IZA DP No. 4132

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ABSTRACT

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Financial inclusion is the broad based delivery of banking and other financial services at affordable cost to the poorest sections of society. In India, financial inclusion emphasizes to include maximum number of people under formal financial systems. The most important part of financial services in a region is typically measured by number of people who have access to bank accounts. The present study investigates the drive to financial inclusion in the form of the growth in bank accounts of scheduled commercial banks and the changes in below poverty line population. The result suggests that the growth in bank accounts is not significantly associated with the reduction in below poverty line population across states. Providing banking services to maximum number of people is unsuccessful as a poverty reduction strategy. As a poverty reduction strategy, developing inclusive financial systems should give priority, which is financially and socially sustainable.

JEL Classification: G24, G21, I32

Keywords: banking, financial inclusion, poverty

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1. Introduction

A person may be said to have access to financial services if he or she is able to use formal or semiformal financial services in an appropriate form at reasonable prices when such services are required (Fernando, 2007). The access to finance in developing countries has been considered as a necessity just like safe water or primary education (Beck & de la Torre, 2006; Leeladhar, 2005). In developed countries, financial services covers almost majority of the population (Peachy and Roe. 2004). In developing countries only 20 per cent population has access to formal financial services (World Savings Banks Institute, 2004). A large section of population remains financially excluded are belongs to low-income households. With the growth in urbanization and the policy discretion by the central banks access to finance in both urban and rural areas are increasing rapidly in many developing countries.

Measuring access to finance is seemingly difficult because of very nature of reveal preference choice of an individual towards financial services. In less developed countries it has been widely practiced that the majority amount of finance is not percolated to people who have the actual need of it. Financial inclusion is the availability of banking services at affordable costs to the disadvantages section of population. Financial inclusion emphasizes access of a host of financial services, which includes savings, loans, insurance, credit etc that are supposed to help the poor people out of poverty. The most important part of financial services in a region is typically measured by number of people who have access to bank accounts (Beck & De la Torr, 2006; Littlefield et al, 2006). This is because bank accounts enables people to perform important financial functions like access to savings schemes, access to credit, taking loan, insurance, money transfer etc. Thus, bank accounts determines access to many other financial services (Mohan, 2006). Internationally, having a current or saving accounts on its own is not regarded as an exact indicator of financial inclusion. In developed countries, financial inclusion is generally related to the issues about social exclusion and welfare. In India, the basic concept of financial inclusion is the percentage of adult population having bank accounts. Only 41 per cent of adult populations do not have access to banking services. The coverage of financial services in terms of banks accounts are 39 per cent for rural areas, and 60 per cent for urban areas.

The reasons behind the dismal number of bank accounts are two fold: One can be addressed from the demand side and the other has its origin from the supply side. Prevailing inequality is the fundamental reason for lower growth in bank accounts in India. People working in the unorganized sectors or even in the agricultural sector do not have sustainable as well as surplus level of income so that they can even think of about opening a bank account. Another reason behind the low demand for organized financial services in the rural area is the lack of investment opportunity in rural India. From the supplier point of view, directed credit is always considered as a leakage to the banking business. Further, people struggling to meet their both ends do not have any mortgage holding so that they can proceed for loan from organized financial systems. The supply side disturbance can be solved with the help of active government policy, even within a short span of time. However, the demand side problems are acute and chronic in nature. It requires structural change of the economy. The following flow chart explains the demand-side barriers of the growth in finance services.

Low level of income / poverty

↓

High level of consumption

↓

Low level of saving

↓

Low demand for banking services

↑

Lack of investment opportunity

Again financial exclusion can acts as a fundamental source of poverty. This implies that poverty causes low demand for organized financial system and financial exclusion causes poverty. Therefore, there is a bidirectional cause and effect relationship between poverty and financial inclusion. In either ways people needs access to credit and necessary financial services, which are best enable through a bank accounts. In India, financial inclusion is confined to ensuring bare minimum access to savings account without frills to all.

Alleviating poverty has long been the primary goal of the policy makers in India. The situations of poverty become more deplorable if it is adjusted for international yardstick of poverty measurement. According to recent World Bank estimate, India had 456 million people or about 42 percent of the population living below the new international poverty line of 1.25 US dollar per day. The number of Indian poor contributes 33 percent of the global poor, which is pegged at 1.4 billion people. If the measurement of the international poverty line is slightly increased from the 1.25 US dollar a day to 2.00 US dollar a day then the scenario is even further disheartening. Based on that measurement, India had 828 million people, or 75.6 percent of the population living below the poverty line surpassing the Sub-Saharan Africa, considered the world's poorest region, with 72.2 percent people living without 2 US dollar a day. This clearly demonstrates the mammoth inequality prevailing in India even after the inclusive growth policy commitment by various governments following a number of five-year plans. Poverty hit people who are highly concentrated in rural areas with limited access to financial services. Global microfinance campaign has helped changing lives of poor. In India, an estimated 410 lakh[1] poor households have access to formal banking system under the SHG-Bank Linkage Programme.

In this context, the present study concerns with the drive towards financial inclusion and the changes in poverty level across different states in India. This apart, the study provides an insight into the demographic decomposition of scheduled commercial bank activities regarding the growth of savings and credit accounts. Emphasis is given to investigate the changes observed in different periods. In addition, the growth of savings and credit has also been investigated. The paper is organized into the following sections. Section 2 describes the background for financial inclusion in India. Section 3 presents the growth of banking sector (scheduled commercial bank) across the different demographic composition. In the next section, the state wise scenario of poverty is presented. Section 5 relates the drive towards financial inclusion with state level poverty situation. Finally, in Section 5 concludes the whole study.

[1] 1 Lakh = 1,00,000

2. a Background of financial inclusion in India

After independence rural cooperative banks were established in an attempt to disseminate financial services among marginalized sections of population. The basic intension was to provide more credit to agriculture and small-scale industries. However, the entire plan failed to materialize as majority of the bank credit was mobilized towards big enterprises. In order to combat this problem, in 1969 banks came under the ownership of the government in two phases (14 banks in 1969 and 6 banks in 1980). The bank nationalization was marked a paradigm shift in the banking sector. Under this arrangement, at least 40 per cent bank lending had to be extended in the priority section and 25 per cent of these loans had to be extended to weaker sections within priority section. Other feature of nationalization includes interest rate controls on credit upto 2 lakhs, interest subsidy, capital subsidy schemes like IRDP, SGSY etc. The nationalized banks and regional rural banks (RRBs) control over 73 per cent of all commercial banking assets. Since bank liberalization, the distribution of financial services in the country has been quite extensive compared to other developing economies.

2. b Extent of financial exclusion

The basic objective of financial inclusion is to reach poor and disadvantage section of population. According to the latest NSSO data, almost half of the farmer households do not have access to credit, either from institutional or non-institutional sources. Organized bank branches specially the nationalized commercial banks covered only the 27 per cent of total farm households. As per NSSO survey 2003, financial inclusion was only 49 percent in 18 states. Andhra Pradesh ranked at the top with 75 per cent inclusion. The financial inclusion scenario of the North-Eastern states is very dismal compared to the industrially advanced states. The poorer a state, the greater is the level of financial exclusion (Rangarajan, 2007). The extent of financial exclusion from credit market is higher. According to NSSO data 51.4 per cent households do not have access to credit. As per Rangarajan Committee's report on Financial Inclusion 2008, financial exclusion is widespread which varies widely across regions, social groups and asset holdings. The problem of financial inclusion is the resurgence of moneylenders as the prominent source of credit to the rural population. Thus, extra initiatives must be taken in the form of rural counseling centers to advise people about financial products, information dissemination, setting up Rural Credit Bureau, increasing financial education and micro insurance products.

3. Demographic Decomposition of Growth of Banking Sector

3.1 Growth in bank accounts

Commercial banks contain over half the deposits in India. The overall growth in saving bank accounts was 10.22 per cent per annum during the pre reform period, the highest of the three sub-periods[2] (Table 1). This is because of the bank nationalization and emphasis on priority sector lending. However, the growth fell drastically to 1.42 per cent during reform period. The annual growth increased marginally to 2.94 per cent in the post reform period. During pre-reform period rural area achieved the annual growth in bank accounts of 13.81 per cent, followed by urban areas (9.98 per cent), semi urban areas (9.31 per cent) and metropolitan areas (8.2 per cent). Reform period was the worst in terms of the growth in bank accounts as the overall growth in bank account fell drastically to 0.87 per cent per annum, while metropolitan areas witnessed highest growth of 2.66 per cent per annum. In the post reform period, the growth in bank accounts was urban centric, as the highest growth in bank accounts was achieved in metropolitan areas (5.38 per cent), followed by urban areas of 3.08 per cent per annum. The growth in bank accounts in rural and semi-urban areas was 2.06 per cent and 1.8 per cent respectively. This is because of the emergence of a vibrant middleclass population in urban and metropolitan areas.

Table 1: Growth in deposit bank accounts by population groups

	Pre-reform Period (1980-1990)	**Reform Period (1991-1999)**	**Post reform Period (2000-2007)**
Rural	12.99	0.87	2.06
Semi-Urban	9.31	1.53	1.80
Urban	9.98	0.95	3.08
Metropolitan	8.2	2.66	5.38
Total	10.22	1.42	2.94

Source: Basic Statistical Returns of Scheduled Commercial Banks in India.
Note: Growth rates are compound annual growth rates

The annual growth in credit accounts witnessed significant annual growth in the pre reform period (12.16 per cent). The growth was highest in rural areas (14.33 per cent), followed by urban area (10.92 per cent), semi-urban area (9.99 per cent) and

[2] The total period of the study (1980-2007) is divided into three sub periods - pre-reform period (1980-90), reform period (1991-99) and post reform period (2000-07).

metropolitan area (9.96 per cent). However, the overall growth in credit accounts went into negative territory during reform period. Only metropolitan area achieved positive growth of 3.63 per cent per annum. The situation was reversed in the post reform period. The growth in credit accounts recovered into positive territory; with the overall growth rate was 9.16 per cent per annum. Metropolitan areas achieved outstanding growth of 24.06 per cent during post reform period, the highest among the subgroups, while rural area witnessed the slowest growth (3.01 per cent).

Table 2: Growth in credit accounts by population groups

	Pre-reform Period (1980-1990)	**Reform Period (1991-1999)**	**Post reform Period (2000-2007)**
Rural	14.33	-3.82	3.91
Semi-Urban	9.99	-2.09	6.79
Urban	10.92	-2.77	8.84
Metropolitan	9.96	3.63	24.06
Total	12.16	-2.58	9.16

Source: Basic Statistical Returns of Scheduled Commercial Banks in India.

3.2 Growth in volume of bank credits

The overall growth rate of credit volume of commercial bank was highest in the post-reform periods (22.59 percent). This is because of the increasing outreach and functional diversification of the scheduled commercial banks. During the pre-reform the growth was 16.81 per cent, while reform period witnessed a marginal decline of growth to 15.47 per cent. This is due to the growth in service and manufacturing sector bypassing the agricultural sector just after the economic reform. As far as geographical distribution of credit is concerned, except metropolitan area the growth in bank credits has declined. Rural credit was severely neglected during the reform period compared to pre reform period. However, the growth in rural credit recovered in the post reform period. However, the credit growth in rural areas has recovered in the post reform period. Growth in bank credit in metropolitan areas increased gradually during the different periods. Urban and semi-urban group of people enjoyed higher volume of credit in the post-reform reform period compared to pre reform and reform periods.

Table 3: Growth in credits by population groups

	Pre-reform Period (1980-1990)	**Reform Period (1991-1999)**	**Post reform Period (2000-2007)**
Rural	24.57	9.2	22.15
Semi-Urban	17.35	12.9	18.56
Urban	16.79	12.23	23.14
Metropolitan	14.09	20.16	23.42
Total	16.81	15.47	22.59

Source: Basic Statistical Returns of Scheduled Commercial Banks in India.

3.3 Growth in bank deposits

The growth in bank deposits of scheduled commercial banks remained constant in both pre-reform and reform period, grown at around 17 per cent annually. Even the banking sector reform has failed to increase the relative amount of deposits although the absolute amount of deposits has increased. Growth of bank deposit in rural area has suffered a lot during the post-reform period. The growth bank deposits gradually decreasing during various phases of reforms, 20.2 per cent in the pre reform period, 15.84 per cent in the reform period and 10.75 per cent in the post reform period. This is because of the reduction of the per capita income of rural India in the pre-reform period. In contrast, the growth in bank deposits remains higher in urban areas for the entire period of the study. On the other hand, metropolitan areas achieved the highest growth in bank deposits during post reform periods. During pre reform period the bank deposit in metropolitan areas grew at 17.79 percent per annum, while the growth was almost same during the reform period (17.61 per cent).

Table 4: Growth in bank deposits by population groups

	Pre-reform Period (1980-1990)	Reform Period (1991-1999)	Post reform Period (2000-2007)
Rural	20.2	15.84	10.75
Semi-Urban	16.81	16.12	11.34
Urban	18.07	15.77	15.28
Metropolitan	17.79	17.61	22.45
Total	17.97	16.62	17.43

Source: Basic Statistical Returns of Scheduled Commercial Banks in India.

4. Bank outreach and poverty

4.1 Growth in Bank Accounts: State-wise Scenario

State wise growth in bank accounts suggests that during the post reform period Andhra Pradesh achieved highest growth of 5.69 per cent in rural areas, followed by Kerala (3.40 per cent) and Gujarat (9.23 per cent), constituting top three states in India. States where the negative growth in bank accounts observed are Chandigarh (-0.96 per cent), Delhi (-0.94 per cent), Andaman & Nichobar (-0.69 per cent) and West Bengal (-0.01 per cent). The growth in bank outreach in urban area is much better in urban areas. The highest growth is observed in Jammu and Kashmir of 6.61 per cent. Pondicheery ranked second with 6.07 per cent growth rate in bank accounts, followed by Andhra Pradesh (5.93 per cent) and Gujarat (5.33 per cent) witnessed significant growth rates.

Only West Bengal, among the urban areas witnessed negative growth in bank accounts of -0.01 per cent.

4.2 Changes in Poverty: State-wise Scenario

Changes in percentage of population living below poverty line are presented in Table 5. The differences in percent of population below poverty line were taken between 1999-2000 and 2004-05 for states and union territories. The data was collected from Planning Commission and NSSO[3]. There are two types of measurement of below poverty line population in 2004-05, uniform reference period and mixed reference period. The present study uses uniform reference period calculation. At all India level the level of below poverty line population was 26.1 per cent in 1999-2000 which increases to 27.5 in 2004-05. State wise scenario suggests that during this period population living below poverty line decline significantly by 28.15 per cent, followed by Madhya Pradesh (22.43 per cent), Nagaland (20.07 per cent) and Meghalaya (-16.57 per cent). The percentage of population living below poverty line increased substantially was Punjab (40 per cent), Daman and Deu (28.76 per cent) and Karnataka (20.26 per cent).

[3] The Expert Group under Planning Commission of India has estimated the poverty lines and poverty at the national and state levels at six points of time 1973-74, 1977-78, 1987-88, 1993-94 and 1999-2000. In 2004-05, poverty is estimated using different methodology.

Table 5: Ranking of states in terms of change in poverty ratio, growth in bank accounts (Rural Areas)

Ranking of states in terms of change in poverty		**Ranking of states in terms of growth in deposit accounts**	
State / Union Territory	**Change in poverty level between 1999 – 2005**	**State / Union Territory**	**Growth in bank accounts**
Delhi	-6.5	Andhra Pradesh	5.69
Gujarat	-5.93	**Kerala**	3.40
Maharashtra	-5.88	**Gujarat**	2.93
Haryana	-5.33	**Rajasthan**	2.92
Rajasthan	-4.96	Madhya Pradesh	2.79
Goa	-4.05	Jammu & Kashmir	2.78
Kerala	-3.82	**Haryana**	2.77
Karnataka	-3.42	Orissa	2.75
Himachal Pradesh	-2.76	Bihar	2.62
Punjab	-2.75	Pondicherry	2.33
Pondicherry	-2.35	Himachal Pradesh	1.83
Andaman & Nicobar Islands	-2.35	Karnataka	1.71
Tamil nadu	-2.25	Maharashtra	1.67
Uttar Pradesh	-2.18	Uttar Pradesh	1.44
Chandigarh	-1.35	Punjab	1.23
Jammu & Kashmir	-0.63	Goa	0.25
Andhra Pradesh	-0.15	Tamil Nadu	0.08
Madhya Pradesh	0.16	West Bengal	-0.01
Orissa	1.21	Andaman & Nicobar Islands	-0.69
Bihar	2.2	Delhi	-0.94
West Bengal	3.25	Chandigarh	-0.96

Note: Selection of states is dependent on availability and comparability of data.
Growths are compound annual growth rates, are measured from 2000-2007

Table 6: Ranking of states in terms of change in poverty ratio, growth in bank accounts (Urban Areas)

Ranking of states in terms of change in poverty		**Ranking of states in terms of growth in deposit accounts**	
State / Union Territory	**Change in poverty level between 1999 – 2005**	**State / Union Territory**	**Growth in bank accounts**
Rajasthan	-13.05	**Jammu & Kashmir**	6.61
Karnataka	-7.35	Pondicherry	6.07
Jammu & Kashmir	-5.92	**Andhra Pradesh**	5.93
Delhi	-5.78	Gujarat	5.33
Maharashtra	-5.39	**Orissa**	4.93
Haryana	-5.11	Karnataka	4.71
Madhya Pradesh	-3.66	Kerala	4.54
Bihar	-1.69	Tripura	4.53
Orissa	-1.47	**Madhya Pradesh**	4.36
Andhra Pradesh	-1.37	**Rajasthan**	4.19
Punjab	-1.35	Tamil Nadu	4.19
Pondicherry	-0.09	Haryana	3.95
Tamil Nadu	-0.09	Bihar	1.91
West Bengal	0.06	Delhi	1.83
Kerala	0.07	Punjab	1.65
Uttar Pradesh	0.29	Uttar Pradesh	1.61
Gujarat	2.59	Maharashtra	1.45
Tripura	4.17	West Bengal	-0.01

Note: Selection of states is dependent on availability and comparability of data.
Growths are compound annual growth rates, are measured from 2000-2007

4.2 Growth in Bank Accounts and Changes in Poverty: A Comparison

Table 6 and 7 compares the state-wise growth in bank accounts and the percentage changes in below poverty line population. States are ranked in terms of their growth in bank accounts and changes in below poverty line population in both rural and urban areas. In rural areas, the top ten states in terms of reduction of below poverty line population are Delhi, Gujarat, Maharashtra, Haryana, Rajasthan, Goa, Kerala, Karnataka, Himachal Pradesh and Punjab. Among them Kerala, Gujarat, Rajsathan and Haryana observed the highest growth in bank accounts (See Table 6). In urban areas, the highest change in below poverty line population observed in Rajasthan, while J&K observed highest growth in bank accounts. Jammu & Kashmir, Andhra Pradesh, Orissa, Madhya Pradesh and Rajasthan included among the top states in terms of reduction in poverty between 1999-2000. In rural areas, high growth in bank accounts was accompanied by reduction in below poverty line population in Kerala, Gujarat, Rajasthan and Haryana. However, in urban areas high growth in bank accounts was accompanied by higher reduction in below poverty line population was achieved in Jammu & Kashmir, Andhra Pradesh, Orissa, Madhya Pradesh and Rajasthan. That is, for other states, the growth in bank accounts is not accompanied by the reduction in below poverty line population across various states. Table 7 presents the correlation between changes in poverty and the growth in bank accounts in both rural and urban areas. Both these variables are negatively correlated, that is growth in bank accounts is accompanied by reduction in poverty. However, the strength of association is insignificant. It is essential to ensure social sustainability of financial inclusion programs. Drive towards financial inclusion should accompanied by support programs which catalyze employment opportunities. Targeted support services could provide economic empowerment, improved earnings and reduced vulnerability. Thus, inclusive policies are required to make financial inclusion as a successful poverty reduction strategy.

Table 7: Spearman rank correlation between changes in poverty and growth in bank accounts

Area	**Correlation Coefficient**	**t-value**
Rural	-0.007	0.975
Urban	-0.079	0.739

Note: Both the values of correlation coefficient are not significant compared to the t value.

5. Summary and Conclusion

Financial inclusion is the availability of banking and financial services at affordable costs to the disadvantages section of population. Financial services comprise of savings, loans, insurance, credit, payments etc, which are generally provided through banks. The most important part of financial services in a region is typically measured by number of people who have access to bank accounts. The present study investigates the banks outreach among various section of population in the form of savings and deposit accounts during different reform periods. This apart, stage wise scenario of below poverty line population is compared financial inclusion. The total study period (1980 – 2007) are divided into three sub periods – pre reform (1980-1990), reform period (1991-1999) and post reform period (2000-2007). The result shows that reform period was the worst in terms of the growth in bank accounts. Rural area fared better in terms of deposit accounts during pre reform period, while during post reform period highest growth in bank accounts observed in metropolitan areas. As far credit growths of commercial banks are concerned rural credit was severely neglected during the reform period, was revived in the post reform period, but failed hold the growth achieved in the pre-reform period. During post reform period highest growth in bank accounts is observed in metropolitan areas due to the growth in service and manufacturing sector, bypassing the agricultural sector just after the economic reform. In rural areas, high growth in bank accounts was accompanied by reduction in below poverty line population in Kerala, Gujarat, Rajasthan and Haryana. However, in urban areas high growth in bank accounts was accompanied by higher reduction in below poverty line population was achieved in Jammu & Kashmir, Andhra Pradesh, Orissa, Madhya Pradesh and Rajasthan. That is, for other states, the growth in bank accounts is not accompanied by the reduction in below poverty line population across various states. Thus, state wise growth in bank accounts and corresponding poverty scenario indicates weak association between them. Thus, covering maximum number of people under banking services and providing credits without developing inclusive financial systems has failed to lift people above poverty line. As a poverty reduction strategy, developing inclusive financial systems should be given priority, which is financially and socially sustainable.

Acknowledgement

I am grateful to Mr. Anup Saha for his valuable comments. The author is grateful to the participants in the 29th Conference of Bengal Economic Association (BEA). The usual disclaimer applies.

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Appendix

Table 7: State wise scenario changes in below poverty line population

State / Union Territory	Percentage Change in population below poverty line between 1999 - 2005
Northern Region	
Chandigarh	2.27
Delhi	8.06
Haryana	6.37
Himachal Pradesh	6.37
Jammu & Kashmir	6.52
Punjab	40.24
Rajasthan	-6.88
North-Eastern region	
Arunachal Pradesh	-15.87
Assam	-16.39
Manipur	2.16
Meghalaya	-16.57
Mizoram	-0.97
Nagaland	-20.07
Tripura	-11.94
Eastern Region	
Andaman & Nicobar Islands	3.71
Bihar	-1.20
Jharkhand	
Orissa	-28.15
Sikkim	-14.45
West Bengal	12.58
Central Region	
Chhattisgarh	
Madhya Pradesh	-22.43
Uttar Pradesh	-12.25
Uttaranchal	
Western Region	
Dadra & Nagar Haveli	-10.04
Daman & Diu	28.76
Goa	10.30
Gujarat	-0.27
Maharashtra	13.28
Southern Region	
Andhra Pradesh	0.03
Karnataka	20.26
Kerala	12.28
Lakshadweep	0.40
Pondicherry	0.73
Tamil Nadu	-1.20

Source: Planning Commission