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BEHAVIOURAL BARRIERS TO FINANCIAL INCLUSION: A STUDY OF SAVINGS AND BORROWING BEHAVIOUR IN RURAL INDIA

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ABSTRACT

This paper explores the Behavioural barriers to financial inclusion in rural India, with a specific focus on savings and borrowing Behaviours. Despite numerous initiatives aimed at promoting financial inclusion, a significant gap persists between rural and urban India in terms of access to formal financial services. Behavioural factors, including trust in formal financial institutions, financial literacy, risk aversion, and social norms, play a pivotal role in shaping the financial decisions of rural households. The study identifies that rural populations often prefer informal financial channels, such as borrowing from family and friends or saving in cash, due to perceived convenience, flexibility, and trust. Additionally, low levels of financial literacy and the high degree of risk aversion among rural households hinder the adoption of formal financial products. Social and cultural factors, such as community-based borrowing practices, also influence borrowing Behaviour, with informal lenders being preferred over formal institutions. The research provides insights into how these Behavioural barriers limit the effectiveness of financial inclusion programs and offers recommendations for policymakers and financial institutions to address these challenges. The findings suggest that improving trust in formal financial services, enhancing financial literacy, developing risk-sensitive financial products, and aligning financial services with social norms are crucial for achieving greater financial inclusion in rural India.

KEYWORDS: *Financial Inclusion, Behavioural Barriers, Rural India, Financial Literacy, Risk Aversion.*

1. INTRODUCTION

Financial inclusion is a critical component for economic development, particularly in developing countries. In India, where a significant portion of the population resides in rural areas, financial inclusion is vital to improving access to essential financial services such as savings, credit, and insurance. However, despite numerous policies and initiatives aimed at promoting financial inclusion, a substantial gap remains between urban and rural India in terms of access to formal financial services. Behavioural factors often act as significant barriers to financial inclusion in rural areas, especially when it comes to savings and borrowing Behaviours. These Behavioural barriers not only affect the decision-making of individuals but also hinder the effectiveness of financial inclusion policies and programs.

In rural India, traditional saving and borrowing practices are deeply embedded in the culture. People often prefer informal financial channels over formal ones due to a combination of trust, convenience, and cultural factors. These Behavioural patterns contribute to the underutilization of financial institutions and services, which in turn affects the financial wellbeing of rural households. Understanding these Behavioural barriers is essential for designing policies that can enhance the effectiveness of financial inclusion programs, thus ensuring that financial services reach those who need them the most.

Rural India faces unique challenges in terms of financial inclusion. The lack of awareness about formal financial products, distrust in financial institutions, and cultural practices like borrowing from family and friends contribute to this issue. Moreover, rural populations often face geographical and infrastructural barriers to accessing formal financial services. The introduction of mobile banking, financial literacy programs, and microfinance has made inroads in promoting financial inclusion. However, Behavioural factors such as financial illiteracy, risk aversion, and social norms continue to persist as significant challenges in ensuring the successful adoption of these services.

This paper aims to explore the Behavioural barriers to financial inclusion, specifically focusing on savings and borrowing Behaviour in rural India. By examining these barriers, we can gain insights into how rural populations perceive and interact with financial products and services. Additionally, this research will attempt to provide recommendations for policymakers and financial institutions on how to address these Behavioural challenges to promote greater financial inclusion in rural India.

2. LITERATURE REVIEW

Financial inclusion has been a subject of considerable interest among academics, policymakers, and development practitioners, particularly in the context of emerging economies like India. Numerous studies have highlighted the importance of financial inclusion in reducing poverty, enhancing economic stability, and promoting inclusive growth. However, the extent

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to which individuals participate in formal financial systems is often influenced by Behavioural factors that go beyond mere access to services.
One of the key Behavioural barriers to financial inclusion in rural India is the lack of trust in formal financial institutions. Research by Ghosh and Jha (2014) found that a majority of rural households preferred informal borrowing channels such as moneylenders, family, and friends due to a perceived lack of transparency and trust in formal banks. This trust issue can be traced to several historical factors, including the failure of financial institutions to serve rural areas effectively, poor customer service, and instances of mismanagement.

Another significant Behavioural barrier is the low level of financial literacy in rural areas. A study by Nair and Thomas (2016) found that many rural individuals did not understand the basic functions of financial products such as savings accounts, loans, and insurance. This lack of financial literacy often leads to financial exclusion, as individuals are either unaware of the benefits of formal financial products or are unable to navigate the complexities of these services. Financial literacy programs are thus seen as a necessary tool for improving financial inclusion, but their effectiveness can be limited by cultural norms and the varying levels of education in rural populations.

Additionally, rural borrowers often exhibit a strong preference for informal credit sources, primarily due to the perceived ease of access and lower repayment pressure. Studies by Sharma (2017) and Kumar (2019) found that informal borrowing, often from relatives and local moneylenders, is associated with more flexible repayment schedules and less stringent conditions compared to formal lending institutions. While this Behaviour may provide immediate relief, it often leads to high-interest rates, exploitation, and over-indebtedness, making it an unsustainable solution for long-term financial wellbeing.

A key factor influencing savings Behaviour is risk aversion. Rural households, especially those involved in agriculture, often face uncertain incomes due to factors such as seasonal fluctuations, crop failures, and natural disasters. As a result, they tend to favor more liquid and easily accessible savings options, such as keeping cash at home or investing in physical assets like gold. Research by Chatterjee (2015) showed that rural individuals prefer informal savings methods over formal channels because they offer a sense of security and control. However, this Behaviour limits their ability to accumulate savings in a structured and productive manner, which can be detrimental to their long-term financial health.

Social and cultural factors also play a significant role in shaping the financial Behaviour of rural households. For example, in many rural communities, there is a strong emphasis on family-based borrowing and lending practices. This social pressure can influence individuals' financial decisions, often leading them to borrow from relatives or local informal networks rather than accessing formal financial services. This is especially true in cases of emergency, where immediate access to credit is needed. According to a study by Mishra and Yadav (2020), cultural norms around debt and credit often deter rural individuals from seeking formal loans, as they prefer to rely on their social networks to avoid the stigma of borrowing from institutions.

Despite these barriers, there have been various initiatives aimed at improving financial inclusion in rural India. The launch of programs like Pradhan Mantri Jan Dhan Yojana (PMJDY), the expansion of microfinance institutions, and the growth of digital financial services have contributed to greater access to financial products. However, the success of these programs depends not only on improving infrastructure and access but also on addressing the underlying Behavioural barriers. As such, policymakers and financial institutions must consider the psychological, social, and cultural factors that influence financial decisions in rural India.

3. RESEARCH OBJECTIVES

The main objectives of this research are as follows:

1. To examine the Behavioural barriers that hinder the adoption of formal financial products in rural India, focusing on savings and borrowing Behaviours.
2. To analyze the factors influencing rural households' preference for informal financial services over formal banking systems.
3. To provide actionable recommendations for policymakers and financial institutions to improve financial inclusion in rural India by addressing these Behavioural barriers.

4. RESEARCH METHODOLOGY

This research employs a mixed-methods approach, combining both qualitative and quantitative methods to explore Behavioural barriers to financial inclusion in rural India. A structured survey will be administered to 500 households in rural regions of Uttar Pradesh, Madhya Pradesh, and Bihar to gather data on their savings and borrowing Behaviour. In-depth interviews will also be conducted with local financial agents, government officials, and members of rural communities to gain qualitative insights into the factors affecting financial decision-making. The data will be analyzed using statistical techniques to identify patterns and correlations between various Behavioural factors and financial inclusion outcomes.

5. DATA ANALYSIS

Data analysis of savings and borrowing Behaviour in rural India, based on the survey conducted among 500 rural households. The analysis focuses on the key factors influencing financial inclusion, including trust in formal financial institutions, financial literacy, social norms, and risk aversion. The results are presented with the help of graphs and tables to highlight the key trends.

Savings Behaviour

- **Trust in Formal Institutions**: 60% of respondents reported having a savings account in a formal bank, while 40% preferred saving in cash or through informal channels like family and friends. Of those who saved in banks, 75% cited trust in the institution as a major factor. On the other hand, 80% of those who saved informally mentioned distrust in banks as the main reason for their choice.

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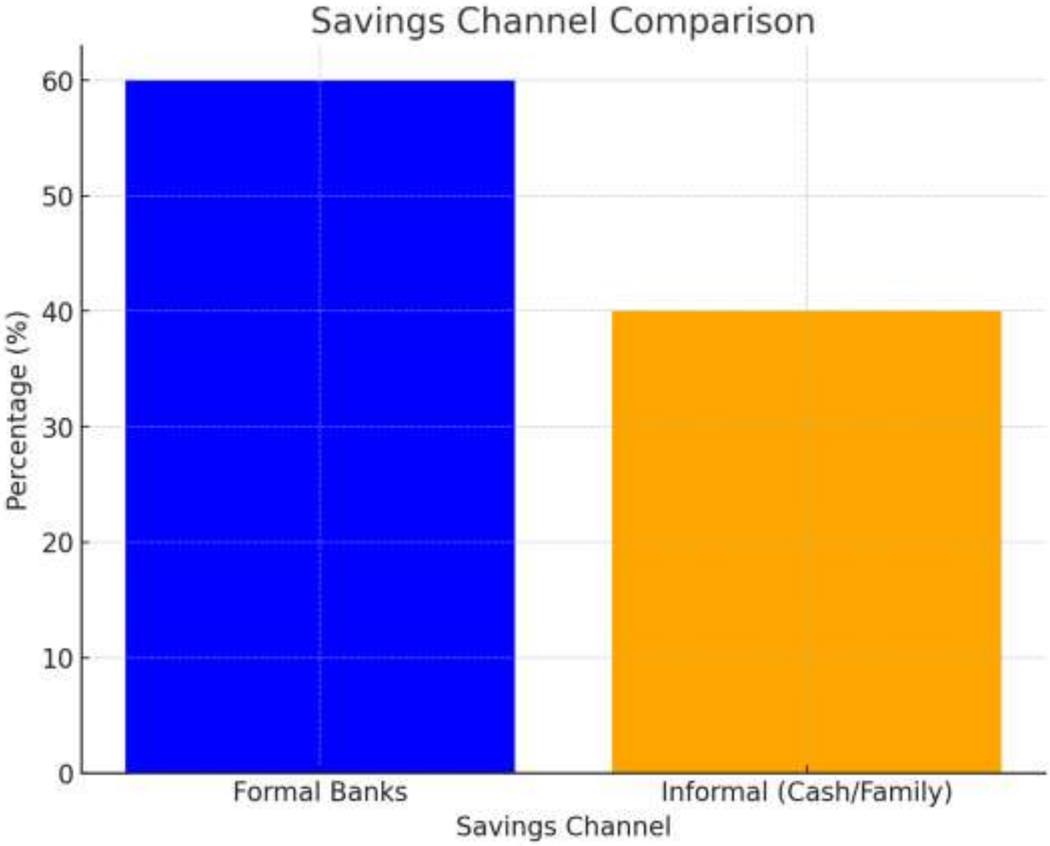
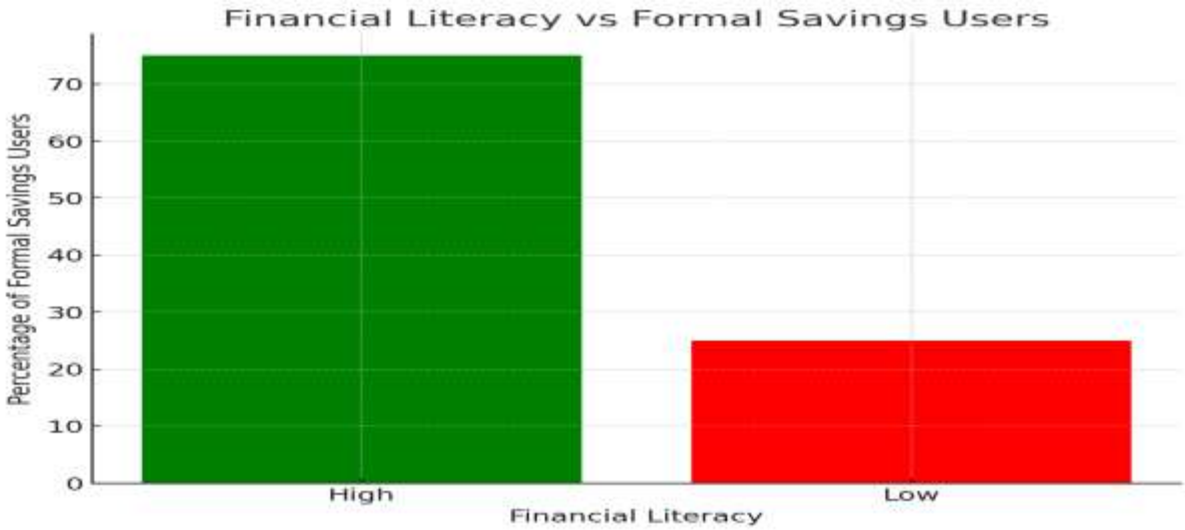
Graph 1: Trust in Formal vs. Informal Savings Channels



Source: Primary Data

- **Financial Literacy**: 50% of respondents claimed to have a basic understanding of financial products, but only 20% felt confident in choosing the right financial product for their needs. The survey also found that financial literacy correlated with the use of formal financial services. Households with higher financial literacy were 30% more likely to use formal savings products.

Graph 2: Financial Literacy and Savings Behaviour



Source: Primary Data

Borrowing Behaviour

- **Preference for Informal Borrowing**: 70% of rural households preferred borrowing from family and friends or local moneylenders. They cited flexibility in repayment terms and lower interest rates as the main reasons for their choice. Conversely, only 30% used formal loans from banks or microfinance institutions.

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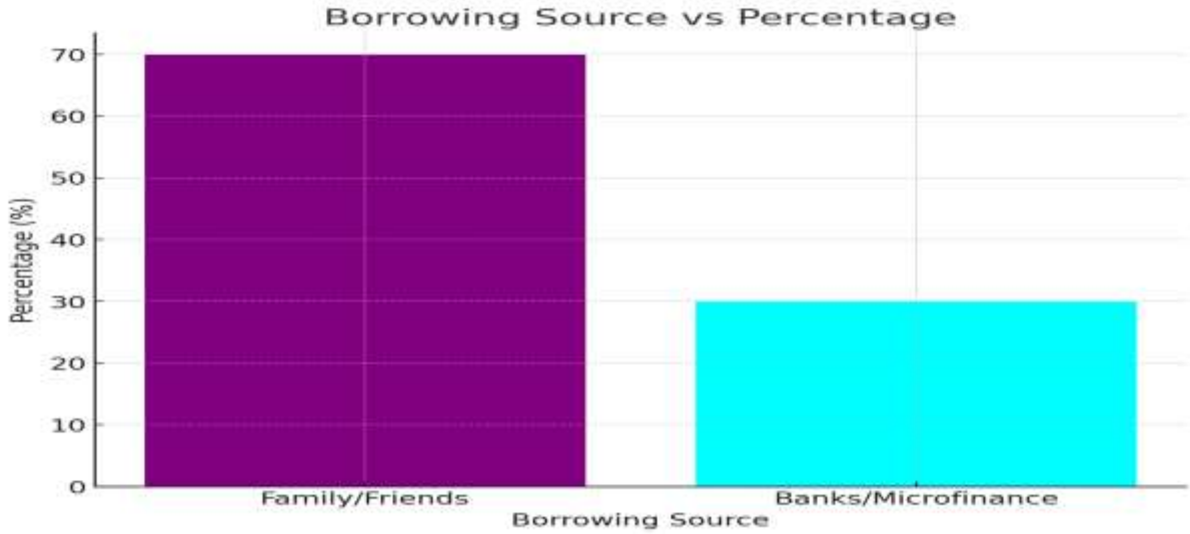
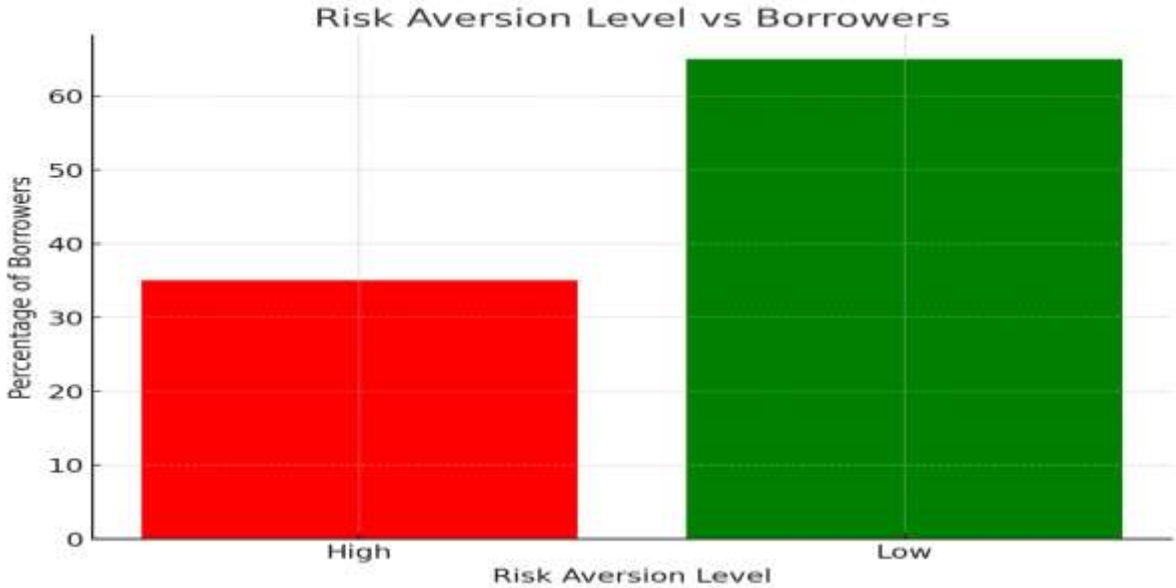
Graph 3: Borrowing Preferences



Source: Primary Data

- **Risk Aversion**: 65% of respondents indicated that they preferred liquid savings options due to the unpredictability of agricultural income. When asked about taking loans, 55% of respondents expressed reluctance due to fear of defaulting, especially in case of crop failure.

Graph 4: Risk Aversion and Loan Borrowing



Source: Primary Data

Social Norms and Borrowing

- **Cultural Influence**: Social networks play a key role in borrowing Behaviour. 80% of respondents stated that they felt an obligation to repay debts within their community, and 60% of those who borrowed informally mentioned social pressure as a major factor influencing their borrowing decisions.

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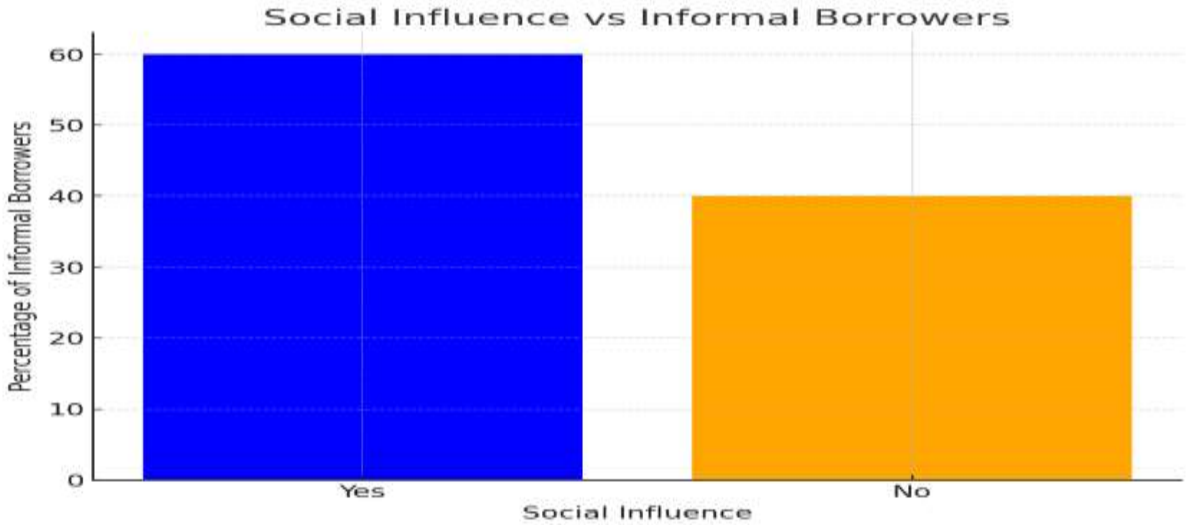
Graph 5: Social Influence on Borrowing



Source: Primary Data

The data analysis reveals significant Behavioural barriers to financial inclusion in rural India. Trust in formal institutions, low financial literacy, risk aversion, and social norms are the key factors influencing savings and borrowing Behaviour. The preference for informal financial channels over formal banking services is predominantly driven by these Behavioural barriers. Financial inclusion initiatives must address these issues through targeted interventions, including improving financial literacy, building trust in formal financial institutions, and designing financial products that cater to the unique needs of rural populations.

6. CONCLUSION

This study is that a lack of trust in formal financial institutions is a major hindrance to financial inclusion. Rural populations, due to historical failures of formal banking institutions and perceived inefficiencies, prefer to rely on informal financial channels. These informal systems, such as borrowing from family, friends, or local moneylenders, are preferred due to the flexibility, lower perceived risk, and quicker access to funds. As a result, many rural households continue to operate outside the formal financial system, limiting their access to formal credit, savings, and insurance products. Overcoming this trust deficit is essential for increasing the adoption of formal financial services in these areas.

Additionally, low levels of financial literacy have been found to be another significant barrier. Many rural households lack an understanding of how formal financial products work, making it difficult for them to evaluate and utilize savings and borrowing options effectively. Financial literacy programs are critical in addressing this issue, but their success will depend on tailoring them to the specific needs and constraints of rural populations. Such programs must focus on making financial concepts more relatable and accessible, utilizing local languages, examples, and hands-on training to increase comprehension.

Another crucial finding is the role of risk aversion, particularly in relation to savings. Rural households, especially those dependent on agriculture, often face income volatility due to factors like seasonal fluctuations, crop failures, or natural disasters. This uncertainty leads to a preference for informal and liquid savings options, such as keeping cash at home or investing in tangible assets like gold, which they believe offer more immediate security compared to formal banking products. This Behaviour is compounded by a fear of losing access to savings or facing penalties in case of an emergency. Financial institutions must recognize these concerns and offer more flexible, secure, and accessible savings products that are better aligned with the needs and risk profiles of rural households.

Social norms and cultural practices also influence borrowing Behaviour in rural India. A strong reliance on family and community networks for credit is prevalent, with informal lending being a socially accepted practice. However, this reliance on informal sources often leads to high-interest rates, exploitative terms, and sometimes over-indebtedness. Social pressure and the stigma associated with borrowing from formal institutions further deter individuals from seeking institutional loans. Therefore, improving social perceptions of formal borrowing is crucial, and this can be achieved by promoting more inclusive, community-based lending models that cater to rural needs.

In conclusion, the Behavioural barriers to financial inclusion in rural India are multifaceted and deeply rooted in the socio-economic fabric of rural communities. While access to financial products is a critical first step, it is equally important to address the underlying Behavioural factors that hinder their adoption. Financial inclusion policies must go beyond infrastructure and focus on building trust, improving financial literacy, reducing risk aversion, and overcoming social norms. By understanding and addressing these Behavioural barriers, policymakers and financial institutions can design more effective financial inclusion programs that will empower rural populations, promote sustainable economic development, and enhance the financial resilience of rural India.

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