



Government of Nepal

Tel. No.: 4259837
4259804

MINISTRY OF
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PROJECT ADMINISTRATION AND FINANCIAL MANAGEMENT REPORT
**NEPAL: RURAL FINANCE SECTOR DEVELOPMENT
CLUSTER PROGRAM I**
(JANUARY-MARCH 2010)

PREPARED BY

ECONOMIC AFFAIRS AND POLICY ANALYSIS DIVISION
MINISTRY OF FINANCE

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Abbreviations

ADB	Asian Development Bank
ADBL	Agriculture Development Bank Limited
AFMS	Account and Financial Management Specialist
CEO	Chief Executive Officer
CTA	Chief Technical Advisor
CBS	Core Banking System
DGM	Deputy General Manager
GBB	Grameen Bikas Bank
HRIS	Human Resource Information System
HRMD	Human Resource Management Division
HRMS	Human Resource Management Specialist
IT	Information Technology
KPIs	Key Performance Indicators
MOF	Ministry of Finance
MS	Marketing Specialist
NBA	Nepal Bankers' Association
NBTI	National Banking Training Institute
NRB	Nepal Rastra Bank
PPTA	Project Preparatory Technical Assistance
RFSDCP	Rural Finance Sector Development Cluster Program
SFDB	Small Farmers' Development Bank
STI	Second Tier Organization
TA	Technical Assistance

1. Summary

1. Implementation of Rural Finance Sector Development Cluster Program I (RFSDCP I) started in November 2006 and series of activities/initiatives started after loan effectiveness on achieving intended goals. The project consists of five components with vivid results in all five components. The Government withdrew from refinancing and direct provisioning of credit to major RFIs, including Agricultural Development Bank Limited (ADBL). The Government phased-out priority sector lending scheme while continuing deprived sector lending. Rural finance outreach is steadily improving and clients served by Rural Finance Institutions (RFIs) have reached to over 1.8 million savings clients and 1.5 million loan clients, an increase from 0.9 million savings clients and 640,000 loan clients in 2004. Major RFIs¹ have achieved operating self-sustainability and financial self-sufficiency of 95% or above.

2. There has been improvement on capacity of the Nepal Rastra bank (NRB) to regulate and supervise RFIs. National Banking Training Institute (NBTI) was established with leading commercial banks as promoters with mandate to build the capacity of RFIs. Most RFIs are adopting BASEL II standards. ADBL, all Microfinance Development Banks (MDBs) [except Grameen Bikas Banks (GBBs) and two apexes: Rural Microfinance Development Centre (RMDC) and Small Farmer Development Bank (SFDB)], about 27 Financial Intermediary NGOs (FI-NGOs), over 1,000 rural Savings and Credit Cooperatives (SCCs) and 100 Small Farmers Cooperatives Limited (SFCLs) are providing savings, insurance and remittance services to their clients.

2. Component Outputs

3. RFSDCP is aimed at (i) ensuring sustainable access of rural households to institutional financial services, and (ii) encouraging private sector participation in the RF sector. The objective is to develop a sustainable RF system to generate income and reduce poverty of rural households. Considering the comprehensiveness of sector reform, and medium-term approach to institutional reforms, RFSDCP was structured in two sequential subprograms under the program cluster modality. The objective of subprogram I was to develop an enabling RF sector framework through policy, legal, regulatory and institutional reforms. As a continuation of subprogram I, subprogram II aims at promoting enabling sector environment, expanding sound RF outreach, and enhancing private sector participation in RF. The processing of subprogram II started since mid 2009 is at the final stage of appraisal.

4. The program components of RFSDCP are (i) policy reforms to create an enabling RF sector environment, (ii) restructuring and reforms of RFIs, (iii) supportive legal and regulatory framework, (iv) sector capacity building, and (v) product and process innovations. The policy reforms are to deregulate and liberalize RFIs to limit Government interventions and to increase private sector participation. RFSDCP supports fundamental reform and restructuring of the major RFIs, including the ADBL for commercialization and, eventually, privatization.

5. The programme emphasizes on consolidating fragmented RF regulatory framework, initiating commercialization of RFI operations, and upgrading sector capacity. The ADB provided a loan of \$56 million from the Asian Development Fund with a loan term of 24 years, including a grace period of 8 years at interest rate of 1.0% during the grace period and 1.5% thereafter.

¹These RFIs are Microfinance Development Banks except Grameen Bikas Bank (GBBs), financial intermediary NGOs, some Savings and Credit Cooperatives (SCCs) and Small Farmers' Cooperative Limited (SFCLs)

6. Implementation of RFSDCP I started in November 2006 and will be completed in June 2011. The programme consists of three components: programme loan, programme grant and technical assistance. The program loan was released in two tranches over 2 years. The first tranche of \$40 million was released upon loan effectiveness, while the second tranche of \$16 million was about 12 months after the first tranche.

7. The Ministry of Finance (MOF) is the Executing Agency. As the Implementing Agencies, ADBL, Nepal Rastra Bank (the central bank), and Small Farmers Development Bank has set up program implementation units. MOF has constituted a program steering committee for interagency coordination, comprising the program implementation unit directors and representatives from MOF and other Government agencies.

8. ADB will provide a grant of \$8.7 million from its Asian Development Fund resources to support the Government's RF sector reform efforts by facilitating institutional reform and restructuring of key RFIs, and improving sector capacity and governance. The Executing and Implementing Agencies, as well as the implementation arrangements, for the project grant are the same as the program loan. The expected closing date of the grant is 30 June 2011.

9. A discussion on status of component outputs of RFSDCP I as of March 2010 follow hereunder.

2.1 Favorable Policy Environment

10. Aligned with the Government's financial sector reform strategy, the program focused on creating a favorable policy environment. Some of these initiatives were establishment of a supervisory and regulatory system for RFIs, divestment of NRB shares in RFIs (GBBs) to legally defined level², phase out of government ownership in the technically insolvent RFIs and discontinuation of setting interest rate ceilings to ADBL and SFDB. This implies that there has been substantial progress in creating favorable policy environment.

11. RFSDCP has supported towards financial reforms. These includes ensuring full enforcement of debt recovery law for willful defaulters; promoting lending from formal and semiformal RFIs to CBOs; divesting the Government shares and increasing participation of the private sector in ADBL and SFDB; and gradual discontinue of the Government interventions in ADBL and SFDB to implement financially or economically unsound concessions, write-offs, or waivers.

12. In order to enhance access to financial services through improved institutional coordination, supervision and regulation from formal and semiformal RFIs³, NRB has drafted microfinance act consistent to Microfinance Policy 2008. Government is in a process to gradually phase-out its ownership on three state-owned commercial banks and GBBs⁴. Government phased-out priority sector lending requirements for commercial banks while expanding the scope of deprived sector lending requirements⁵.

²The Nepal Rastra Bank Act, 2001 restricts NRB shareholding up to 10% of the equity of a financial institution.

³Fiscal year 2008 budget speech; semi-formal MFIs include approximately 4,500 microfinance NGOs and SCCs.

⁴As part of its ongoing reengineering initiatives, NRB has completely withdrawn its ownership in three GBBs and partially withdrawn its ownership in one GBB.

⁵Monetary Policy 2009 states that commercial banks, development banks and finance companies are required to invest 3 percent, 2 percent and 1 percent of their total loan portfolio in deprived (i.e. rural finance) sector under Deprived Sector Lending requirement.

2.2 Institutional Restructuring and Reforms

13. As discussed already, institutional restructuring and reforms mainly relates to the restructuring and reforms of ADBL, SFDB and GBBs. A discussion on activities started under this component during the reporting period follows hereunder.

2.2.1. Agricultural Development Bank Limited

14. RFSDCP supported reform and restructuring of ADBL⁶ which focused on its transformation into a viable and efficient RFI relevant to enhance access to finance to un-reached and contribute to poverty reduction. The restructuring under RFSDCP focused on progressive divestment of Government shares of ADBL which has been instrumental on improving the performance and driving it towards commercialization and eventually creating environment for privatization. The restructuring of ADBL is detailed in ADBL Restructuring Plan (ARP)⁷ Implementation Guide. Important reform outputs are: divestment of Government shares to legally defined level under the Banks and Finance Institutions Act (BFIA) 2005, initiation of the initial public offering (IPOs), completion of a voluntary retirement scheme, and attainments of viable operations by meeting performance indicators and critical implementation targets set under ARP.

15. There has been several reform initiatives started in ADBL since November 2006. The government began the process of recapitalization of ADBL since May 2006 through the conversion of the then outstanding loan of the government with ADBL to preferential shares and injecting additional capital by subscribing more preference shares subject to ADBL's ability to meet agreed performance benchmarks⁸. The Board of Directors (BOD) of ADBL has been constituted in accordance with BAFIA requirement, the Company Act and the Articles of Association. The efforts however suffered due to frequent change in BOD pursuant to changes in government due to political instability.

16. A team of three consultants: Human Resource Management Specialist (HRMS) and Account, Finance Management Specialist (AFMS) and IT Programme Manager under grants and six consultants: Commercial Banking Specialist/Chief Technical Advisor, Treasury Specialist, Risk Management Specialist, Business Process and Portfolio Management (BPPM) Specialist, Trade Finance Specialist and Training Specialist under TA 4857 NEP are assisting ADBL to enhance its financial, operational and management capacity on different aspects. Consultants has supported on different aspects of ADBL management during the reporting period. These activities are summarized hereunder.

17. During the reporting period, CTA working under TA 4857 NEP mainly mentored the performance of domestic consultants procured both under grants and TA to assure quality of outputs produced. CTA worked with IT Division, especially IT Programme Manager to support implementing CBS project, identifying functional stream training courses, preparing internal payment procedures for CBS installation, worked with HRM Division in upgrading HR management policy.

18. During the reporting period, HRM Specialist (HRMS) worked with HR Division to prepare the HR policy and HR plan, worked with the HR working group to prepare the job descriptions, provide candid opinion on 'Staff Rules Amendment Task Force' as a member, advised Training Specialist on designing HRM training, training for trainers and

⁶ADBL was founded as the Agricultural Development Bank of Nepal (ADBN) under the ADBN Act, 1967 with the objective of contributing to developing agriculture and improving living standards of rural population.

⁷ADB. 2006. Report and Recommendation of the President on the Proposed Sector Development Program Cluster of Loans, Asian Development Fund Grant, and Technical Assistance Grant for Nepal: Rural Finance Sector Development Cluster Program Manila, Supplementary Appendix F.

⁸Progress since then has been the private placement of 5% of ordinary shares to Group NB shareholders and the bank is now preparing for the issues of 30% of ordinary shares for public subscription, and has appointed ACE Development Bank as issue manager in order to bring issue capital to NRs. 2.5 billion.

impact evaluation of training and discussed with CEO and DC, HR regarding implementation of proposed Organization Structure, visited with HR, DC and discussed on implementing new organization structure and functions with DC, BMD and managers of some branch offices and assisted the training specialist working under TA 4857 NEP to design training utilization record/survey form and provided required advice on training plan and career paths. Further, HRMS participated in a number of meetings with ADBL management, staff unions, etc. to discuss on various issues related to reform on HR management system.

19. Account and Finance Management Specialist (AFMS) finalized accounting policy, inter-branch reconciliation system, payment procedure manual and drafted accounting (deposit account) manual and provided technical inputs to IT department programmer to develop software for account reconciliation for reconciliation of previous year transaction under Account Code 17 and the software has been brought into implementation⁹. Accounting policy and payment procedure manual has been approved by the Board and has come into effect. New Reconciliation System under centralized approach suggested by the specialist during June 2009 is not adopted in its basic form and some of the recommendations such as establishing specific code for reconciliation have been agreed upon under Account Code 17. The accounting (deposit account) manual is at the final stage of obtaining immediate approval and implementation.

20. Under TA 4857 NEP, specialists in Management Information System, Treasury, Risk Management, Business Process and Portfolio Management, Trade Finance and Training were mobilized. The team worked with concerned divisions of ADBL and implementing various activities outlined in the inception report.

21. MIS Specialist examined the MIS to propose modifications to make it more effective as a business management tool.

22. BPPM specialist has worked on business processes and problem account management. BPPM specialist supported the working group formed to upgrade credit policy and procedures and to examine how to organise all credit operations into a single division and there has been constant consultation towards this direction. In this regards, an operational framework for business process and portfolio management has been worked out and work has been started towards manual preparation. The work is yet to be initiated on training preparation and delivery.

23. Throughout the reporting period, Risk Management Specialist attended Central ALCO meetings regularly, agreed modifications needed in policies and procedures for ALCO and LPMC operations, worked on revision of risk management policy statement and an upgrading of risk management manual, and contributed to resuming LPMC meetings which was not held in ADBL for more than a year. Towards this direction, ALCO and LPMC framework and format has been prepared and process has been started on procedure revision as well as manual preparation. Actual training and trainers preparation is yet to be started.

24. Trade Finance Specialist (TFS) prepared an initial working paper, discussed it with TA Team members, DC Branch Management and DC Credit divisions and then with the CEO and urged caution on early offer of trade finance to public in order that manual be prepared and staff be trained in depth. TFS also assisted IT Division with the preparation of letters of credit needed for the procurement of goods and services for the CBS

⁹The software is in process of revision to include the matching codes. The matching codes are generated in the Transaction Recording System. The New Reconciliation System under centralized approach suggested by the specialist during June 2009 is not adopted in its basic form. Some of the recommendations such as establishing specific code for reconciliation have been agreed upon under Account Code 17. Directive incorporating new mechanism is yet to be circulated by the Department.

installation. The TFS finalized the strategy for the trade finance awaiting final approval from ADBL management and BOD and started to prepare the operational manual for handing guarantee and letter of credit business.

25. Training Specialist (TS) reviewed the capacity in the ADBL training units and work on career development curricula has been in abeyance awaiting adoption of a revised HRM Policy. It has been expected that the HR policy will define the career paths, minimum entry criteria and rules for recruitment and promotion which is required for the design of the curriculum. In the meantime, TS designed an upgraded training of trainers course and implemented in the RTC Manglapur. TS also designed the training impact assessment procedures and actual assessment of training impact started however actual analysis delayed due to lack of enough sample size.

26. Treasury Specialist (TrS) recommended some modification and additions to his predecessor's plan, worked on liquidity management and drafted a strategy and policy statement now being discussed with the bank. The TrS prepared the treasury policy for ADBL, worked with Treasury division and other concerned on risk management system and at the final stage on manuals and training materials preparation on treasury management.

2.2.2.Small Farmers Development Bank

27. The program targets to strengthen SFDB and SFCLs to supplement ADBL's efforts to meet the agriculture credit needs of small farmers in areas where commercial banks do not consider their operation to be viable. In addition, transformation of SFDP into SFCLs and their links with SFDB was redesigned for expediting outreach to small farmers and local communities. The SFDB Restructuring Plan was prepared based on the diagnostic review of SFDB¹⁰ which seek to enhance the viability and outreach of SFCLs with specific key performance indicators (KPIs). The restructuring assistance was prioritized strengthening SFDB's microfinance and banking operations, staff capacity building and accounting and auditing. The reform output targets was the adoption of SFDB restructuring plan, initiation of restructuring process, and partial divestment of Government shares to legally required level as set out in the BFIA. Series of reform initiatives was started in SFDB since November 2006 as part of implementation of the SFDB restructuring plan.

28. SFDB's reform initiatives can be broadly grouped into three viz. automation of MIS, restructuring and strengthening of SFCLs, and institution development of SFDB. A Microfinance and Banking Operation Specialist (MBOS) financed under programme grant is providing technical support to SFDB since February 2009. During the reporting period, MBOS supported SFDB on the procurement of the MIS Hardware and Software including the evaluation criteria and contract awards, strengthen SFCLs and documented the financial products offered by SFCLs. SFCLs are provided inputs to prepare and implement the business plan and prepare the financial products suitable to the SFCLs.

29. SFDB is gradually using outputs produced by MBOS for its enhanced operational and financial performance. To start with, lending guidelines is used for on-lending to seven non-SFCLs. It is implementing SFCL restructuring plan and using the manual on business planning and institutional assessment for day to day operation. It has been planning to implement a pilot project to expand the microfinance services in hills.

30. MBOS started work on compiling the operational manuals and guidelines as well as training module on governance, financial management, operational risk management,

¹⁰ADB. 2003. Technical Assistance to the Kingdom of Nepal for Strengthening Selected Rural Financial Institutions (Co-financed by the Government of Germany). Manila (TA 4259-NEP, for \$515,000, approved on 16 December 2003).

delinquency management, new product development, business planning, etc. and identify the gaps requiring immediate improvement in order to prepare SFDB to move towards sustainability.

2.2.3. Grameen Bikash Banks

31. There is no significant work done on restructuring of GBBs during reporting period. NRB divested its share in four (Eastern, Central, Western and Mid-western) out of the five GBBs and divestment of the share of Far Western GBB to the level defined in the NRB Act is currently pending despite that Monetary Policy of GON announced by NRB for FY 2009/10 has outlined divestment of far western GBB and its privatization as one of the activities.

2.3 Supportive Legal and Regulatory Framework

32. During the reporting period, the NRB received feedback on draft microfinance act, approved from the Microfinance Act Drafting committee in NRB and eventually approved from NRB BODs. NRB BOD has approved the act with few comments to be incorporated in the act. NRB is at the final stage on forwarding the draft microfinance act to MOF for further work.

2.4 Sector Capacity Building

33. National Banking Training Institution (NBTI) has recruited CEO, prepared draft business plan related to course curriculum, materials, library, training of trainers, and equipment. NBTI has started actual training course on bank operation and management while working to obtain licence from Ministry of Education to operate as an instructional institution. NBTI has started recruitment of the support staff. During the reporting period, CTA working under TA 4857 NEP assisted NBTI Board towards its institutional development.

34. Process is underway for the strengthening of the operational process in Debt Recovery Tribunals (DRT) and Credit Information Bureau (CIB), especially to expand their scope of support on microfinance sector.

2.5 Product and Process Innovations

35. There has been no significant work on product and process innovations during the reporting period. The need to revisit and re-define scope of product and process innovation component, conduct training on market led-approach to new product development, technical support to new product development and process refinement and piloting of crop insurance scheme.

3. Program Management

36. PMU appointed Project Coordinator/Rural Finance Sector Specialist (PC/RFSS) continued assisting Program Director to coordinate, monitor, and supervise overall program implementation in cooperation and coordination with other staff in the PMU. A system of conducting monthly and quarterly review meeting with the consultants was instituted in ADBL and SFDB. PC/RFSS regularly contacted PIU in ADBL, SFDB and NRB in addition to review of project performance consistent to the PAM and RRP.

3.1 Project Expenditures

37. RFSDCP comprises of a program loan of \$56 million and a project grant of \$8.7 million, supplemented by a TA grant of \$500,000.

38. Government used program loan to recapitalize ADBL through cash subscription of additional preference shares, which has been divided into redeemable and irredeemable shares. The project grant is being used to finance (i) consultants inputs for RFI restructuring; (ii) procurement of CBS for ADBL and MIS for SFDB, (iii) office equipment for RFIs, and (iv) a vehicle.

39. Project steering committee has agreed to re-allocate original allocation of project budget under consulting services thereby reducing the allocation on consulting services and increasing the allocation under equipments and training. Table 1 provides information on allocation of project grant and expenditure as of June 2009.

Table 1: Project Expenditures as of March 2010

Number	Items	Allocation (\$)	Expenditure as of March 2010 (\$)*	Remarks
1	Equipment	5,152,900	181,065	
2	Vehicle	25,300	-	
3	Training	490,800	218,945	
4	Consulting services	2,555,700	382,362	
4a	International consultants	648,000	90,000	
4b	National consultants	1,907,700	292,362	
5	Project Management Support	61,000	33,136	
6	Unallocated	414,300	-	
		8,700,000	815,508	

Note: Advances amounting US\$ 250,000 and US\$ 25,541.46 has been deposited in the second generation imprest account in ADBL and NBA respectively.

* The expenditure as of March 2010 is indicative and accurate information is yet to be compiled.

40. The project is rather slow on expenditure on grant. Only a fraction of the project grant has been used as of the March 2010.

3.2 Procurement

41. Using the allocated project grant, the program is procuring goods, related services and works. The major share of grant resources are allocated for the procuring the CBS in ADBL and automation of MIS in SFDB. Other procurement includes procurement of equipment, vehicle, consulting (national and international) services and project management support.

3.2.1. Procurement of CBS in ADBL

42. Process continued on procuring CBS in ADBL adopting international competitive bidding, the procurement process was finalized and agreement signed between ADBL and Wlink/Temanous for CBS supply, installation and operation. Consultants from Wlink/Temanous are mobilized to support the implementation of CBS project during the reporting period.

3.2.2. Automation of MIS in SFDB

43. Procurement plan for automated MIS in SFDB was progressed and approved during reporting period. A procurement committee was constituted in SFDB and bidding documents for procuring the MIS was discussed and approved by procurement committee, steering committee and SKBBL BoD and the Expression of Interest to procure software and Bid notice to procure hardware was published in December 24.

44. SFDB has been processing the bid of for the procurement of the hardware and software for the MIS and is about to finalize the whole process. Actual work on implementing the MIS is expected to start in the next reporting period.

3.2.3. Procurement of Vehicle

45. Project Steering Committee has agreed the procurement of a vehicle in ADBL to facilitate and expedite project implementation and ADBL has yet to procure the vehicle.

3.2.4. Procurement of Consulting Services

46. The project was designed to finance approximately 26 person-months of international consulting services and 318 person-months of national consulting services to support implementation and provide capacity development support for institutional and policy reforms. The consultant recruitment process was initiated by the Government in March 2007 and was only completed in February 2009. Project Steering Committee reduced the inputs of national consulting services to 104 person months in cognizance to the context, realities, need and functions that have already been taken by staff of the IAs. The consultants recruited in the last reporting period continued their services during this reporting period.

47. **Consultant Inputs:** The project has used 36 person month services of the international consultant and 105.5 person month services of national consultants. Table 2 provides information on inputs of various consultants used by the project as of March 2010.

48. **Outputs Produced by the Consultant:** The consultants have produced different outputs during their tenure in this project. Information on type of outputs produced by the consultants and their use by host organisations is provided in Appendix 1.

49. **Consultant's Planned Outputs and Deadlines:** All consultants working in the project either under TAs or grants was asked to provide outputs that they are producing under this assignment along with deadlines in order to ensure transparent monitoring of consultant's outputs. Information on planned outputs and deadlines of each consultant is provided in Appendix 2.

50. **Assessment/Level of Satisfaction of Consultants' Performance:** A total of 12 consultants worked in different host organizations (i.e. ADBL, SFDB and NRB) under this project in different capacity. Host organization's level of satisfaction on consultant

performance has been assessed based on factors such as creativity, timeliness, communication, attitude and technical soundness. In general, host organization expressed their satisfaction on consultant's performance with few exceptions. The findings of the assessment revealed that host organizations are (i) satisfied with the performance of 8 consultants; (ii) partially satisfied with the performance of three consultants and (iii) suggested the replacement for one consultant. For partially satisfied consultant they mentioned the need to enhance performance, change attitude and improve communication. Details on the assessment of the level of satisfaction of consultant's performance by host organization are provided in Appendix 3.

Table 2: Consultant Inputs Used as of March 2010

S.N.	Type of Experts	Revised inputs (Person months)	Used inputs (Person months)	Based on
	International Consultants			
1	Chief Technical Advisor	30	30	ADBL
2	MIS Specialist	6	6	ADBL
	Total	36	36	
	Local Consultants			
1	Project Coordinator/Rural Finance Sector Specialist	15.5	12.5	MOF
2	Internal Audit Specialist	12	12	ADBL
3	Human Resource Management Specialist	16	14	ADBL
4	Account and Financial Management Specialist	16	13	ADBL
5	Marketing Specialist	12	12	ADBL
6	Banking and IT Specialist	24	20	ADBL
7	Microfinance and Bank Operation Specialist	17	14	SFDB
8	IT Project Manager	12	8	ADBL
		119.5	105.5	

51. **Reporting Arrangements:** In order to ensure effective and efficient monitoring of consultants work, a system of monthly and quarterly reporting was introduced. In general, monthly reporting is done verbally in a meeting between concerned DCs, the consultants, Director/PIU with one person to record the proceedings and the record when edited becomes monthly report for work in concerned host institutions. On the other hand, quarterly reporting is a combination of verbal and written reporting at a meeting between DGMs, concerned DCs, consultants and PC/RFSS with someone to record meeting, specifically question and answer part of the meeting. The consultants are preparing brief reports based on reporting format which is being circulated before the meeting. This arrangement has been effective from January 2009.

3.3 Disbursement

52. Program loan was disbursed 100% while the project lagged significantly behind for the disbursement of project grant. Table 3 provides information on total disbursement of the project as of March 2010.

53. As of March 2010, only US\$ 883,033 was disbursed out of the project grant. Disbursement from grant was delayed due to prolonged holdup on CBS procurement, institutional development of NBTI including recruitment of CEO and training specialist and recruitment of national and international consultants for ADBL, SFDB and NRB.

Table 3: Disbursement as of March 2010

Number	Items	Original Allocation (\$)	Disbursement*	Remarks
A	Loan	56,000,000	56,000,000	
B	Grants			
1	Equipment	5,152,900	181,065	
2	Vehicle	25,300	-	
3	Training	490,800	218,945	
4	Consulting services	2,555,700	382,362	
4a	International consultants	648,000	90,000	
4b	National consultants	1,907,700	292,362	
5	Project Management Support	61,000	33,136	
6	Unallocated	414,300	-	Advance deposited in the second generation imprest account in ADBL and NBA
		8,700,000	815,508	

Note: * The expenditure as of March 2010 is indicative and accurate information is yet to be compiled.

3.4 Highlights of Audit Report of ADBL and SFDB

54. Audit of overall operation and management of the ADBL and SFDB for FY 20064/65 and 2065/66 was undertaken on time, however program expenditure for the FY 2064/65 was undertaken on time while MOF has yet to start the programme audit for 2066/67. In the completed audit, the auditors have not raised any serious objections. Both ADBL and SFDB have already addressed the objections raised by the Auditors.

4. Issues and Recommended Actions

4.1 Issues

55. There are some issues inherent to project implementation that needs to be addressed for achieving the desired outcomes, purposes and goals of the project. Some of these issues are outlined hereunder.

56. *Procurement of CBS in ADBL:* The success on RFSCDP implementation is centered on the procurement, installation and operation of CBS, which has been delayed due to varied reasons. There is a need to expedite installation and operation of CBS at the earliest.

57. *Automation of MIS in SFDB:* SFDB should expedite the procurement of the MIS software in order to enhance efficiency and effectiveness on its operation.

58. *Re-structuring of GBBs:* Under this project, government and NRB has been quite-effective to privatize four GBBs as re-structuring initiatives. There is still government share to be divested to ensure that GBBs are fully managed by private investors. Further, little is known on post privatization performances of these GBBs and there is mixed reaction from stakeholders on their efficiency and effectiveness. The far western GBB yet to be privatized is almost insolvent and decision to this effect needs to be made without further delay. Further, re-structuring of the GBBs need to re-defined under new context.

59. *Duplication of activities (SME finance in ADBL and Microfinance by SFDB):* One of the covenants that ADBL had to comply to be eligible for borrowing the second trench has been the completion of the phasing-out of the SFDP which eventually means that ADBL should phase-out its microfinance operation and channel microfinance services through SFDB. In contrast, ADBL has created SME division¹¹ that is providing wholesale lending facilities to SFCLs promoted by ADBL, which are also the partner MFIs of SFDB. It is irony that interest rate (10.5% p. a.) charged by ADBL under SME scheme to partner SFCLs is significantly lower than interest rate (11% p. a.) charged to SFCLs by SFDB. There is duplication on access to financial services extended by SME division of ADBL and SFDB. This issue needs immediate attention.

60. *Absorption of Technical Services provided by Consultant:* A number of international and national consultants in the past and at present provide technical support on different aspects of ADBL and SFDB management to enhance their technical capacity. There are cases where consultants are working either in isolation or counterpart staff is not interested on consultant's work. Staff of the host organization is not fully aware on type of output that consultant will be producing and extent to which such an output will meet their expectation and priorities. There is less than adequate effort to ensure ownership of consultant's work by concerned RFIs.

61. *Operation of National Banking Training Institute:* Despite being promoter of NBTI, key actors of the Nepalese financial sector still lack shared vision on its rationale, scope of work, operational mechanism and extent to which NBTI will meet their capacity development needs.

4.2 Recommended Actions

62. Any delay on addressing outstanding issues outlined above will affect the implementation of the project and delivery of project outputs. Hence, these issues should be addressed systematically. Table 4 outlines key actions recommended for effective project implementation.

Table 4: Recommended Actions

S.N.	Recommended actions	Responsibilities		Time-line
		Primary	Support	
1	Procurement of CBS in ADBL			
	Staff training on computer application	IT Project Manager	CTA	30/06/10
2	Automation of MIS in SFDB			
	Staff training on computer application	SFDB	ADB	30/06/10
3	Re-structuring of GBBs			
	Decision on privatization of far-western GBB	MFD/NRB	MOF	30/06/10
	Review the performance of GBBs after divestment	MFD/NRB	MOF	30/06/10
	Implementation of re-structuring plan for GBBs	MFD/NRB	MOF	30/06/10
4	Duplication of activities			
	Review the scope of SME operation in ADBL	CTA, HRMS	PC/RFSS	30/06/10
	Policy on SME lending	BDS	CTA	30/06/10
	Phasing out of micro-enterprise lending in ADBL	ADBL	CTA	30/06/10

¹¹Contrary to the conventional notion that SME relates the small and medium enterprise finance, ADBL is defining it as small and micro enterprise finance and undertaking the business through SFCL.

S.N.	Recommended actions	Responsibilities		Time-line
		Primary	Support	
5	Absorption of Technical Services provided by Consultant			
	Consultative meeting with consultant and concerned division in ADBL and management in SFDB	CTA	PC/RFSS	30/06/10
6	Operation of National Banking Training Institute			
	Recruitment of training consultant	NBTI	CTA	30/06/10
	Design of training curricula	CEO	CTA	30/06/10
	Accreditation with national, regional and global level universities	CEO	CTA	30/06/10
	Develop certification process	CEO	CTA	30/06/10

Note: CTA = Chief Technical Advisor, CEO = Chief Executive Officer, NBTI = National Banking Training Institute, PC/RFSS = Project Coordinator/Rural Finance Sector Specialist, MOAC = Ministry of Agriculture and Cooperatives, HRMS = Human Resource Management Specialist, MFD/NRB = Microfinance Department / Nepal Rastra Bank, MBOS = Microfinance and Banking Operation Specialist, ADB = Asian Development Bank.

Appendix 1: Outputs Produced by the Consultants and Status of Use by Host Institutions

S.N.	Outputs Produced	Date	Status of Use by Host Organization	Remarks
A	Human Resource Specialist			
1	Rationalization of Organization Structure	July 2009	Gradual adoption by ADBL management	
2	Strengthening HRIS in ADBL	August 2009	Endorsed by ADBL management	
3	List on authority delegation on training nomination, transfer, leave sanction and deputation	31 August 2009	Review	Additional task submitted to DC, HR
4	Format /Form for transferred employee and process thereof	September 2009	Review	Additional task submitted to DC
5	Change in employee promotion rules as per the direction of CIAA	September 2009	Review	Additional task submitted to DC
6	Draft Service Rules	March 2010	Review	
B	Account and Financial Management Specialist			
1	Inter-Branch Reconciliation System	June 2009	New Reconciliation System under centralized approach suggested by the specialist during June 2009 is not adopted in its basic form. Some of the recommendations such as establishing specific code for reconciliation have been agreed upon under Account Code 17.	Implemented
2	Revised Accounting Policy	Aug. 2009	Approved by the Board and has come into effect	Implemented
3	Accounting Manual			
A	Payment Procedure Manual	Aug. 2009	Approved by the Board and has come into effect.	
B	Accounting Manual related to Staff and Expenditure	Sept. 2009		
C	Accounting Manual (Draft) Deposit Acc. Manual	Dec. 2009	In process of obtaining immediate approval and implementation.	
D	Consolidated accounting manual	March 2010	Review	
C	Microfinance and Banking Operation Specialist			
1	SKBBL's business plan	April, 2009	SKBBL has applied business plan in day to day operation	
2	SFCLs restructuring and Strengthening Plan	April, 2009	Change management in process	
3	MIS Procurement plan	June, 2009	Under review by SFDB management and other concerned	
4	Lending guidelines and brochure of SKBBL's product and services	July 2009	Change management in process	
5	Proposal for extending microfinance services in the hills and mountains of Nepal.	Aug., 2009	Proposal submitted to ADB	
6	Brochure on SKBBL's product and services	July 2009	Change management in process	
7	Manual and guideline for business planning in SFCL and SCCs	Sept. 2009	Change management in process	
8	Institutional Assessment tools	Sept. 2009	Change management in process	

S.N.	Outputs Produced	Date	Status of Use by Host Organization	Remarks
	for SFCLs and SCCs			
9	Training on Business planning to SFDB and SFCL staff	Sept. 2009	Institutionalization of business planning concept within SFDB and SFCLs	
10	Documentation of financial products offered by SFCLs	Dec. 2010	Being disseminated during trainings/workshops of SFCL	
11	Draft Operational Procedure Manual	March 2010	Review	
D	TA 4857 NEP Team			
1	Inception Report	August. 2009		
2	Comment on the report	Sept. 2009	Relevant divisions agreeing action to be taken by TA team members in conjunction with divisional personnel	
3	Business Plan for NBTI	Sept. 2009	Newly recruited CEO is currently revising the business plan	
4	Policy Statement and Trade Finance Strategy	Dec. 2009		
5	Manual on Trade Finance	March 2010	Review	
6	Policy Statement and Treasury Specialist	Dec. 2009		
7	Manual on Treasury Management	March 2010	Review	
8	Manual on Risk Management	Dec. 2009		
9	Training Materials on Risk Management	March 2010	Review	
10	Policy Statement on Human Resource Management	Dec. 2009		
11	Job description of staff	March 2010	Review	
12	Draft report on impact of training	March 2010	Review	

Appendix 2: Schedule of Planned Outputs of the Consultants and Deadlines

S. N.	Expertise type	Host Organization	Planned Outputs	Deadlines
A	Grant financing			
1	Human Resource Management Specialist	ADBL	Position requirements (staffing standard including staff mix ratio)	Apr. 2010
			Job description of key positions	June 2010
2	Account and Financial Management Specialist	ADBL	Budgeting system	Apr. 2010
			Comprehensive Accounting Manual	June 2010
3	Microfinance and Banking Operation Specialist	SFDB	SFDB and SFCL Operational Manual	June 2010
			Training Manual on Operational System	June 2010
B	TA 4857 NEP (supplementary)			
1	International Team Leader	ADBL/NRB	Report on HR and Change Management	May 2010
2	Treasury Specialist	ADBL	Manuals and Training Materials for Treasury Management	Apr. 2010
			Trainers Preparation	May. 2010
			Conducting training	July 2010
3	Risk Management Specialist	ADBL	Training Preparation and Materials	Apr. 2010
			Trainers Preparation	May. 2010
			Conducting training	July 2010
4	Business Process and Portfolio Management Specialist	ADBL	Training preparation	Apr. 2010
			Conducting training	July 2010
5	Training Specialist	ADBL	Course Materials Amendment/Design	Apr. 2010
			Medium Term Training Plan	May 2010
			Trainers Preparation	July 010
6	Trade Finance Specialist	ADBL	Operational Manual for Handling Guarantee and Letter of Credit Business	Apr. 2010
			Trainers Preparation	May. 2010
			Conducting training	July 2010

Appendix 3: Assessment/Level of Satisfaction of Consultant's Performance by Host Organization

S. N.	Expertise type	Host Organization	Basis of Assessment					Overall level of satisfaction
			Creativity	Timeliness	Communication	Attitude	Technical soundness	
A	Grant financing							
1	Human Resource Management Specialist	ADBL	Low	Medium	High	Negative	Medium	Need improvement on performance
2	Account and Financial Management Specialist	ADBL	High	Medium	Medium	Positive	High	Satisfactory
3	IT Project Manager	ADBL	High	High	High	Positive	High	Highly Satisfactory
4	Microfinance and Banking Operation Specialist	SFDB	Medium	Medium	Medium	Positive	High	Satisfactory
B	TA 4857 NEP (supplementary)							
1	International Team Leader	ADBL/NRB	High	Medium	Low	Negative	High	Need some improvement on attitude and communication.
2	Risk Management Specialist	ADBL	High	Medium	Medium	Positive	High	Satisfactory – some irregularities noted in the recent days
3	Training Specialist	ADBL	Medium	Medium	Medium	Positive	Moderate	Need some improvement on communication
4	Trade Finance Specialist	ADBL	Medium	Medium	Medium	Positive	Moderate	Satisfactory
5	MIS Specialist (International)	ADBL	Medium	Medium	Medium	Positive	High	Satisfactory
6	Legal and Regulation Specialist (International)	NRB	Medium	Medium	Medium	Positive	High	Satisfactory
7	Business Process and Portfolio Management Specialist	ADBL	Medium	Medium	Medium	Positive	High	Satisfactory
8	Treasury Specialist	ADBL	High	Medium	Medium	Positive	High	Satisfactory