



ICICI Bank Extends Reach to Rural India:

Innovative Business Model serves 300 Million People in 600,000 Villages

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ICICI Bank is India's second-largest bank and the largest private bank in the country, having more than US\$50 billion in assets. ICICI Bank provides a wide range of banking products and financial services — investment banking, life and non-life insurance, venture capital and asset management to corporate and retail customers through a variety of delivery channels and specialized subsidiaries and affiliates. Customers of all the groups under the ICICI umbrella are served through roughly 614 branches and global services provided through 14 international offices. ICICI has incubated Financial Information Network & Operations Pvt. Ltd. (FINO). Manish Khera, a key member of the ICICI Bank management team has been tasked with heading FINO and is the founding CEO of FINO.

Rural India has approximately 500 million people who, until now, have had limited access to traditional banking services simply because most commercial banks found it too uneconomical to serve them. These people live in 600,000 odd villages across India's vast terrain and are in the market for banking products that are typically a hundredth the size of a banking product in the United States or Europe and at a tenth the size and cost of a product in urban India. At ICICI Bank, one of the high-focus endeavors has been to create a

What is Microfinance?

Microfinance is the provision of a broad range of financial services, including deposits, loans, money transfers and insurance to low-income households and their micro-businesses.

Microfinance in India

In India, a country of 1.1 billion people, more than 500 million people live on an annual income of less than US\$1000. Though India is the largest market for microfinance in the world, only less than five percent of India's poor have access to microfinance services.

transaction banking system for micro-finance institutions (MFIs); a platform accessible through multiple online and offline channels in the same way a mainstream banking entity might offer. Micro-finance and development-credit institutions have largely catered to the needs of the people without bank access so far — but these have remained largely local, grassroots efforts hampered by their lack of access to technological resources. It is against this backdrop that ICICI Bank decided to explore the possibility of delivering value, at very low per-unit costs, to this largely under-served market in need of financial products and services.

Achieving this goal called for a new and separate business model that enables access to more than half-a-million villages at a tenth of the cost of reaching urban India. This had to be done by partnering with existing local grassroots organizations (in this case MFIs) as a branch-led banking model would not work. No matter how much it was scaled down, the costs would always be too high for it to be a competitive and profitable mechanism for reaching the rural customers. Since the breadth of coverage was also enormous, the micro-finance institutions were best suited to handle the complexities of the local economies they served.

It was clear to ICICI Bank that they had to design a partnership model that would allow each player in the solution focus on its core competence. At the same time, more partners needed to share the risks of doing business with the largely agrarian and monsoon-dependent economies of rural India. FINO, short for Financial Information Network and Operations, was conceived and incubated by ICICI Bank to focus on the information system (IS) and technology piece.

By bringing scale and technology to the "micro" business, FINO could lower costs for local MFIs and simultaneously act as their internal technology department. With FINO's technology resources at their disposal, the MFIs would also be able to increase penetration locally and provide expanded coverage, thereby reducing unit costs.

Partnerships to Share the Effort and the Risks

FINO's clients are based in some of the most inaccessible and remote areas of the country, where availability of basic infrastructure such as electricity, network and connectivity pose a big question mark. Architecting a robust IT platform that ensured foolproof delivery of financial services in a predominantly offline environment was a big challenging task. To succeed in rural India, FINO is working to provide technological solutions in banking and insurance, and especially health insurance, to these under-served communities. To do so, FINO needed to put in place the technology and systems to interact with, for instance, a partner financial institution, a micro-finance institution or a commercial entity — an organization that was already operating in the local villages for a business purpose. The new business model to reach new markets would need to leverage such partnerships in order to conduct business.

Melding Core Banking with Extensive Offline Usage

FINO's platform supports its remote transaction delivery model through the use of smart cards and mobile devices. This decentralization of decision-making around transaction validation and authentication was necessary in order to empower the local "partners" to undertake that function. This led to a solution that provided a secure infrastructure for storing and uploading banking transaction information, and a core platform with a marked stress on offline banking. The core banking solution will be used to securely transfer information from partner-users — micro-finance institutions, non-banking companies, regional rural banks and cooperative banks — back to the lender's information system. End-consumers will use biometric smart cards to conduct highly secure banking transactions over offline hand-held devices. All this will be done at extremely low annual per-unit costs – Rs 25 per account, per year – equal to approximately US\$.60!

The biometric security card that can authenticate the local micro-clients will enable a product offering that includes savings, loans, insurance, recurring deposits, fixed deposits and remittances in association with partner MFIs. FINO will leverage ICICI Bank's partnership with more than 100 such organizations and the bank is expected to take the tally up to 200 MFIs by March 2008.

FINO's Outsourcing Process

FINO realized that the partnership model did not stop with MFIs and other financial institutions, but there was clearly a large role to be played by the technology solutions and services providers as well. The FINO team initiated the outsourcing process in parallel with company formation, fund-raising and business development.

With an aim to arrive at a services contract that was based on world-class best practices and global benchmarks, FINO requested specialist advice from the TPI team to review the contract documentation. FINO was also desirous of weaving in an appropriate service-level methodology into the contract that would facilitate management of relationship with the service provider and enable contract governance on an objective basis.

The FINO team followed the conventional RFP process for inviting interested service providers to act as solution providers for the initiative. A fully transparent methodology of solution evaluation at various stages was adopted to arrive at two final competing proposals.

The final solution that emerged proved highly innovative in all aspects. FINO's contract is with the primary IT outsourcing service provider for the IT infrastructure and management systems. The core banking application which is provided by a leading Indian ISV, runs on the underlying infrastructure and can be securely accessed by MFI users over the Internet. The pricing model is based on a utility paradigm that not only "variablizes" all fixed cost components and enables a risk-reward sharing partnership, but also provides simple and elegant usage from an ongoing sourcing management and governance perspective. FINO gets charged on an all-inclusive, per-account-basis at the end of every month — and there are no other price components in the contract.

The FINO context added a considerable amount of complexity to the situation. Drafting statements of work that captured service operations in the market environment described earlier and balancing those to keep them fair to both the contracting parties was a real uphill task for the team. The balancing act was achieved by creating a comprehensive agreement that gradually accommodates increases in service intensity depending on the end off take by FINO's clients. This adjustability in the services intensity helps FINO prime its deployment pipeline and also allows the services provider the flexibility of dynamic allocation of resources.

Taking into account the lengthy duration of the contract and its associated TCV, the provisions for termination and transition assistance were very critical elements. This coupled with the complexity of three contracting parties — FINO, the services provider and the ISV — and the potential adverse business impact on FINO's clients in case of severance of any of the contractual linkages, made the termination provisions very challenging to deal with. The eventual structure of two five-year contracts with options for two one-year extensions has worked out to the satisfaction of the contracting parties. In the event of premature termination, FINO's interests have been adequately safeguarded with the provision for three-month transfer assistance and a six-month option for temporary extension of services. Another potential solution risk, wherein on termination, FINO could have ended up without a banking application, was decisively addressed by going in for a backup License Agreement with the ISV. Along-with

taking care of the solution risk, this arrangement also provides FINO an unlimited recourse in case of third-party IPR infringements against it.

Arriving at a workable service-level methodology was a difficult proposition given the inherent complexity of the solution and the unique context. In the absence of a clear reference point, force-fitting ready-to-use templates was a non-starter. Moreover, the solution of this nature being a first of its kind for the solution provider as well, there existed no alternate starting points. However, the team went ahead and identified certain critical SLs, critical deliverables and key measures based on the mutual agreement between the parties. These identified parameters will now be monitored for their efficacy in indicating the quality of service being delivered by the service provider. In subsequent review meetings, a final decision will be made on the suitability of the identified parameters for their intended purpose. Once frozen, the parameters will be subject to the best practices of continuous improvement, raising the performance bar ever higher. The utility arrangement has provided a much more balanced look by ensuring the service provider's skin in the game.

Apart from standard system and component availability, latency, resolution times and packet-loss-based metrics, the service level framework includes business transaction service levels that are critical to FINO's operations. TPI worked as an integral part of the FINO sourcing team, designing and incorporating the service level methodology into the final agreement, reviewing the overall contract and supporting the FINO team in final negotiations and conclusion of the deal.

The Future

FINO's standardized and on-demand infrastructure is now beta-operational. FINO's technology and solutions partners are working hard to meet the go-live dates later this year.

FINO expects to provide technology-enabled banking services to two million new customers this year. In the next five years, an additional 25 million people will access financial services through FINO's platform at levels in proportion to their "micro-requirements," and at a cost that is not only attractive for them but also profitable for the lending institutions.

This move has brought ICICI Bank closer to as many as 300 million new banking customers - collectively an enormous scale of customers will provide a base for further expansion as India's rural economies grow and strengthen. ICICI Bank's push to offer services to so many rural communities across India, leveraging the best technologies and biometric security is truly innovative and can serve as a model for other banks with large-scale populations to reach.