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KATHMANDU, NEPAL

PROJECT ADMINISTRATION AND FINANCIAL MANAGEMENT REPORT
**NEPAL: RURAL FINANCE SECTOR DEVELOPMENT
CLUSTER PROGRAM I**
(OCTOBER-DECEMBER 2009)

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January 2010

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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 the Rural Finance Sector Development Cluster Program I (RFSDCP I) started in November 2006 and series of activities / initiatives started after loan effectiveness on achieving the intended goals. The project consists of five components and the results are vivid in all five components. For instance, 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 1.4 million savings clients and 1.3 million loan clients, an increase from 640,000 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) has been established with leading commercial banks as promoters with the mandate to build the capacity of the RFIs. Most RFIs are adopting BASEL II standards. ADBL, all Microfinance Development Banks (MDBs) [except Grameen Bikas Banks (GBBs) and two apexes namely 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. The goals of the RFSDCP are to (i) ensure sustainable access of rural households to institutional financial services, and (ii) encourage 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 the sector reform, and the 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 will aim to promote enabling sector environment, expand sound RF outreach, and enhance private sector participation in RF. The processing of subprogram II is underway.

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 Agricultural Development Bank Limited (ADBL) for commercialization and, eventually, privatization.

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

6. Implementation of RFSDCP I started in November 2006 and completed in December 2009. The program loan under RFSDCP I were released in two tranches over 2

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)

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 2010.

9. A discussion on status of component outputs of RFSDCP I as of December 2009 follow hereunder.

2.1 Favorable Policy Environment

10. Aligned with the Government's financial sector reform strategy, the program seeks to create favorable policy environment by (i) establishing a supervisory and regulatory system for RFIs, (ii) divest NRB shares in RFIs to legally defined level², (iii) phase out government ownership of technically insolvent RFIs and (iv) discontinue application of interest rate ceilings to ADBL and SFDB. There has been substantial progress in creating favorable policy environment.

11. The reforms measures pursued throughout RFSDCP revolved around (i) ensuring the full enforcement of the debt recovery law for willful defaulters; (ii) promoting lending from formal and semiformal RFIs to CBOs; (iii) divesting the Government shares and increasing participation of the private sector in ADBL and SFDB; and (iv) discontinuing 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 and 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.

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 in relation to institutional restructuring and reforms of ADBL, SFDB and GBBs during the reporting period follows hereunder.

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.

2.2.1. Agricultural Development Bank Limited

14. RFSDCP support to reform and restructure ADBL⁶ 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 is linked to performance improvement and commercialization eventually creating environment for privatization. The restructuring of ADBL is detailed in ADBL Restructuring Plan (ARP)⁷ Implementation Guide. Important reform output targets are: (i) divestment of Government shares to the legally defined level under the Banks and Finance Institutions Act (BFIA) 2005, (ii) initiation of the initial public offering (IPOs), (iii) completion of a voluntary retirement scheme, and (iv) attainments of viable operations by meeting performance indicators and critical implementation targets set under ARP.

15. Series of reform initiatives started in ADBL since November 2006. The government began the process of recapitalization to cover debt and authorized capital of NRs. 12 billion since May 2006 through the conversion of the then outstanding loan of the government with ADBL to preferential shares and is planning to inject additional capital by subscribing more preference shares subject to ADBL's ability to meet agreed performance benchmarks⁸. The Board of Directors (BOD) is 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 two consultants: Human Resource Management Specialist (HRMS) and Account and Finance Management Specialist (AFMS) 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 in reaching agreement with the CBS vendors, identifying functional stream training courses, preparing internal payment procedures for CBS installation, and worked with HRM Division in upgrading HR management policy.

18. During the reporting period, HRM Specialist (HRMS) prepared a report on strengthening Human Resource Information System (HRIS) in ADBL, drafted Staff Rules, facilitated to form a working teams and briefed them for preparing job descriptions, provided candid opinion on 'Staff Rules Amendment Task Force' as a member, advised Training Specialist on designing HRM training, training for trainers and 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 the new organization structure and functions with DC, BMD and managers of main banking Office and New Road Branch and assisted the training specialist working under TA 4857 NEP to

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.

design the 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 develop software for account reconciliation to IT department programmer 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 in process 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, advised on CBS contract negotiation, and examined technical training needs of IT staff at ADBL. It was agreed that Mr Singh would return in early 2010 to examine the MIS to propose modifications to make it more effective as a business management tool.

22. BPPM specialist mobilised on 25 November 2009 as replacement for earlier specialist decided to follow the plan earlier consultant with some additional input in relation to business processes and problem account management. A working group has been formed to upgrade credit policy and procedures and to examine how to organise all credit operations into a single division.

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.

24. Trade Finance Specialist (TFS) mobilized on 9 October 2009 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 installation.

25. Training Specialist (TS) reviewed the capacity in the ADBL training units and because work on career development curricula has been in abeyance because adoption of a revised HRM Policy, in which are defined the career paths, minimum entry criteria and rules for recruitment and promotion (essential to the design of the curriculum), is still in progress. In the meantime, TS designed an upgraded training of trainers course

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.

and a budget for an initial course at RTC Manglapur and designed procedures for assessment of training impact; the work will commence in January 2010.

26. Treasury Specialist joined on 25 November 2009, 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.

27. A team of consultants comprising of International Team Leader and domestic MIS Specialist, HRD Specialist and Banking Business Development Specialist are working under PPTA TA 7196 NEP: Rural Finance Sector Development Cluster Program II completed their work during the reporting period. The team (i) undertook diagnostic review of ADBL financial and operational performance, (ii) review status of procurement of CBS including guidelines for successful installation, (iii) review existing ADBL HR policy on recruitment, promotion, incentive, etc. and (iv) assess critical issues of Nepalese financial sector, determine best suitable service delivery mechanism, develop new products especially fee-based including credit lending process. The team prepared (i) policy matrix for RFSDCP II, (ii) ADBL Restructuring Plan II, and (iii) ADBL Capital Restructuring Plan which has been submitted to ADBL and ADB for their observation, comments and suggestions.

2.2.2.Small Farmers Development Bank

28. The program targets to strengthen SFDB and SFCLs to supplement ADBL's efforts to ensure that agriculture credit needs of small farmers are met adequately 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 prepared based on the diagnostic review of SFDB¹⁰ seek to enhance its viability and outreach to SFCLs with specific key performance indicators (KPIs). The restructuring assistance has prioritized strengthening SFDB's microfinance and banking operations, staff capacity building and accounting and auditing. The reform output targets was (i) adoption of SFDB restructuring plan, (ii) initiation of restructuring process, and (iii) 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.

29. 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) is providing technical support to SFDB in this process since February 2009. During the reporting period, MBOS supported to finalize the MIS Hardware and Software Procurement plan including evaluation criteria, strengthen SFCLs and documented the financial products offered by SFCLs. The bidding documents for procuring the MIS has been discussed and approved by procurement committee, steering committee and SKBBL Board and the Expression of Interest to procure software and Bid notice to procure hardware was published in December 24. Evaluation criteria for evaluating the proposals for software and bids for hardware has been developed and approved by SKBBL procurement committee. SFCLs are provided inputs on the business plan they have developed and financial products offered by sampled SFCLs and recommended loan, savings and insurance products has been documented and the findings is being disseminated during the trainings/workshops of SFCL.

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).

30. 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.

31. International Microfinance and Banking Operation Specialist working under PPTA TA 7196 NEP: Rural Finance Sector Development Cluster Program II prepared draft SFDB Restructuring Plan (SRP) II which is being discussed by SFDB management. The SFDB restructuring plan was presented in key stakeholder's workshop in October 2009. SFDB's BODs are currently reviewing SRP for eventual approval and implementation by early February 2010.

2.2.3. Grameen Bikash Banks

32. There is no significant work done on restructuring of GBBs during reporting period. International Microfinance and Banking Operation Specialist working under PPTA TA 7196 NEP: Rural Finance Sector Development Cluster Program II prepared a working paper on GBB. The plan outlines the need to divest the NRB shares at the Far Western GBB to the level defined in the NRB Act and eventual privatization of Far Western GBB. 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

33. During the reporting period, the NRB engaged key stakeholders of the sector for drafting the microfinance act consistent to Microfinance Policy 2007. Under TA 4857 NEP, a Regulation and Supervision Specialist is assisting NRB to create supportive legal and regulatory framework for rural finance sector including providing feedback on draft microfinance act. A roundtable discussion on draft microfinance act has been held in November 2009 to obtain feedback on draft act.

34. Rural Finance Legislation Specialist working under TA 4857 NEP also offered NRB a draft Act in which the issues raised by the initial draft were addressed. Further, series of consultation were organized with key stakeholders including officials in MoF in regulating exceedingly large numbers of small and micro institutions.

35. NRB has incorporated the relevant feedbacks provided by the participants of the workshop and at the final stage of preparing draft microfinance act.

2.4 Sector Capacity Building

36. RFSDCP I supported to establish National Banking Training Institution (NBTI) as an educational institution under Nepal's Company Act to address capacity building needs of formal and semiformal RFIs for enhancing access of rural communities to financial services and improve financial literacy of rural communities. Bankers' Association of Nepal led the establishment of NBTI with share capital from all commercial banks. CEO for NBTI was recruited from open competition¹¹. Draft business plan for NBTI is prepared and management for course curriculum, materials, library, training of trainers, and equipment is in process. NBTI has yet to start actual training course. NBTI is currently working to obtain licence from Ministry of Education to operate as an instructional institution and ADB is supporting NBTI in this process. No action has been taken in staff recruitment as NBTI Board wishes major administrative decisions upon CEO recruitment.

¹¹International Chief Technical Advisor/Commercial Banking Specialist under TA 4857 NEP provided technical backstopping support to NBTI to design operational and management system.

During the reporting period, CTA working under TA 4857 NEP assisted the NBTI Board to complete the recruitment of a CEO, prepare a draft of the institute's business plan, and apply for the drawdown of ADB funds.

37. International Microfinance and Banking Operation Specialist working under PPTA TA 7196 NEP: Rural Finance Sector Development Cluster Program II working paper on (i) Debt Recovery Tribunals (DRT) and (ii) Credit Information Bureau (CIB) to expand the scope of support on sector capacity building.

2.5 Product and Process Innovations

38. There has been no significant work on product and process innovations during the reporting period. International team Leader working under PPTA TA 7196 NEP: Rural Finance Sector Development Cluster Program II has flagged 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

39. 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 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

40. 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.

41. 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 for NBTI.

42. 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 original and revised allocation of project expenditure and expenditure as of June 2009.

Table 1: Project Expenditures as of December 2009

Number	Items	Original Allocation (\$)	Revised Allocation (\$)	Expenditure as of December 2009 (\$)*	Remarks
1	Equipment	5,152,900		6,626.00	
2	Vehicle	25,300		0.00	
3	Training	490,800		62,572.78	
4	Consulting services	2,555,700		52,500.00	
4a	International consultants	648,000		90,000.00	
4b	National consultants	1907,700		379,713.53	

Number	Items	Original Allocation (\$)	Revised Allocation (\$)	Expenditure as of December 2009 (\$)*	Remarks
5	Project Management Support	61,000		16,078.92	
6	Unallocated	414,300		0.00	
		8,700,000		607,491.23	

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 December 2009 is indicative and accurate information is yet to be compiled.

43. The project is rather slow on expenditure on grant. Only a fraction of the project grant has been used as of the December 2009.

3.2 Procurement

44. 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

45. Process continued on procuring the 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. Operation of the CBS will be started in 2010.

3.2.2. Automation of MIS in SFDB

46. 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 has been discussed and approved by procurement committee, steering committee and SKBBL Board and the Expression of Interest to procure software and Bid notice to procure hardware was published in December 24.

3.2.3. Procurement of Vehicle

47. Project Steering Committee has agreed the procurement of a vehicle in ADBL to facilitate and expedite project implementation and ADBL has procured the vehicle.

3.2.4. Procurement of Consulting Services

48. 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.

49. **Consultant Inputs:** The project has used 36 person month services of the international consultant and 87.5 person month services of national consultants. Table 2

provides information on inputs of various consultants used by the project as of December 2009.

50. **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.

51. **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.

Table 2: Consultant Inputs Used as of December 2009

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	9.5	MOF
2	Internal Audit Specialist	12	12	ADBL
3	Human Resource Management Specialist	16	11	ADBL
4	Account and Financial Management Specialist	16	10	ADBL
5	Marketing Specialist	12	12	ADBL
6	Banking and IT Specialist	24	20	ADBL
7	Microfinance and Bank Operation Specialist	12	11	SFDB
8	IT Project Manager	12	2	ADBL
		119.5	87.5	

52. **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, the consultants and PC/RFSS with someone to record the meeting, specifically the Q&A part of the meeting. The consultants will prepare brief reports based on reporting format which will be circulated before the meeting. This arrangement is being effective from January 2009.

3.3 Disbursement

53. 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 December 2009.

54. As of December 2009, 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 December 2009

Number	Items	Original Allocation (\$)	Disbursement*	Remarks
A	Loan	56,000,000	56,000,000	
B	Grants			
1	Equipment	5,152,900	6,626.00	
2	Vehicle	25,300	0.00	
3	Training	490,800	62,573.78	
4	Consulting services	2,555,700	52,500.00	
4a	International consultants	648,000	90,000.00	
4b	National consultants	1907,700	379,713.53	
5	Project Management Support	61,000	16,078.92	
6	Unallocated	414,300	275,541.46	Advance deposited in the second generation imprest account in ADBL and NBA
		8,700,000	883,033.69	

Note: * The expenditure as of December 2009 is indicative and accurate information is yet to be compiled.

3.4 Highlights of Audit Report of ADBL and SFDB

55. Audit of overall operation and management of the ADBL and SFDB as well as program expenditure for FY 20064/65 was undertaken on time. In both the audit, the auditors have not raised any serious objections. Both ADBL and SFDB have already addressed the objections raised by the Auditors.

56. Audit of overall operation and management of the ADBL and SFDB as well as program expenditure for FY 2009/10 is un process. As of the reporting time, none of the organizations have completed the audit of their transaction. Highlights of the audit report of ADBL and SFDB will be included in next reporting period.

4. Issues and Recommended Actions

4.1 Issues

57. 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.

58. *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 beginning the January 2010.

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

60. *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 GBB yet to be privatized (far-western GBB) 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.

61. *Duplication of activities (SME finance in ADBL and Microfinance by SFDB):* One of the covenants that ADBL had complies 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 division¹² 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.

62. *Product and Process Innovations:* Scope of product and process innovations component has been limited and requires renewed focus on new product development, diversification of products and services and expansion of services in inaccessible hills and mountains where enhancing access to financial services is a challenge to different financial service providers.

63. *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 counter-part 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.

64. *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. Operation of NBTI has been delayed due to delay on recruitment of CEO and completion of other formalities to operate as educational institution including affiliation with universities and accreditation process.

4.2 Recommended Actions

65. 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	31/12/09

¹²Contrary 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	
2	Automation of MIS in SFDB			
	Expedite MIS procurement process	CEO, SFDB	PC/RFSS	31/10/09
	Staff training on computer application	SFDB	ADB	31/10/09
3	Re-structuring of GBBs			
	Decision on privatization of far-western GBB	MFD/NRB	MOF	30/06/09
	Review the performance of GBBs after divestment	MFD/NRB	MOF	30/06/09
	Implementation of re-structuring plan for GBBs	MFD/NRB	MOF	31/12/11
4	Duplication of activities (SME finance in ADBL and Microfinance by SFDB)			
	Review the scope of SME operation in ADBL	CTA, HRMS	PC/RFSS	3/03/10
	Policy on small and medium enterprise (SME) lending	BDS	CTA	3/03/10
	Phasing out of micro-enterprise lending by ADBL to SFCL	ADBL	CTA	3/03/10
5	Product and Process Innovations			
	Training on market led-approach to new product development and processing mapping to selected MFIs	MFD/NRB	PC/RFSS	3/03/10
	Technical support to new product development and process refinement	MFD/NRB	PC/RFSS	3/03/10
	Piloting of crop insurance scheme	MOAC	Selected MFIs	3/03/10
6	Absorption of Technical Services provided by Consultant			
	Consultative meeting with consultant and concerned division in ADBL and management in SFDB	CTA	PC/RFSS	3/03/10
7	Operation of National Banking Training Institute			
	Recruitment of CEO and training consultant	NBTI	CTA	31/1/10
	Business plan for NBTI	CTA	NBA	30/04/10
	Recruitment of support staff	NBTI	CEO	30/04/10
	Design of training curricula	CEO	CTA	30/04/10
	Accreditation with universities (national, regional and global level)	CEO	CTA	30/04/10
	Develop certification process	CEO	CTA	30/04/10

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
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.	
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 for SFCLs and SCCs	Sept. 2009	Change management in process	

S.N.	Outputs Produced	Date	Status of Use by Host Organization	Remarks
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	
D	PPTA TA 7196 NEP Team			
1	Policy Matrix	October 2009	Finalized, approval in progress	
2	ADBL Restructuring plan II	Nov. 2009	Finalized, approval by ADBL board in progress	
3	Working Paper on Debt Recovery Tribunals	Nov. 2009	Finalized	
4	Working Paper on Credit Information Bureau	Nov. 2009	Finalized, and CIB in process to open-up microfinance unit within it	
5	SFDBL Restructuring Plan II	Nov. 2009	Finalized, approval by SFDB board in progress	
6	Working Paper on GBB	Nov. 2009	Finalized and review by NRB in progress	
7	ADBL Capital Restructuring Plan	Nov. 2009	Finalized, approval by SFDB board in progress	
E	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	Policy Statement and Treasury Specialist	Dec. 2009		
6	Manual on Risk Management	Dec. 2009		
7	Policy Statement on Human Resource Management	Dec. 2009		

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	Draft staff rules	Oct. 2009
			Staff Rules	Feb. 2010
			Position requirements (staffing standard including staff mix ratio)	Apr. 2010
			Job description of key positions	June 2010
2	Account and Financial Management Specialist	ADBL	Draft Account Manual	Sept. 2009
			Review of key performance indicators for FY 2008/09	Jan. 2010
			Accounting manual	Mar. 2010
			Budgeting system	Apr. 2010
3	Microfinance and Banking Operation Specialist	SFDB	Documentation of business expansion model	Oct. 2009
			Develop guidelines for calculating set KPIs	Nov. 2009
			Monitoring format for SFCL and SFDB	Nov. 2009
			Procurement plan for MIS in SFDB	Dec. 2009
			Documentation of innovative products offered by SFCLs	Dec. 2009
			Update SFDB website	Jan. 2010
			Technical support report	Jan. 2010
B	PPTA (TA 7196 NEP)			
1	International Team Leader	ADBL/NRB/SFDB	Review of ADBL Restructuring Plan I	Nov. 2009
			ADBL Capital Restructuring Plan II	Nov. 2009
			ADBL Restructuring Plan II	Nov. 2009
2	Financial Analysis Specialist	ADBL/SFDB	Consultant's report on Financial Management	Nov. 2009
3	Management Information System Specialist	ADBL/SFDB	Consultant's report on Management Information System	Oct. 2009
4	Human Resource Development Specialist	ADBL	Consultant's report on Human Resource Development	Oct. 2009
5	Banking Business Development Specialist	ADBL	Consultant's report on Banking Business Development	Nov. 2009
6	Microfinance and Banking Operation Specialist	NRB/SFDB	SFDBL Restructuring Plan II	Nov. 2009
			GBB Restructuring Plan II	Nov. 2009
			Debt Recovery Tribunal - Preliminary Paper on Technical Assistance	Nov. 2009
			Credit Information Bureau - Preliminary Paper on Technical Assistance	Nov. 2009
C	TA 4857 NEP (supplementary)			
1	International Team Leader	ADBL/NRB	Report on HR and Change Management	May 2010
2	Treasury Specialist	ADBL	Treasury Policy for ADBL	Jan. 2010
			Risk management system	Jan. 2010
			Manuals and Training Materials for Treasury Management	Jan. 2010
			Trainers Preparation	Jan. 2010
3	Risk Management Specialist	ADBL	ALCO and LPMC framework and format	Jan. 2010
			Procedure Revision and Manual	Jan. 2010
			Training Preparation and Materials	Jan. 2010

S. N.	Expertise type	Host Organization	Planned Outputs	Deadlines
			Trainers Preparation	Feb. 2010
4	Business Process and Portfolio Management Specialist	ADB L	Operating framework	Jan. 2010
			Manuals preparation	Jan. 2010
			Training preparation and delivery	Feb. 2009
5	Training Specialist	ADB L	Course Materials Amendment/Design	Jan. 2010
			Medium Term Training Plan	Jan. 2010
			Trainers Preparation	Mar.2010
6	Trade Finance Specialist	ADB L	Strategy on Trade Finance	Jan. 2010
			Operational Manual for Handling Guarantee and Letter of Credit Business	Feb. 2010