among community groups as well as with small businesses and help create conditions that are essential for participation



of individuals in financial activities in a bid to financially empower them and reduce poverty. In this context, financial inclusion, which is an essential driver of economic growth, is a prime responsibility of banks of developing and transition economies like Sri Lanka.

Financial Inclusion and Integrated Development

'People were poor not because they were stupid or lazy. They worked all day long, doing complex physical tasks. They were poor because the financial institutions in the country did not help them widen their economic base', says Muhammad Yunus, Bangladeshi Nobel laureate & founder of Grameen Bank. As Muhammad Yunus correctly points out, poverty is not an individual condition; it is a social condition, a social exclusion imposed upon people by society and financial exclusion forms a major part of it.

The poor can be empowered by financial inclusion, i.e. giving them the initiative and encouraging them to participate in the financial system of the country. The banking sector can play a critical role in this regard. If economic development should ultimately result in individual freedom, the contribution of the Banking sector to economic development will not be complete unless and until they empower the bottom of the pyramid through financial inclusion.

Financial inclusion has been defined as 'the provision of access to appropriate, convenient, usable, valuable and affordable financial services and products to the widest part of the population, especially through the delivery of basic banking services to the low income people and the still unbanked, as a way out of poverty' (*WSBI Santiago Declaration 2009*). As per the definition, the products and services offered under financial inclusion should fulfill a number of requirements that fall into three dimensions: the geographical dimension, by providing financial products to underserved population in rural and remote areas; the product dimension, by offering accessible and affordable services, adapted to the specific needs of low income population and the time dimension, by maintaining a more permanent relationship with clients and following more stable policies in the good and bad times.

Financial inclusion is considered a top priority by the United Nations, which has identified the following as the main goals of Inclusive Finance:

1. Access at a reasonable cost of all households and enterprises to the range of financial services for which they are 'bankable', including savings, short and long-term credit, leasing and factoring, mortgages, insurance, pensions, payments, local money transfers and international remittances.
2. Sound institutions, guided by appropriate internal management systems, industry performance standards, and performance monitoring by the market, as well as by sound prudential regulation where required.
3. Financial and institutional sustainability as a means of providing access to financial services over time.



4. Multiple providers of financial services, wherever feasible, so as to bring cost-effective and a wide variety of alternatives to customers (which could include any number of combinations of sound private, non-profit and public providers).

World Savings Bank Institute (WSBI), a body that actively promotes financial inclusion, in its Survey on Financial Inclusion of WSBI member countries in March 2011, identifies four practices upon which financial inclusion is built.

- The promotion of accessible, small-scale and basic services
- The continuing construction of a large distribution network
- The strengthening of the social and welfare investment activities in their communities
- The recognition of the importance of financial education.

Exhibit 1: Poverty and Financial Inclusion: South Asia

Country	Population below Poverty Line (%)	Gross Domestic Savings (% of GDP)	Access to Finance Ratio (Hanohan Index) (%)
Bangladesh	81.3	20.1	32
Bhutan	49.5	n/d	16
India	75.6	30.4	48
Nepal	77.6	9.7	20
Pakistan	60.3	11.4	12
Sri Lanka	39.7	18	59

Sources: *WSBI Perspectives 62 (March 2011)*,

ADB Key Indicators for Asia and the Pacific (2010)

Note: *Afghanistan and Maldives have not been included in both Reports.*

Causes of Financial Exclusion

There are several reasons for financial exclusion mainly categorized as supply-side factors and demand-side factors. Supply side factors are the lack of physical and social infrastructure, establishment of industries, employment opportunities etc. In remote hilly, desert and sparsely populated areas the physical and communication infrastructure are insufficient. As a result access to financial services/institutions is severely restricted. This is further aggravated by long distance of branch from the residence, un-adjustable timings of the branch, complicated procedure and intricacies of documentation, unfamiliar language and unsuitable products. Another huge challenge is changing the mindset of the people (staff) who are working at the field level on how to treat these people (those without any bank account), how to make them understand that these people are bankable, they are profitable ultimately for the bank as a business. The requirements of documentary proof of identity and residential address are the biggest barriers in opening not only



bank accounts but also for availing of the financial services. Even an account holder in the bank cannot borrow if he or she fails to mobilize a guarantor.

On the demand-side, the barriers are illiteracy, lack of awareness and financial literacy, low income, pre-owned collateral/assets and social exclusion. Unless and until the financially-excluded people understand (and experience) the need for and the benefits of inclusion in the financial system, they would not be motivated to connect with banks. Financial literacy will serve to change their attitude towards banks and also to remain in the banking system on a sustained basis. All in all, in order to implement financial inclusion, we need to arrest both supply-side and demand-side barriers.

Financial Inclusion and Banking Sector

‘When we want to help the poor, we usually offer them charity. Most often we use charity to avoid recognizing the problem and finding the solution for it. Charity becomes a way to shrug off our responsibility. But charity is no solution to poverty. Charity only perpetuates poverty by taking the initiative away from the poor. Charity allows us to go ahead with our own lives without worrying about the lives of the poor. Charity appeases our consciences.’ - M u h a m m a d Yunus

Yunus is essentially highlighting the difference between CSR and sustainable financial inclusion. Financial inclusion, for banks, has become one of the underlying principles of their business activities. Access to finance is an essential driver of economic growth in developing and transition economies. It is also important in developed economies, where it stimulates the social inclusion of certain groups of the population. Access to finance empowers people, gives them the opportunity to have an account, to save and invest, to insure their homes or to take a loan and – in many cases – to break the chains of poverty.

Financial inclusion or in other words, bigger and deeper banking systems go hand in hand with more advanced economic development. The purest purpose of money – in particular in a dematerialized form – is to serve as a more efficient means of exchange than do barter and counter-trade. The purpose of bank based money as opposed to pure cash is two-fold. First, it is a better store of value. Second, it allows economies to gear up their working capital (savings) to form also a platform for long-term capital (investment) through the maturity transformation process that only banks can effectively make. Obviously money, and more particularly bank-based money, can only provide these advantages when the transaction costs of operating a bank account are below the inefficiency costs (and middle-man’s margin) of managing barter and counter-trade. All this is particularly crucial in poorer developing countries, where evidence (quote the source) shows that availability of credit does increase economic activity but to become financially self-sustaining, this has to be augmented by small scale savings mobilization.



Pitfalls of Financial Inclusion

Financial inclusion comes with potential dangers. Recent experiences all around the world show that poor people take loans that they have no capacity to service. Farmers have also taken loans that they have not been able to repay. Recent history tells many incidents where many farmers have been driven to suicide because of debt problems. Unless financial literacy goes hand in hand with financial inclusion, there could be dangers ahead. At a global level, the U.S. mortgage crisis showed how banks did not have a control over poorly educated consumers taking loans, and agents offering the loans etc. Financial inclusion therefore should necessarily be accompanied with financial literacy and financial discipline.

The biggest pitfall of financial inclusion is taking the concept in isolation. It comes as a holistic package and unless there is all other kinds of inclusion, merely enabling somebody to open an account or giving little bit of access to loans is not really going to solve the problem of financial exclusion. Survey around the world has shown that most of such accounts could become inoperative after sometime due to various reasons such as lack of regular income or irregular collection by the bank in the event of lack of a branch in the particular area. Similarly, granting loans to the poor who may fail to service the loans due to the incompatibility of their income and consumption patterns with regular loan repayment is not financial inclusion. Various red-tapes in opening accounts like documentation and granting loans like guarantors or security and staff that do not have the correct attitude or disposition towards the poor are barriers to financial inclusion. In short, sustainability and empathy need to be embedded in every aspect of financial inclusion.

On the other hand, while initiatives like creating no-frills accounts, facilitating or easing the KYC norms are implemented to help the unbanked-underprivileged people to access the banking system, a conducive environment should be created for these people to remain in the banking system on a sustained basis. That requires social infrastructure, access to health, education, water, roads and establishment of industries etc. If we talk of financial inclusion in isolation we will really miss the larger picture and lose the sole purpose of financial inclusion.

Sri Lanka's Status of Financial Inclusion

Sri Lanka's Access to Finance ratio, according to *Honohan Index* (2010) developed by WSBI (Exhibit 1), is 59% which is the highest in South Asia while the population living below the Poverty Line is the lowest at 39.7%. However, India, whose population below the Poverty Line (75.6%) is almost twice as Sri Lanka's, has achieved 48% Access to Finance ratio, which is only 8% decrease from Sri Lanka's ratio. As per the ratio India is well ahead of Sri Lanka in implementing financial inclusion, a fact further substantiated by India's Domestic Savings Ratio of 30.4% which is almost twice as that of Sri Lanka (18%). It should also be noted that Singapore, ranking high in Asia, has set a regional benchmark in financial inclusion by achieving 98% Access to Finance ratio.



**Exhibit 2: A Comparative Analysis of Access to Finance:
South Asia vs. Singapore & Malaysia
(i) Commercial Banks**

Country	Deposits			Loans			Outreach
	Accounts per 1,000 Adults	Value (% of GDP)	Average Account Value (% of Income Per Capita)	Accounts per 1,000 Adults	Value (% of GDP)	Average Account Value (% of Income GDP)	Bank Branches per 100,000 adults
Afghanistan	83.85	25.90	n/d	3.32	7.79	n/d	2.00
Bangladesh	316.67	50.04	232.52	41.37	36.88	1,311.74	5.16
India	747.29	55.03	107.86	137.46	40.93	436.09	10.11
Nepal	n/d	57.62	n/d	n/d	40.70	n/d	4.19
Pakistan	229.49	29.72	206.50	37.67	21.67	996.76	8.68
Sri Lanka	1,891.74	39.52	27.58	n/d	29.86	n/d	9.50
Singapore	2,236.25	280.88	151.53	914.55	213.43	281.55	11.44
Malaysia	2,063.33	105.45	72.96	963.6	113.16	167.64	10.54

Source: CGAP-World Bank Report 2010

Note: Bhutan and Maldives have not been included in the Survey.

(ii) Specialized State Financial Institutions

Country	Deposits			Loans			Outreach
	Accounts per 1,000 Adults	Value (% of GDP)	Average Account Value (% of Income Per Capita)	Accounts per 1,000 Adults	Value (% of GDP)	Average Account Value (% of Income GDP)	Bank Branches per 100,000 adults
Afghanistan	n/d	n/d	n/d	n/d	n/d	n/d	n/d
Bangladesh	40.02	2.75	101.04	38.52	2.81	107.39	1.26
India	n/d	n/d	n/d	n/d	n/d	n/d	n/d
Nepal	n/d	4.91	n/d	n/d	n/d	n/d	1.39
Pakistan	11.32	0.21	29.39	8.37	1.14	216.66	0.52
Sri Lanka	1,016.32	7.76	10.09	n/d	2.96	n/d	2.65
Malaysia	1,146.06	13.71	17.08	113.07	12.09	152.6	4.26

Source: CGAP-World Bank Report 2010

Note: No data on Singapore is given. Bhutan and Maldives have not been included in the Survey.



(iii) ATMs & POS Machines

Country	Outreach	
	ATMs per 100,000 adults	POS Terminals per 100,000 adults
Afghanistan	0.38	2.75
Bangladesh	n/d	n/d
India	7.29	67.06
Nepal	1.81	n/d
Pakistan	4.06	48.98
Sri Lanka	12.29	n/d
Singapore	49.83	2,091.42
Malaysia	53.99	1,063.09

Source: CGAP-World Bank Report 2010

Note: Bhutan and Maldives have not been included in the Survey.

As per the World Bank and Consultative Group to Assist the Poor (CGAP) Report for 2010 which uses a number of indicators for financial inclusion based on deposits, loans and outreach (Exhibit 2 (i) & (ii)), it shows that even though Sri Lanka ranks the highest in the number of deposit accounts per 1,000 adults, the country ranks the lowest in the Average Account Value as a percentage of income per capita. This plainly indicates that even though accounts have been opened in Sri Lanka, their average account value is as low as 28% (Commercial Banks) and 11% (State Banks) compared to higher average account values of Bangladesh (233% & 101%), Pakistan (207% & 30%) and India (Commercial Banks 108%). This clearly indicates an absence of sustainability in financial inclusion as implemented in Sri Lanka.

As for outreach, State Banks in Sri Lanka are well ahead of the South Asian countries in enhancing their accessibility to the grassroots and Sri Lanka's Commercial banks too have fared well being only second to India. Exhibit 2 (iii) shows that in terms of ATM penetration too, Sri Lanka is ahead of its South Asian counterparts with 12 ATMs per 100,000 adults as against 7 of India and 4 of Pakistan. These stats clearly indicate that despite enhanced physical outreach, Sri Lanka's banks have not really been able to effectively and productively promote financial products among the masses and get the masses into the banking system. Our banks seem to be left with a high number of accounts with low value or no value, for the simple reason that the financial products and services offered may not be affordable or adapted to the specific needs of low income population or lack of commitment of both parties to maintain a more permanent relationship.

It is in this context that the Central Bank of Sri Lanka highlights the need for 100% financial inclusion by 2015 (Road Map) and also plans to regularize microfinance through the proposed Microfinance Bill (Annual Report 2010). Towards achieving this objective, Central Bank has



identified the following measures to improve financial inclusion and reduce poverty:

- i. Overall focus to link low income people with banking sector
- ii. Conduct financial literacy programmes among people who are currently outside the formal financial sector.
- iii. Facilitate best practices to improve productivity and quality of produce
- iv. Establish market linkages for rural produce to enhance income of producers
- v. Central Bank is planning to continue its series of Consumer Finance and Socio Economic Surveys in 2011/2012 covering the entire island for the first time since 1981/82.

As highlighted by the Central Bank, banks have a greater role to play in facilitating the un-banked and the under-banked masses to enter and be benefited by the financial system of the country. The banks may implement the following to ensure sustainable financial inclusion in Sri Lanka.

- **Promotion of appropriate, accessible, usable, valuable and affordable small-scale, basic financial services is a must for financial inclusion** – Banks should strive to simplify their products and services to be more flexible to accommodate the lifestyles of the grassroots by adopting measures such as loosening KYC requirements, introducing 'basic accounts' with mandated lower fees and low minimum balances etc.
- **Continuing construction of a large distribution network** – banks need to be accessible to people in their own territories. Bank's physical presence as well as its impact should be felt on the people's lives for them to build confidence in the banking system. Branchless banking tools like palmtop banking can be used to reach out to the customers at their doorstep.
- **Strengthening of the social and welfare investment activities in their communities** – Banks should seek to uplift the lives of the people through sustainability exercises that go beyond mere CSR. It is the nature of the people that they will seek banking facilities only when their other basic needs and requirements are fulfilled. Therefore in order to promote financial inclusion, conditions surrounding them need to be improved.
- **Recognition of the importance of financial education** – people who do not have a favourable attitude to banking need to be rid of their negative mindset. They need to be taught about the benefits of inclusion in the banking system. The bank staff too should be educated on the need to include the grassroots in their clientele and change their attitude. Attitude of the Bank staff has been proved to be a major turn-off for the poor in including them in the banking system.



Exhibit 3: Financial Inclusion: Analysis of Outreach

	High Income Countries	Developing Countries	South Asia	Sri Lanka
Bank Density (No. of bank branches per 100,000 persons)	32	10	7	14
ATMs per 100,000 persons	94	29	4	11

Source: CGAP-World Bank Report 2010, Central Bank of Sri Lanka Annual Report 2010

Conclusion

Banks may implement business strategies of their choice such as priority banking to enhance their bottom line, but they should also implement strategies to include the less income earning segments in their clientele on a sustained basis such as barefoot banking since upliftment of the life standards of the masses will undoubtedly project a long-lasting impact and enduring benefit to society at large and businesses in particular. However, Banks should avoid falling into the trap of CSR in implementing financial inclusion. Financial inclusion does not mean opening savings accounts to all the people in a village and declaring the village to be 100% financially included; it goes much deeper. Financial inclusion means providing accessible and affordable financial services adapted to the specific needs of low income population and maintaining a more permanent relationship with clients and following more stable policies in the good and bad times. More importantly, financial inclusion should also be accompanied with financial literacy and financial discipline to make it more sustainable.

The financial inclusion and integrated development: which should come first? As mentioned in the introduction, this is similar to 'Chicken or egg?' situation, as we cannot segregate the causal relationship of these two clearly. Instead of arguing on this, what is important is to understand that financial inclusion and integrated development are the two critical components of a process which seeks to realize the ultimate objective of well being of the people of the country. In this process both financial inclusion and integrated development will go hand in hand and development of one will help to improve the other and vice versa. In order for this process to function properly, it is of paramount importance that we have the right policy framework for implementation of the strategies which are aligned to address changes taking place regionally and globally followed by close monitoring with in-depth analysis of progress.

If social and economic arrangements are the most efficient means of realizing freedom and general welfare, all our efforts towards economic development should answer only one question and that is, 'How far does our collective economic wealth improve all individuals' ability to live as they would like?'



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