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A Blueprint for the Delivery of Comprehensive Financial Services to the Poor in India

by

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Abstract

If access to finance is broadly interpreted as the ability of economic participants (individuals and enterprises) to obtain a broad range of financial services to manage price and other risks, with ease and at reasonable prices, then improving such access can have a strong welfare impact on the very poor. These financial services allow participants to smooth consumption across time and help them tide over the impact of adverse shocks during their life cycle. Access to financial services allows the participants to invest in and benefit from their skill sets. Presence of well functioning financial markets permits participants to generate surpluses for future investments by eliminating the need to self-insure and over-diversify. However, the scenario of supply of formal financial services within India is that, against an estimated demand for credit ranging from $3 to $9 billion annually the formal sector is barely able to provide $200 to $300 million, less than 20% of rural populations have a bank account, against a total of over 600,000 villages there are barely 30,000 bank branches and while products such as health insurance are completely inaccessible to the poor even the most basic life insurance products remain out of reach. This note attempts to articulate a new vision for the scaled delivery of comprehensive financial services to the rural and urban poor of India. The strategies suggested in the document draw heavily on the lessons from previous experiences in this sector both here in India and other international markets. A few Indian banks and financial service providers have already begun work to realise this vision and have found appropriate roles for themselves – the note will try and document some of the significant steps being taken in this regard by ICICI Bank and a few other participants. However, several gaps remain and the note attempts to draw attention to them.

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A Blueprint for the Delivery of Comprehensive Financial Services to the Poor in India

1. Background

The most important issue that we face today as a country is the extreme poverty within which almost a quarter of our population lives and the very vulnerable status of almost an equal number, giving over 500 million people who are forced to live well below the level at which they could become active participants in the larger economy. And, while high GDP growth rates would definitely help reduce this number, the concern is that, causality could actually be working in the reverse direction and that existence of such large levels of poverty and the associated deficiencies in the health status and educational attainments of individuals could actually start to retard growth rates and prevent the economy from realising its full potential. However, while the problem is relatively easy to state, the solutions are hard to discern with clarity, and even where apparent, are very hard to implement in such a large country.

There is a belief that the poor already have a keen sense of the manner in which many of the challenges that they face may be best addressed. It is possible therefore that if instead of trying to push poorly designed free or subsidised services at them, they can be given the means to better realise their aspirations on their own terms. Through an improved access to high quality financial services, they will be able to quickly find their own way out of the "poverty trap" in which they find themselves. Through the means of such improved access, if they have even a small measure of economic independence, even their ability to exert pressure on providers of public services could improve significantly.

Improved access in this context is defined as the ability of economic participants (individuals and enterprises) to obtain a broad range of financial services (including savings, investments, money-transfer across geographies, loans, insurance services and hedging instruments against price fluctuations) suited to their specific requirements to manage price, yield and other risks that affect the income of the household, as also expenditure, with ease and at reasonable prices.

The ways in which the access to financial services impacts vulnerability reduction and growth are complex and multiple.

Access to finance has been observed to result in substitution of high-cost debts, investment in productive assets, expansion of existing business and in value addition to output with a direct positive impact on household income.

Similarly access to finance also has links to improvement in individual productivity by permitting individuals to move to higher levels of consumption for basic items, investment in education and skill building that determines future earning potential, specialisation in a few activities instead of over-diversification and an improvement in risk taking ability.

Finally access may also have positive effects on the local economy through a general increase in wage labour opportunities and better utilisation of surplus labour.

However, the scenario of supply of formal financial services within India is that against an estimated demand for credit ranging from $3 to $9 billion annually the formal sector is barely able to provide $200 to $300 million; less than 20% of rural populations have a bank account (contrasted with a figure of over 100% for urban populations); against a total of over 600,000 villages there are barely 30,000 bank branches and while products such as health insurance are completely inaccessible to the poor even the most basic life and accident insurance products remain out of reach[1]. It is entirely possible that the 500 million people that were referred to earlier have never been to bank, have never bought any insurance product and have been completely dependent on uncertain and very limited supply of credit, savings and money-management services made available by the informal sector at exploitative and usurious rates.

Over the last 50 years several attempts have been made by the formal sector in India to find solutions to these issues. Many of these attempts have resulted in providing only partial solutions but have offered many interesting lessons on which strategies have worked and which ones have not. Around the world, but most importantly in Bangladesh, Indonesia and Latin America, very effective models for the scaled delivery of these services have emerged. This note attempts to articulate a new vision for the scaled delivery of comprehensive financial services to the rural and urban poor of India. The strategies suggested in the document draw heavily on the lessons from previous experiences in this sector both here in India and elsewhere and also incorporates insights from other markets. A few Indian banks and financial services providers have already begun work to realise this vision and have found appropriate roles for themselves – the note will try and document some of the significant steps being taken in this regard by ICICI Bank[2] and a few other participants. However, several gaps remain and the note attempts to draw attention to them.

a. *The Indian context*

Before a strategy for delivery of micro financial services is articulated it is important to be aware of the context in which these services are planned to be delivered. Some the key aspects of the Indian landscape relevant for the subsequent discussion, are as follows:

1. India has a population of over 1 billion people with approximately 70% living in rural areas and the rest living in densely populated urban centres[3].

2. There are 600,000 villages spread out within over 6,000 blocks and 600 districts. The average population per village is about 2,000 people giving about 200,000 individuals per block and 2 million people per district[4].

3. The average size of each household is 5 individuals. This implies that there are approximately 200 million households in the whole country.

4. More than 70% of the total working population is engaged in agricultural activities of which about 80% are small and marginal farmers. More than 90% of the working population falls in the unorganised sector earning very low wages and not covered by any social security net[5].

5. The country is divided into 28 states. There is an enormous amount of variation in the development and growth status between these states. While states like Punjab, Gujarat and Maharashtra demonstrate per capita Gross State Domestic Product of Rs.15000 (USD 300) and above, Bihar, Uttar Pradesh and Orissa have less than Rs.5000 (USD 100). Similar variations can be observed for health and education indicators as well[6].

6. India accounts for a large portion of the world's disease and malnutrition burden. Over one-third of the world's chronically poor live in India. India accounts for 23% of world child death, 20% of maternal death, 30% of tuberculosis cases and 40% of undernourished children[7]. It also has one of the highest rates of low birth weight (LBW) incidence with 67.2%[8] due to growth retardation in the womb.

7. Around 34% of the country's population is illiterate. Although efforts are being made to improve literacy rates, there are major gaps in the areas of universal enrolment and retention of students in schools[9].

8. About 25% of the total rural population do not have access to safe drinking water, 55% of them do not have electricity in their homes[10] and 40 % of the villages in rural India are not connected by metal roads[11].

2. A strategy for universal access to comprehensive financial services

Given the context outlined in the previous chapter, a strategy for universal access to financial services will have to address two key challenges – ubiquity and comprehensiveness of range of financial services. These have been discussed in greater detail in the following sections.

a. Ubiquitous financial services

By ubiquity, it is meant that the financial service is easily accessible to the individual in terms of geographical proximity and the ease with which it can be dealt with. For far too long, ubiquity has been addressed only in the limited sense of proximity to a source of financial service. The other attributes relating to ease of access have been less emphasised. Morduch and Rutherford (2003) use the dimensions of reliable, continuous, convenient and flexible when studying attributes of micro finance from a client perspective.

For instance, ubiquity as an idea has been pursued in India, but through the route of commercial banks opening branches in rural areas and Regional Rural Banks[12]. There are today over 50,000 commercial bank branches, over 100,000 primary agriculture credit societies (PACS), around 12,000 state and central co-operative bank offices and about 15,000 RRB branches. However, this infrastructure has not been able to address the demand for financial services in a comprehensive and satisfactory manner.

The experience of extending financial services through the infrastructure outlined above suggests the following – costs of delivery have been high under traditional models[13] , local information was not sufficiently leveraged (reflected in poor repayment rates and poorly designed products), there was an almost exclusive focus on credit, neglect to align staff incentives to maximise outreach.

Therefore, in order to achieve ubiquity that is meaningful, models of outreach must have the ability to leverage local information while being cost-effective. The two broad strategies that seem to be effective in this regard appear to be:

1. Delivering these services through high quality, private sector (both for-profit and not-for-profit) local financial institutions, broadly referred to as Micro Finance Institutions (MFIs).

2. Building technology enabled low cost direct service channels. These direct service channels would complement services provided by the MFIs.

a.1 Micro Finance Institutions (MFIs)

Given that MFIs are an important means to achieve ubiquity, it becomes important to articulate a vision for MFIs in India as follows:

1. Existence / creation of 200 mature MFIs serving all the parts of the country.

2. Each MFI to operate in 3 districts of the country with an average population per district of 2 million, giving it a total population of 6 million from within which to choose its customers. This gives it a large base for an adequate level of diversification but is sufficiently concentrated so that the benefit of local knowledge and understanding is not lost.

3. Each MFI to have on average 0.5 million customers.

4. Average credit outstanding per customer being Rs.3,000 (USD 60).

5. Each MFI to provide a comprehensive range of financial services to the customer including insurance, savings, credit and derivatives.

If these numbers are achieved, and if each MFI borrower represents a single household, then financial services would be available to 100 million households. Given approximately 5 members per household, the 500 million poor would have begun to have access to formal financial services either directly or indirectly. With USD 60 per customer, the total amount of credit outstanding would go to USD 30 million per MFI and to USD 6 billion across the 200 MFIs. This would meet almost all of the current estimated demand for credit.

Against a requirement of at least 200 MFIs, there are very few MFIs[14] which have achieved a measure of scale-up and most, despite a very good track record of performance, have not been able to increase the size of their operations[15].

The reasons have principally been the absence of several key ingredients:

a. *Adequate quantities of risk capital to provide the degree of coverage required to absorb the risks inherent in this business and adequate debt funds:* Traditional models of MFI financing have tended to exhibit low leveraging capability owing to the organisation-based approach as against an asset-based one. In 2002, an internal analysis by ICICI Bank revealed that despite consistent evidence of viable demand from clients, exposure to MFIs was constrained due to the organisation-based financing model adopted until then. The partnership model pioneered by ICICI Bank attempted to address the following key gaps:

- Separating the risk of the MFI from the risk inherent in the micro finance portfolio
- Providing a mechanism for banks to continuously incentivise partner MFIs, especially in a scenario where the borrower entered into a contract directly with the bank and the role of the MFI was closer to that of an agent
- Inability of MFIs to provide risk capital in large quantum which limited the advances from banks despite a greater ability of the latter to provide implicit capital

The model has been conceptualised and executed with the following key characteristics:

1. Loan contracts directly between bank and borrower

The loans are contracted directly between the bank and the underlying borrower, i.e., it does not reflect on the balance sheet of the MFI (this feature is similar to the SHG-bank linkage model). The MFI continues to service the loans until maturity. In other words, the bank relies on the MFI's field operations for collection and supervision. The key difference then, between this and the financial intermediation model does not lie in the operating methodology (it is in fact identical), but in the manner in which the financing structure has been designed.

This structure primarily attempts to separate the risk of the MFI from the risk of the underlying portfolio. Why is this important? Because when the bank lends to the MFI, it has no recourse to the underlying borrowers. On the other hand, if the bank lends directly to the borrowers without the funds entering the MFI's balance sheet, it has recourse to the borrowers. So, at least in theory, if the particular MFI goes bankrupt or closes down for any other reason, the Bank can appoint another agency to recover the dues from borrowers. In addition, since the loans are not reflected on the balance sheet of the MFI, its requirement for regulatory capital ceases to exist. Therefore, the lending paradigm shifts from being **organisation-based** to being **asset-based**. This shift has crucial implications for rating, pricing and consequent marketability.

2. Alignment of incentives with a first loss guarantee structure

In order to preserve MFI incentives for portfolio quality in the new scenario where its role is closer to that of an 'agent', the structure requires the MFI to provide a guarantee (typically a first loss default guarantee) through which it shares the risk of the portfolio with the Bank up to a certain defined limit. A first loss default guarantee (FLDG) makes the provider of the guarantee liable to bear losses up to a certain specified limit, say the first 10 percent or 20 percent of loss on the portfolio. It is different from partial guarantees where the guarantor is liable for a fraction of losses on the portfolio, say 50 percent of all losses. In terms of incentive compatibility, an FLDG forces the guarantor to prevent any losses at all as it is affected adversely right from the start. The quantum and pricing of the FLDG will reflect the operating capability and maturity of the MFI.

In this model, the MFI collects a 'service charge' from the borrowers to cover its transaction costs and margins. The lower the defaults, the better the earnings of the MFI as it will not incur any penal charges vis-à-vis the guarantee it provides (which also come out of the service charge it levies). Over a longer period of time, returns from the partnership model can thus, permit the MFI to build its Tier I capital through retained earnings. The Bank receives a fixed amount as interest on its loan. It must be noted that the bank accepts a fixed pay-off while passing on the dynamic benefits/ losses of 'higher than expected recovery' and 'lower than expected recovery' (losses limited to the band defined by the FLDG) to the MFI. The asset that the Bank has thus acquired has a risk-return profile that is now similar to a "AAA" asset for which secondary markets are easier to access.

3. Transfer of explicit capital to the MFI through an overdraft facility

Executing the partnership model at scale begs one question – how will MFIs provide the risk capital implied in the First Loss Default Guarantee (FLDG) in large amounts? In other words, how does it resolve the explicit capital issue? ICICI Bank has evolved a very innovative structure that combines the provision of both debt as well as mezzanine finance in response to this challenge. Along with advancing the credit to meet the demand of the clients, ICICI Bank provides an overdraft (OD) facility to the MFI. The OD facility is equivalent to the amount which the MFI is liable to provide as the FLDG. The OD represents funds committed, but not utilised. The OD is drawn only in the event of default. On default, the MFI is liable to pay a penal rate of interest on the amount drawn down from the OD facility.

The OD facility in effect, assumes the character of mezzanine equity permitting the MFI to leverage it for wholesale funding. In this manner, through the OD facility, the bank enables the MFI to provide explicit capital. The bank's own implicit capital allocation remains more or less unchanged as it has to now allocate capital against the OD limit advanced to the MFI. Given that the FLDG is a fraction varying between 5-20 percent of the loan portfolio, the leverage that the MFI is able to achieve improves tremendously. This has implications for MFI profitability and therefore, on return on equity without any real difference in operating methodology.

With this structure that combines the provision of both wholesale funding and mezzanine equity, the limits to MFI growth are purely posed by its capability to grow field operations in a sustainable manner. Financing ceases to be the binding constraint. This can be a key driver of scale for mature MFIs operating in an environment of high client demand.

Given this structure, it is interesting to note that an MFI that expects to have very low rates of default can grow operations even being a 'shell company' with no equity. All it needs is a robust operating methodology and long-term funds to finance the field operation until it breaks even.

With the Partnership structure, ICICI Bank is working with more than 30 MFIs in India accounting for loans outstanding of approximately US$ 150 million. With the traditional financing structure (second model), ICICI Bank's lending to MFIs did not exceed US$ 10 million in 2001-02.

Efforts are on to develop a secondary market for securitised papers to expand the investor horizon and consequently lower the cost of funding these assets on a continual basis. In this regard, ICICI Bank is actively working with Credit Rating Information Services of India Limited (CRISIL), a premier credit rating agency in India, to develop a smooth and scaleable process for rating the underlying customer assets on an ongoing basis.

In partnership with Grameen Foundation, USA and Citi Group, ICICI bank is in the process of forming a Non Banking Financial Company (NBFC), Grameen Capital India (GCI). GCI is modelled on the lines of Fannie Mae and the Small Business Administration Fund[16] in the USA which has served to catalyse secondary markets for new asset classes, in this case micro finance. This entity will provide credit enhancement to micro finance portfolios and enable MFIs to access mainstream capital markets. It would also provide financial advisory services to help more MFIs leverage domestic debt/ capital.

b. Long-term finance to pay for creation of the necessary infrastructure and pre-operative expenses: In order to build a high-quality micro finance operation, investments are required in creating a trained staff cadre and other field infrastructure. MFIs have largely relied on grants and concessional funds to finance this investment. The volatile inflow of these funds has in turn constrained growth. Since there is an underlying business model inherent in the MFI's expansion, there is no reason why it cannot be funded by commercial debt, albeit of a longer term nature than what has been typically available to MFIs. ICICI Bank is now offering its MFI partners long-term finance of a tenure of 3-5 years to meet this need.

c. Well-trained staff in adequate number at all levels: Micro finance, regardless of the model followed, is a very human resource intensive intervention. Most MFIs are in the emerging phase and have high capacity building requirements. MFIs typically recruit locally and provide on-the-job training. If a target of 200 MFIs is to be achieved for the sector, each employing an average of 100 field personnel, this implies that a capability to train 20,000 individuals needs to be built on an urgent basis.

Over the last decade, various resource units specialising in imparting training to MFIs have emerged. These include organisations like Indian School of Micro Finance for Women, Dhan Academy of Micro Finance, M-TRIL, EDA Rural Systems and Bankers Institute of Rural Development (BIRD). Several funders such as CARE, Friends of Women World Bank (FWWB) have also aimed to impart training to affiliated MFIs. In addition, resource centres have emerged at a regional level to impart training to local NGO/MFIs. Examples of this category would be People's Education and Development Organisation (PEDO) in Rajasthan, Centre for Youth in Social Development (CYSD) in Orissa and Mahila Abhivruddhi Society, Andhra Pradesh (APMAS).

The emphasis of training programmes in micro finance has largely been on the social mobilisation aspects and do not adequately stress on other areas such as advanced financial management and evaluation techniques, product design and human resource management.

However, with rapid rates of growth and hence the need for a management cadre for scaled MFIs increasing, there needs to be a systematic training strategy for the sector. MFIs with portfolio sizes in excess of Rs. 250-500 million (USD 5-10 million) need to build internal capabilities in risk management, asset-liability management and other financial aspects of the micro finance business.

The training agenda is currently being implemented through aggregators who could identify and provide mentoring support to MFIs. ICICI Bank has initiated partnerships in Madhya Pradesh, Andhra Pradesh, Karnataka, Maharashtra, Jharkhand, Orissa, and West Bengal. These partners include the Indian Grameen Services (IGS) which is part of the BASIX group of companies and CARE India.

To add impetus to the programme, a corporate volunteering programme has been initiated wherein senior management resources from ICICI Bank have been assigned to mentor MFIs. The employees are placed with MFIs on a purely voluntary basis according to their interests and the MFI requirements to aid the scale up of the MFI. The mentors advise on issues ranging from credit policy, technology, human resources management and risk management.

ICICI Bank plans to establish a national level Financial Services School in collaboration with MicroSave India. The school will impart training to MFI staff and senior management through a network of regional training resources across the country[17] . The training process will be characterised by a combination of class room level teaching in the regional language, field visits and monitoring for a certain period of time.

d. *Technology:* A discussion on technology is very critical for MFIs because it gives opportunities for reducing costs of delivery and process management, besides bringing about transparency in operations. It assumes significance because of the manpower-intensive nature of business (which gives rise to control issues), underlying financial risks and regulatory sensitiveness.

The aspects of the micro finance business where technology plays a key role include Management Information Systems, cash handling, data capture and subsequent management. In order for MFIs to grow rapidly, operations must be supported by robust and scaleable systems. Several providers have emerged to cater to the micro finance market.

The initiatives of ICICI Bank in this area are: creation of rural connectivity in partnership with telecom companies and internet service providers, assistance to emerging MFIs to adopt scaleable MIS solutions, support to research and development on technological devices that can reduce costs of intermediation (low-cost ATM, low-cost computing devices, smart card, POS terminal, mobile and internet-based transaction platforms). In addition, training initiatives will include a focus on the use of technology by MFI staff.

What has been described above are challenges for existing MFIs to increase their scale of operations. However, the challenges of achieving ubiquity also necessitate an increase in the absolute number of MFIs.

Where will the additional MFIs come from? ICICI Bank is pursuing two models that have the potential to create additional micro finance outreach.

Entrepreneur led model: The hypothesis is that micro finance is a profitable activity that will attract entrepreneurs to start MFIs, provided key inputs are made available and initial pre-operative expenses funded. Therefore ICICI Bank's Social Initiatives Group (SIG)[18] offers support to entrepreneurs to start MFIs in underserved areas[19].

While we are still discovering the various elements critical to the success of this programme, following are our key learnings on dimensions along which entrepreneurs need inputs:

- Organisational and staff incentives structure
- Finance related – break even, source of funds, capital structure
- Legal issues - form of incorporation, regulation on various products
- Business plan related - scale, outreach strategy

Corporate partnership: The thinking here is that several corporates (particularly those in manufacturing) often have a significant presence in rural areas by virtue of their plants and projects. At these locations, the corporate often engages in community development activities, typically from a corporate social responsibility approach. Embedding micro finance within the community development activities of these companies provides an additional track to build access[20].

However one significant challenge is that despite serious efforts, the supply of entrepreneurs willing to start new MFIs remains extremely limited. A strong and perhaps worldwide effort would need to be launched to find such entrepreneurs.

Allied services for Credit Deepening

In order for MFIs to sustain growth and meet a larger share of client requirements, certain non-financial interventions may prove crucial.

MFIs have largely relied on providing cash credit which has financed consumption and small production purposes. What would a strategy for deepening financial service outreach to client households entail? This question is most relevant for MFIs who have already attained a large geographical footprint. They need to balance the twin objectives of scale while not losing local information advantages.

Deepening entails:

- Substituting other financial service providers. For example, several micro finance clients continue to borrow from multiple sources. One of the reasons for this is that MFIs have fixed credit limits which might not satisfy the entire credit requirement of the client. MFIs may progressively seek to increase share of client total borrowings by changing credit limits. This is currently observed among mature MFIs in India.

- Meeting demand for non-cash credit. While MFIs have primarily focussed on meeting cash deficits, clients perhaps avail credit for other purchases from traders, shopkeepers etc for products such as grain, durables etc. If MFIs can offer competing financing products, clients may switch borrowing. For example, Spandana offers clients various commodities/durables through its consumer store. Spandana exploits economies of scale to get cheaper rates on its products. This, combined with bundling of credit offers a superior option to clients. Spandana has therefore witnessed a build-up of its portfolio through its store.

- Enhancing enterprise returns through targeted business development services For example, improving returns on livestock rearing through productivity improvement. With a view to impact cattle productivity, ICICI bank has tried to facilitate a partnership between National Dairy Development Board (NDDB) and MFIs to enhance cattle productivity. Some of the areas of intervention are good quality feed and fodder for cattle, proper selection of breed and artificial insemination (AI) to breed high yielding variety of cattle. The relevance of this initiative may be discerned from the fact that a large proportion of micro finance loans is utilised for livestock purchase. Interventions in productivity enhancement in conjunction with experts have the potential to directly translate into increased incomes for the client household.

- In some contexts, the MFI may develop viable ways of delivering products that have high social returns. For instance, in partnership with the Shell Foundation, two NGOs in India are seeking to bundle credit with the sale of smokeless chulhas[21] . While for the NGO/MFI, it represents another use of credit by the household, this is also expected to have impact on indoor air pollution levels and therefore female and infant health indicators.

a.2 Alternate Direct Service Channels

Although MFIs have been recognised as the key purveyors of micro finance in India, one cannot rule out the potential of new service delivery configurations that combine a 'local agent' and various technological aids for ease of transaction. Some models that have made use of the local agent idea in the past include the Life Insurance Corporation of India's use of agents to sell insurance policies and commercial banks' pygmy deposit scheme which used agents for the function of savings collection. The key challenge in developing scaled agent-based models is to be able to control agent fraud and create incentives for the agents that are aligned to the objectives of the provider.

The emergence of connectivity and transaction devices increases the scope for agent-based models. For example, internet connectivity enables third-party agents to offer 'transaction fulfilment' at a non-bank/provider location. For instance, a person desirous of purchasing an insurance policy can avail it from an authorised agent of the insurance company in a village. The process now looks as follows: client chooses the relevant policy and makes payment to agent; agent accepts cash and remits the money through the payment gateway from his/her account. The agent also updates the database of the provider (in this case the insurance company) on a real-time basis. The provider issues the policy online; the agent prints it out and hands it over to the customer. In this manner, the entire transaction loop is closed at the agent location itself without a time lag and without the client having to ever travel or interact with the provider directly. The distinction between the process outlined above and a traditional agent model is the fact that internet connectivity is leveraged to reduce potential for fraud (agent has to update provider databases online and make payments immediately. Lags in this process increase agent risk) as well as reduce transaction costs (agent is responsible for entire transaction, not parts of it).

Similarly devices such as Automated Teller Machines (ATM) s enable the provider to disburse and collect cash at a non-provider location while minimising the risk of fraud. The ATM has the ability to authenticate the customer and update the transaction on a real time basis. The role of an agent in these models lies in assisting the customer through the various steps of the transaction.

The benefit of agent models vis-à-vis other dedicated channels, eg: the rural branch of a commercial bank is also the fact that the agent represents a multiple service channel. S/he can distribute fixed costs of operation over several services. This has implications for channel viability.

The connectivity scenario in India, that is essential to the emergence of new models, is encouraging. Several participants have been engaged in this task.

a. Bharatiya Sanchar Nigam Limited (BSNL) already has around 0.5 million Village Public Telephones in rural India. Based on this, one estimate says that if wireless system with 10 km range is installed at the existing fibre connected rural exchanges; 80-85% of the villages could be connected. About 70% of the Indian land-mass is covered by optic fibre with cellular networks gradually coming up along national highways.

b. Linked to these technologies, companies such as Vortex and Neurosynaptic have built a variety of devices designed to work within Internet kiosks such as ECG monitors, digital stethoscopes and biometric / low cost ATMs.

Two models that combine agents with internet connectivity and other devices that ICICI Bank is currently working on are:

1. **Internet kiosks:** An infrastructure of village-level kiosks is being promoted across the country by Internet service providers, public-private partnerships and agribusiness corporates. Several participants have been engaged in this task. ITC, n-Logue, Drishtee and Development Alternatives (Tara Haat) have built more than 6,000 internet kiosks using technologies such as Wireless in Local Loop (WILL) and VSAT Terminals. By far the most successful of these initiatives has been the one launched by ITC, both commercially, and in terms of number of kiosks on the ground[22] .

   ICICI Bank has partnered with some of these organisations for the creation of a large number of such kiosks. In partnership with these kiosk network owners, ICICI Bank proposes to finance individual entrepreneurs (usually high-school graduates) who own and operate the kiosk. The entrepreneur invests around Rs.5,000 (USD 100) and ICICI Bank finances the remaining, Rs.55,000 (USD 1100) to purchase the operating license and equipment (including a PC, local language software, power backup, web camera and printer) from the Internet service provider. The online applications currently involve connectivity-based services like e-governance, e-mail, Internet chat, agricultural extension, and video conferencing with hospitals for preliminary diagnosis. Given the low investment required in the channel, the kiosks are expected to break even within the first year of operation of the kiosk. In our experience, a kiosk needs a catchment of about 5,000 people to be a financially viable unit with the current applications, translating in to one kiosk in every cluster of four to five villages.

   The strategy is to reach the poor at their doorsteps by delivering a suite of financial services through these kiosks. Currently, financial services have been rolled out in about 900 kiosks by ICICI Bank. Products such as Life & General Insurance (weather insurance, personal accident insurance etc), Investment Services (Stocks, Bonds, Mutual Funds), gold purchase, credit products including micro-loans, agricultural loans, consumption loans and transaction & bill payment services and derivatives for small farmers (coffee options, soybean futures) can currently be delivered through the kiosks.

2. **Credit Franchisee:** Another agent model that ICICI Bank is working on at a block level (kiosk is a transaction platform for an agent at a village/cluster level) is the Credit Franchisee Model[23] . The credit franchisee is envisaged to provide asset-backed loans (auto, gold, fixed deposit) and other financial services. The credit franchisee will be located in places that are likely to be under-served from a financial services perspective, but would not be able to support a branch-based model of outreach in a viable manner. The credit franchisee is an entrepreneur who contributes equity, has a good understanding of the local market conditions, credit needs and credit history of individuals and who is willing to enter into risk-sharing arrangements with the bank.

However, even here several significant gaps remain. A few examples are given below:

1. The 50 kbps, always on connectivity that is needed for various transactions has proved to be difficult to provide at an affordable cost. ITC has used the VSAT route to provide this connectivity but unless their model is generalisable, the cost of the VSAT terminal is such that it may limit the spread of these kiosks only to large villages or those areas that produce particular crops.

2. Even here, as in the case of MFIs, finding appropriately motivated entrepreneurs at the village level and credit franchisees at the block level has proved to be a challenge.

3. While some progress has been made in developing a range of applications that can work in these kiosks, high quality applications and equally importantly the required back-end systems to service clients and partners have proved to be very difficult to find and slow progress is being made. This delays the break-even of the kiosk considerably.

b. Comprehensive Financial Services

Development of well-designed products that cater to various needs (both risk management as well as growth) of the poor is an important aspect of universalisation of access. Much of the work that has happened in India gas been geared towards increasing access to small loan amounts that may be used either for consumption or for enterprise purposes (typically livestock). While this is a critical need, there are gaps in access/availability of other financial services including insurance (life and non-life), investment, remittance and derivatives.

We have examined the scenario for each of these products to identify current status, provider challenges and regulatory issues.

1. Individual Loans

Although the problems of high transaction cost and information asymmetry have been addressed by the group lending mechanism, our belief is that group-based lending need not be permanent structures. The SHG/JLG represents a group of people who have aggregated in order to access a specific service and the promise of continued access is the glue that binds them. However, as a permanent solution, it is still inferior to the individual directly transacting with the bank.

Our experience is that the small amounts of credit available through group-based lending could be insufficient for those who have passed through several loan cycles and require larger amounts of credit. Typically the needs could be for house construction, marriages, education and enterprise expansion. Currently there is no regular source of credit available for amounts above Rs.15,000 (USD 300). There needs to be a mechanism for the members of the group to 'graduate' to being individual clients with access to higher credit limits. Data on borrower behaviour through three or more loan cycles with an MFI could serve as the deciding factor to migrate members to an individual lending design. We envisage designing such product with one of our current partner MFIs.

Besides 'graduating' group members to individual loans, it is also important to experiment with individual lending on the basis of other observables – say education, health status or track record of bill payment. These will provide insights into the design of individual lending programmes. One format to experiment with for individual loans could be to provide dynamic repayment incentives – such that every individual who successfully repays becomes automatically eligible for a larger loan. This might also be a way to 'select' individuals for larger loan amounts.

ICICI Bank is piloting a personal loan product through the internet kiosks at the village level. These loans will be in the range of Rs.5000 (USD 100) to Rs.25000 (USD 500). The kiosk operator, through a risk sharing model, will originate and service the loan. This, we hope, will be able to replace the high cost small sized individual loans that are currently being provided by the village money lender. In this case, the information of the kiosk operator and his ability to use social sanctions for repayment acts as a substitute for the same function that would otherwise have been done by the joint liability group.

ICICI Bank and other banks offer individual loans against gold or jewellery in rural India. Here, the value of the collateral takes care of information asymmetry issues. Since gold is a popular investment in rural areas, the product is popular for emergency loans.

The key challenges in scaling an individual loan programme are:

- Absence of fundamental insights into the question of 'who is a good borrower and who is not?' The reliance has largely been on joint liability groups which intrinsically slow the process of scaling and might not be suitable for larger loan requirements
- Inability to uniquely identify an individual is a constraint. A national ID initiative is a key requirement.
- Absence of credit information sharing between various lenders in any systematic manner, for example through a credit bureau, has resulted in credit histories not being used to make lending decisions.
- Reliance on intermediaries like the local agent and products such as gold loans might impair ability to reach the poorest of the poor.

2. Health Insurance

Vulnerability stemming from illness and inability to manage these risks is amongst the most important dimensions of poverty. Ill health or death of the breadwinner can result in downslide of a household into indebtedness, asset stripping, and acute poverty[24]. The poor suffers a high incidence of morbidity[25], which adversely affects their household budgets in two ways:

- Large amounts of money and resources have to be spent on medical care
- Income foregone during periods of illness.[26]

In order to meet medical expenses and other household consumption needs, the poor often have to borrow funds at very high interest rates from various informal sources such as the money lender, trader, employer, family and friends or sell/mortgage their assets. The possible consequence of this is that these families could be pushed into a zone of permanent poverty and unmanageable indebtedness.

Traditional health insurance schemes cover less than 1% of the poor and did not cover the specific diseases that the poor were exposed to. These schemes were highly dependent on the availability of the rural health system and infrastructure for their successful implementation. Most poor households, especially in rural areas, are unable to avail these schemes as they reside in backward, hilly and remote regions, where neither government facilities nor private medical practitioners are available. The designs were limited in its response to the high incidence of moral hazard and adverse selection which made the schemes very costly and unviable. Even when the household was covered by the scheme, it did not respond to the emergency need for cash in case of a health event.

ICICI Bank is working with a set of innovative models to deliver customised health insurance products through multiple channels such as Kiosks, MFIs and health provider networks in Orissa, Andhra Pradesh, Konkan coast and Punjab. A pilot has being carried out to assess the feasibility of providing insurance through kiosks.

Some of the important models being tested for delivery of health insurance are:

- *Benefit Payout model for critical illness:* A pre-fixed payout is made to the member on the occurrence of any of the pre-listed diseases, on production of a diagnostic report. The product aims to address the immediate need for cash in case of a health emergency, which the poor fulfil mostly through informal loans at very high rate of interest. This model due to its limited monitoring and management requirement is economical while covering a critical risk.

- *Reimbursement model:* Reimburses actual costs incurred on accessing health services from a health provider. It involves an insurer, an aggregator of the insured (or direct individuals), an identified network of health service providers (hospitals, clinics) and a third party administrator (TPA). Under this model the insured is covered for specific predefined illnesses. The TPA identifies hospitals in the catchments region, standardises hospital procedures and ensures quality of services delivered. In case of the occurrence of the event, the insured incurs the initial cost of hospitalisation in any of the identified hospitals and later applies to the insurer for settlement of claims.

- *The Cashless model:* involves the insured (or an aggregator of the insured members), the insurers, the network of providers and the TPA. This product covers health risk most comprehensively and eliminates the need for emergency cash. The insurance company directly reimburses the health provider for the services received to the members. The cashless service provided is critical for the poor as it protects the household from any financial shock due to the medical emergency.

3. Livestock Insurance

A large proportion of the poor rely on livestock rearing as a primary or supplementary source of livelihood. Livestock insurance might achieve two things. It provides insurance against death of livestock ex-post, and ex-ante it improves the risk taking capability of the individual. One hypothesis we have is that with access to a livestock insurance cover, individuals might be more willing to purchase hybrid varieties for which risks and returns are higher.

Design of livestock insurance products must tackle the critical issues which lead to high moral hazard and reduces the viability of the product. These are:

- Identification of livestock during claim settlement – one very obvious reason for fraud traditionally has been that the insurer is unable to ascertain that the livestock insured is the one for which the claim is being settled[27] .
- Basis risk – Designing products which accurately reflect loss of income/ investment in case of death of cattle. This case is compounded in case of hybrid varieties where the income loss should include the actual valuation of the cattle and the high recurring costs incurred.
- Confirmation of cause of death – Traditional products relied on a veterinary doctor to confirm natural cause of death. While this added to supervision costs, it also could not rule out the possibility of collusion.
- New designs of livestock insurance are examining use of technology to uniquely identify the animal, use local institutions such as MFIs to reduce supervision costs and develop products that minimise basis risk. In order to manage risk that the insurer could be exposed to, initiatives such as collaboration with health care providers and provision of livestock vaccines are being planned.

4. Weather insurance

Weather risks affect the poor in two significant ways – it reduces yield on crops that are largely rain-fed and secondly, adversely impacts local wage labour opportunities. In India, the area-based crop insurance programme has been the traditional product for managing yield risk for farmers. However, the effectiveness of this programme has been debatable[28] . It has experienced prohibitive costs due to the field inspections and loss adjustments to be made. As per the report of the Task Force on Agriculture set up by the Government of India, all the crop insurance schemes were ineffective in estimating the probability of risks covered, leading to claim payouts in the range of four to five times of the premium collected. If crop insurance is to give protection at the level of model yields, the premium might be as high as 30 per cent as against the current 1- 3.5 per cent, according to the study by the Task Force.

Index based insurance products, where payouts are based on a verifiable index, provide an opportunity to provide insurance to farmers and the rural poor without incurring the high overheads of loss adjustment and supervision typical of traditional crop insurance products. Since the index provides a transparent mechanism to compute payouts, claims settlement can be immediate. Moreover, it takes care of the moral hazard challenge as rainfall, unlike yield is not affected by the actions of the insured.

The claim is settled on the basis of a transparent index. The index is created by assigning weightages to critical time periods. The past weather data is mapped on to this index to arrive at a normal threshold index. The actual weather data is then mapped to the index to arrive at the actual index level. In case there is a material deviation between the normal index and the actual index, compensation is paid out to the insured on the basis of a pre-agreed formula.

ICICI Lombard General Insurance Company has customised the weather insurance product to cover the following:

- Groundnut, castor and cotton crops in Andhra Pradesh
- Oranges in Jhalawar, Rajasthan
- Apples in Himachal Pradesh
- Wheat in Madhya Pradesh
- Mustard and coriander in Rajasthan

While the above have been crop-specific policies, there is also an interest to offer insurance/ derivatives for rainfall variation even to those who are not cultivators. A segment of particular interest is agricultural labourers who also stand to be affected by rainfall variation.

The challenges faced in scaling up weather insurance outreach are:

- The currently available crop insurance programme is highly subsidised. This makes the pricing of weather insurance products (which are based on actuarial considerations) non-competitive.
- Design of weather insurance products requires historical meteorological data. There is a need to make historical data sets easily available for all those who would need them.
- Claim settlement requires availability of observation infrastructure to capture weather data preferably at the village level that is representative of a particular geographical location. There is an urgent need to deepen this infrastructure.

5. Commodity Price Derivatives

Small and marginal farmers, forming more than 80 per cent of the total farmer population, are exposed to high price uncertainty and are unable to benefit from price movements. This often leads to distress sale during harvest seasons. There exist weak price discovery mechanisms, poorly developed linkages between geographically isolated markets even for the same commodity and no systematic processes and facilities for cleaning, grading, sorting, warehousing and transportation of commodities. This forces lenders to largely ignore the commodity as collateral both pre and post-harvest, significantly increasing the cost of finance and excluding several potential borrowers whose primary collateral base may only be a commodity.

The inability to manage commodity price risk systematically might be manifested in several informal risk coping mechanisms such as investing in low-value crops, over-diversification and low input usage.

Price risk management enhances the predictability of future revenue and leads to informed cropping decision and aggressive investment. Price protection, when combined with yield insurance, could give income protection to the producer.

ICICI Bank has undertaken a concerted effort in the form of National Commodities and Derivatives Exchange (NCDEX) – promoted by National Bank for Agriculture and Rural Development (NABARD), National Stock Exchange, Life Insurance Corporation of India Limited (LIC) and ICICI Bank. NCDEX offers price discovery though tie ups with Agriculture Produce Market Committees (APMC) mandis[29] , Centre for Monitoring India Economy (CMIE) & CRISIL (for commodities not traded in organised exchanges) and dissemination through the web as well as publishing in the mandis.

The exchange represents a serious effort at developing an integrated price discovery process in commodity markets and will attempt to offer the farmer instruments to hedge both pre and post-harvest price risks. Establishment of this exchange along with efforts on warehouse receipts will considerably improve the collateral value of commodities thus making it easier and cheaper for farmers to seek credit.

NCDEX is taking initiatives in market expansion with nation wide trading terminals. The most noteworthy initiative is in the physical logistics segment – the warehouse delivery process. This involves accreditation and audit of warehouses (by collateral managers) where NCDEX issued warehouse receipts are used by the farmer for financing by the Bank while simultaneously hedging their price risk with the exchange.

ICICI Bank is exploring the possibility of collaborating with commodity exchanges, NGOs, MFIs and farmer co-operatives, who could aggregate and facilitate the participation of small farmers in the commodity exchange. The initiative will draw upon international experiences[30] .

The broad challenges of participation in commodity derivatives markets have been identified as being problems related to aggregation of risks from smaller entities, basis risk, lack of local reference prices, low levels of liquidity or absence of markets for certain commodities internationally, low levels of know-how and counterparty risk[31] .

In addition to the above generic challenges, the specific regulatory challenge in India is that banks are currently not permitted to hedge commodity risk[32] .

6. Savings and Investment product

It has been observed that although the demand for a saving product is very high among the poor, few options of saving with the formal sector are available[33] . In fact the poor have been reported to save at negative rates of interest through the informal mechanisms[34] . The Regulator prohibits institutions other than banks and approved Non-Bank Financial Companies (NBFCs), from collecting savings. This concern is justified in the context of schemes and agencies that have defaulted on their commitments to savers.

In order to provide poor households an avenue to save their surplus within the current regulatory environment, one option that ICICI Bank is exploring is to enable clients of MFIs to invest in mutual funds with the MFI/outreach channel facilitating access to the Asset Management Company. The objective is to provide a safe avenue for savings, an ability to earn returns with little or no volatility and to use the MFI/outreach channel as the facilitator and not as 'mobiliser of savings'.

Money Market Mutual Funds (MMMF) typically known as Liquid Funds would be the most suitable product that could be offered through MFI/outreach channel. The MMMF provides a legal savings option, as MFIs/outreach channels can act as agents and sell units of the MMMF to its members. It replicates the features of the savings bank account as it allows for deposits and withdrawals, which is facilitated through purchase and redemption of fund units. Being highly liquid, the members are free to redeem the units and convert them back into money when needed. The reconciliation details for each customer are maintained by ICICI Bank through the MFI/outreach channel. This permits the use of the MFI/outreach channel's collection capabilities while ensuring safety of the savings of clients as the Asset Management Company is responsible for all matters related to the clients' investments.

7. Warehouse Receipt Finance

As discussed earlier, the value of commodity as collateral is not sufficiently leveraged in the Indian agriculture context. Warehouse receipts convert commodity inventories into negotiable instruments. This receipt can then be used as collateral to access financing from commercial banks. Use of warehouse receipts reduce 'physical risk' of the crop and usually lead to lower lending rates.

ICICI Bank is currently offering warehouse receipt based financing for various commodities like oilseeds, maize, raisins, raw cashew nuts, and rubber across the country. The bank is also trying to facilitate the delivery of the product by partnering with Central Warehousing Corporation (CWC), a Government of India owned chain of warehouses.

Warehouse receipts have to be treated as a negotiable instrument[35] under Negotiable Instruments Act, 1882, so that credit can easily be availed against it. Dematerialisation of warehouse receipts would also foster growth of secondary trading and provide depth in the commodity markets.

8. Remittances

The National Commission on Rural Labour estimated that there are approximately 10 million seasonal and circular migrants in the country[36]. The migration rates are extremely high in villages, which are remote, and drought prone. Historically, poor asset less communities, who typically are from low caste and tribes, migrate[37]. A substantial majority of these migrants are absorbed in the unorganised labour market as low wage labourers.

In the absence of a formal mechanism to facilitate the flow of money between the point of destination (migrant) and the point of origin (family), this segment is compelled to resort to high cost informal channels like the labour contractors and mechanisms like the Hundi system[38]. ICICI Bank is trying to design remittance products to cater to the needs of migrants, especially for the inter-state migrants. The presence of local institutions like MFIs in the places of origin and destination would be leveraged to deliver such a product.

Adhikar, an NGO working in Orissa, offers remittance products to Oriya migrants in Gandhidham, Gujarat through its Shramika Sahajoga scheme. Workers are registered as members of Shramika Sahajoga and money transmitted from Gandhidham to their families in Orissa through inter-account transfers. In Gandhidham, the organisation offers recurring deposit and voluntary savings products to the members.

The product that is currently offered by ICICI Bank is an international remittance product that is offered at the village level through internet kiosks. The process of accessing the product is as follows. The sender remits to the beneficiary's ICICI account through an exchange house. The details of the transaction can be viewed online by the beneficiary through the Internet Banking facility available at the kiosks. Once the money is credited to the beneficiary's account, the beneficiary can either collect the remittance at the nearest bank branch or at the kiosk, through an attached ATM.

There are opportunities to design credit products based on remittances that may also be made available at kiosks.

3. Key enablers in building access to financial services

In order to create an environment conducive to maximising access to financial services, some initiatives at the sectoral level are necessary. Some of these have been identified below. Regulators and multilateral agencies have much to contribute in this area.

1. *Unique identifier:* As discussed in the section on products, having a unique identifier is the basis on which initiatives such as credit history tracking and targeting for services such as health insurance can be implemented. This is best done by the Government or agencies such as the Employees Provident Fund Organisation (EPFO) so that the unique ID can be used for other purposes as well.

2. *Credit bureau:* Credit information tracking and sharing enables lenders to provide incentives to those with good credit history and provides a strong deterrent to wilful default. This will also facilitate transition to individual lending programmes over time. NABARD may play an important role in this initiative.

3. *Rural infrastructure:* Investment in certain kinds of rural infrastructure will enable providers to offer financial services with a superior design and convenience to the client. While such investment might be too much to undertake for any one provider, such infrastructure will assume the character of public goods. Relevant examples include computerised weather stations providing real-time weather data and internet connectivity at the village level enabling ATMs and other payment devices.

4. *Regulator support for hybrid models:* Creative responses to the challenge of access to financial services will require experimentation with several delivery formats. Regulators including the RBI, SEBI and IRDA must encourage providers to carry out pilots in order to better address the challenges. Learnings from these pilots may be actively disseminated.

5. *Focus on urban micro finance:* Most of the micro finance outreach has been achieved among the rural poor. There is limited understanding/insights on expanding access to financial services for the urban poor. Some of this may be attributed to lack of 'incentives' for formal providers in working with the urban poor. For instance, finance for urban poor housing does not qualify for priority sector benefits.

6. *Discontinuation of direct subsidies:* Subsidising financial services directly (either through interest rate caps or premia caps) blunt incentives of providers to innovate in product design. A case in point is the crop insurance product where the subsidised Government programme has resulted in very limited participation from the private sector. Subsidy may be best channelled towards public goods as outlined before.

4. Advancing thinking and practice in Micro finance

It is ICICI Bank's belief that evaluation and experimentation hold the key to design of models with the potential for scale. In order to institutionalise these aspects, ICICI Bank has two key initiatives – the Social Initiatives Group and the Centre for Micro Finance Research.

The Social Initiatives Group

The Social Initiatives Group (SIG) of ICICI Bank works with a mission to build the capacities of the poorest of the poor to participate in the larger economy. It is a grant making group that identifies and supports initiatives designed to break the intergenerational cycle of poor health and nutrition, ensure essential early childhood education and schooling as well as access to basic financial services. Thus, by promoting Early Child Health, catalysing universal Elementary Education and maximising access to Micro Financial Services, ICICI Bank believes that it can build the capacities of India's poor to participate in larger socio-economic processes and thereby spur the overall development of the country.

The SIG works by understanding the status of existing systems of service delivery and identifying critical knowledge and practice gaps in their functioning. It locates cost effective and scalable initiatives and approaches that have the potential to address these gaps and supports research to understand their impact. This is undertaken in collaboration with research agencies, Non-Governmental Organisations (NGOs), companies, government departments, local stakeholders and international organisations. In this process, the SIG builds long-term relationships with suitable partners and works actively to improve their efficacy. The strategies so developed are mainstreamed to ensure scale of impact.

The SIG has an interactive portal the www.icicisocialinitiatives.org website which houses three micro sites on each of the focus areas of SIG. The Micro Financial Services micro site is aimed at the following:

- Bringing together participants in the debate issues around access to financial services. Interactive features include discussion boards and facilities to post papers, articles or other resources.
- Publishing research related to innovations and significant problems within the identified thematic areas.
- Enabling online application for funding.

The Centre for Micro Finance Research

The Centre for Micro Finance Research aims to catalyse and support empirical research evaluating the impact of access to financial services. The Centre will support research initiatives aimed at understanding innovations and designs that have the potential to overcome information asymmetries characteristic of this market and expand access to financial services for under-served segments.

The CMFR will engage with researchers and policy makers on issues pertinent to the deepening of the financial sector in India with special emphasis on micro finance and rural financial markets. Additionally, it aims to develop expertise in the evaluation of social programmes allied to micro finance. The centre will be established in association with the Institute of Financial Management and Research (IFMR) at Chennai, an academic institution closely affiliated with and sponsored by ICICI Bank.

5. Conclusion

Access to financial services for the poor is a critical part of the growth and development process of any country. In order to achieve rapid advances in providing access, efforts of several players are required. ICICI Bank's own approach attempts to build natural partnerships in the pursuit of universal access to financial services.

Ideas and collaborations are keenly sought, specifically in the areas of:

1. Design of new products for micro finance clients
2. Design of individual lending methodologies
3. Investments in training and technology
4. Participation in providing mezzanine finance to MFIs under the partnership structure
5. Advisory support for micro finance entrepreneurs
6. Credit bureau design
7. Micro finance programme evaluations

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2 ICICI Bank (www.icicibank.com) is India's second largest bank and its largest private sector bank with a significant presence in Retail Banking, Commercial Banking, Project Finance and Financial Markets and through its subsidiaries in Life Insurance, General Insurance, Investment Banking and Venture Capital. ICICI Bank has recently built a significant presence in the rural and micro finance segment in India. It is a comprehensive provider of services including credit, insurance (life, accident, health and weather), remittance and investment products in rural India with an outreach to over 500,000 rural and poor households. The business is being scaled up to cover new geographies and extend a broader range of financial services. ICICI Bank's Social Initiatives Group (www.icicisocialinitiatives.org) is an action-research team whose micro finance practice aims to maximise access to basic financial services for the poorest of the poor.

3 There are 5000 cities in India with each having a population of over 20,000 individuals.

4 There is an enormous amount of variation in the size of each village across the country with over 50,000 villages having fewer than 500 people. (Census 2001)

5 Census of India, 1991

6 Census of India, 2001

7 WHO 2000, The World Bank 1999

8 National Neonatology Forum (NNF), 1997

9 Only about 45% of the students who enrol into grade I complete the elementary cycle of education (8 years of formal education). In addition, a large proportion of the students who complete the cycle do not achieve the desired educational competencies.

10 Sadanand A. Shetty "Blueprint for a new rural India", Hindu Business Line, March 29, 2004.

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12 In an effort to provide credit to the poor from institutional sources, the RRBs were established in 1975. It was thought that these banks would combine the rural focus of the cooperatives with the business orientation of the commercial banks, to make credit widely available to rural India's disadvantaged communities. Nitin Bhatt and YSP Thorat, "India's Regional Rural Banks: The institutional dimension of reforms", Journal of Microfinance, Vol 3, no. 1

13 The total accumulated losses for RRBs till November 2002 is around Rs. 10347.5 million (USD 206.95 million) (for 29 loss making RRBs in 14 states) www.indiastat.com Lok Sabha unstarred question no.832

14 There are approximately 30 mature MFIs with a combined outreach of less than 3 million households.

15 The MFI sector has together cumulatively disbursed funds approximating Rs 3000-3500 million (USD 60-70 million). Bindu Ananth, Soju Annie George, "Scaling Up of Micro Financial Services: An Overview of Challenges and Opportunities", Working Paper Series, icicisocialinitiatives.org, August 2003

16 Fannie Mae is the largest source of financing for home mortgages in USA. (www.fanniemae.com). SBA deals with small _business financing (www.sba.gov)

17 In order to get a complete understanding of the training needs of the microfinance sector, ICICI Bank is commissioning a Training Needs Assessment involving key players of the sector (wholesale lenders, policy makers) and a sample of MFIs representing the various stages of growth. The assessment, being conducted by MicroSave India, will also try to understand the training resources currently available and their capacities.

18 The Social Initiatives Group is a not-for profit action research group within the bank working on the specific focus areas of Early Child Health, Elementary Education and Micro Financial Services. (www.icicisocialinitiatives.org)

19 KAS Foundation is an MFI supported by SIG under this programme. It started its operations in 2003 and is currently reaching to 75,000 clients in Orissa and Chattisgarh. SIG is providing a combination of technical and financial assistance.

20 The SIG has partnered with the Jindal Vijayanagar Steel Company (JVSL) and a resource partner to implement this model in Bellary district of Karnataka. The JVSL Foundation, in this case, is the MFI equivalent.

21 Traditional chulhas are firewood stoves that are predominantly used in almost all rural households for cooking purposes.

22 ITC's International Business Division has conceptualised the e-Choupal as a chain of Internet kiosks to facilitate procurement of specific commodities. These kiosks are connected through VSATs and are managed by the farmers, selected from within the community and trained, known as 'Sanchalaks'. Each kiosk is a part of a hub and spoke model with the ITC Procurement centre as the hub and the e-Choupals as the spokes. The investment in each kiosk is around Rs. 0.25 million (USD 5000). At the kiosks, the 'Sanchalaks' help the farmers readily access the different agricultural crop-specific websites that ITC has created in the relevant local language.

The farmers can learn on-line the best farm practices for their crop, the prevailing prices and price trends for the crop in the Indian and world markets, and the local weather forecast. Moreover, if the farmer decides to sell his goods in the ITC procurement centre, the kiosk operator issues him a referral slip, which the farmer uses to sell his goods in the centre. As a direct marketing channel, virtually linked to the mandi system for price discovery, e-Choupal aims to eliminate wasteful intermediation and multiple handling. It currently has 4700 installations covering 28,000 villages in 6 states (www.itcportal.com)

23 While the number of villages per block varies, on the average this number is around 100.

24 Risk and Vulnerability, 1999/2000, World Development Report.

25 67% of respondents state that they or their family members have experienced frequent illness at least once in the past two years, while 20% state they have experienced chronic illness and another 19% sudden illness. Social Risk Management Survey 2003, Andhra Pradesh

26 ibid

27 Traditional cattle insurance products attempted to control such fraud through techniques of ear tagging of the cattle. This mechanism allowed a high degree of fraud.

28 Parchure, 2003

29 Mandis are markets where trading and auctioning of agriculture and agri-related produce takes place. Farmers typically sell their produce to licensed traders who in turn sell it to wholesalers.

30 Examples –include Coffee futures and options through exporters in Guatemala; Wheat, maize and soya options in Mexico; Cotton futures and options in Uganda. United Nations Conference on Trade and Development, "A survey of commodity risk management instruments", April 1998

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35 A fully negotiable warehouse receipt is the most liquid type. It can be successively negotiated by endorsement, without returning to the warehouse operator. Jonathan Coulter, G. Ramachandran, "A strategy for development of warehouse receipt system for agriculture in India", 2000.

36 Khandelwal, Rajiv & Katiyar, Sudhir,' Between Two Worlds ', Humanscape, March 2004

37 Rao, Laxman & Deshingkar, Priya,' Labour on the Move', Humanscape, March 2004

38 In India, ESCAP (1986) estimates the level of unrecorded remittances from migrant workers in Kerala to be in the region of 40 percent of total remittance. Kardar, 1992; Kazi, 1989; Saith, 1992