

**NEP 2268 (SF) - NEPAL: RURAL FINANCE SECTOR DEVELOPMENT CLUSTER PROGRAM I
PROGRAM PROGRESS REPORT
(As of March 2010)**

| Objective | Actions | Time line | Status | Action to be Taken |
|---|--|-----------|--|---|
| Transform ADBL into a sustainable and efficient RFI | Issuance of a notice to offer ADBL shares to the small shareholders of ADBL | | ADBL issued a notice on 7 October 2007 to offer NRs450 million worth of ADBL ordinary shares at par value of NRs100 to small shareholders and the notice was issued from 30 November 2007 to 3 January 2008. | - |
| | Decision to initiate initial public offering of ADBL | | ADBL issued Initial Public Offering of NRs. 960 million worth of ordinary shares at par value of NRs. 100 to general public and successfully implemented in 4-7 April 2010. | - |
| | Settlement of the Government's dues payable to ADBL | | Government settled full amount of accumulated dues amounting NRs96.76 millions ¹ on 28 November 2007. | - |
| | Finalize divestment plan of Government shares in ADBL | | On 21 November 2007, GOA/MOF finalized/approved ADBL divestment plan which included, among other, (i) issue 5% of total ordinary shares to small shareholders between November 2007 and January 2008, (ii) issue IPO of 30% of total ordinary shares within 2009 and (iii) divest Government ordinary shareholding to at least 40% of total ordinary shares by 2011. | - |
| | ADBL will (i) write-off bad debts and (ii) provide adequate provisions for its other categories of debts, in each case in accordance with NRB directives | | ADBL started to write-off bad debt and make loan loss provisions complying with NRB directives ² and Bank and Financial Institution Act 2062. A loan portfolio management system is established in head offices and all the branch offices to comply with NRB directives and Bank and Financial Institution Act 2062 on write-off | <ul style="list-style-type: none"> • Training on Portfolio and Risk Management, and • Training on best practices to recover Non Performing Loans and Non Bank Assets. |

¹These expenses include mainly the expenses incurred for implementing Government sponsored projects.

²ADBL categorizes loans and maintains loan loss provisions in accordance with NRB directives. For the FY2006, ADBL made loan loss provision in excess of the minimum provision requirement of NRs6.13 billion based on the NRB directive. ADBL writes off its bad debts in accordance with NRB's Loan Write Off Regulation 2005.

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| | | | and loan loss provisions. | |
| | Revision and update by ADBL of its policies related to (i) human resource management, (ii) portfolio management, (iii) financial management and (iv) credit management to the satisfaction of ADB | | ADBL BODs adopted new policy on (i) portfolio management, (ii) human resource management, (iii) financial management, and (iv) credit management since early 2008 and (v) account and financial management policy in October 2009. | <ul style="list-style-type: none"> Continued review and update of these policies; Finalize staff rules, and Conduct election of Collective Bargaining Agent to address the problem inherent to staff union management. |
| | Completion by ADBL of second voluntary retirement scheme | | ADBL completed three (June 2006, January 2007 and March 2009) voluntary retirement schemes (VRS) for staff with more than 20 years of service to accept early retirement. A total of 588, 574 and 262 staff took early retirement under first, second and third VRS respectively. | - |
| | Achievement of the performance indicators and critical implementation targets set out in ADBL Restructuring Plan to the satisfaction of ADB | | Progress on ADBL restructuring is evaluated based on sustainability, outreach, and productivity indicators. ADBL demonstrated some notable changes on performance targets ³ , except outreach indicators ⁴ . | <ul style="list-style-type: none"> Awareness on performance indicators and critical implementation targets. Decentralize the performance indicators and critical implementation targets for branch and regional offices. |
| | Establishment of a separate unit within ADBL to deal with client complaints, including those relating to corruption. The unit will report to the Audit Committee | | ADBL established a client complaints unit ⁵ in May 2007 which receives and investigates client complaints and directly reports, as and when needed, to audit committee to ADBL BODs. | |

³Non-performing loan ratio of ADBL declined from 36.5% in FY2005 to 9% in FY2009. ADBL went from a net loss of NRs79 million in FY2005 to a profit of NRs353 million, NRs. 700 million and NRs. 633 Million in 2007, 2008 and 2009 respectively.

⁴Two consultants (i) Human Resource Specialist and (ii) Account and Financial Management Specialist under grant finance and five consultants (i) Treasury Specialist, (ii) Business Process and Portfolio Management Specialist, (iii) Training Specialist, (iv) Risk Management Specialist, (v) Trade Finance Specialist and (vi) Chief Technical Advisor under technical assistance are providing technical backstopping support for improved operational and financial management of ADBL.

⁵Key responsibilities of the unit are to (i) investigate client complaints including those regarding corruption and allegations of misconduct by units and/or employees of ADBL, and propose remedial actions; (ii) formulate for approval of ADBL Board of Directors policy and procedures for managing complaints from clients about conduct of ADBL and its employees; (iii) advise and support branch managers and regional directors in applying complaints policies and procedures; and (iv) prepare quarterly reports on the status of client complaints, outcomes, and actions taken.

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| | Establishment of Management Information System (MIS) by ADBL that allows measurement of its banking service outreach to women and disadvantaged group | | ADBL has designed and implemented MIS to monitor performance indicators and has been producing quarterly performance monitoring report covering indicators on outreach, financial performance, operating efficiency, productivity and risk. ADBL signed an agreement with Wlink/Temanous for the supply and installation of Core banking System (CBS) and procurement process is ongoing. | <ul style="list-style-type: none"> ▪ Use of MIS for Operational Decision Making ▪ Review the actual process to procure CBS including Letter of Credit. |
| | Completion of the phasing out of the ADBL's small farmers development program | | ADBL phased-out the SFDP on 15 July 2007 and transferred related loan portfolio to SFDB. | <ul style="list-style-type: none"> ▪ Review the scope of work and expand the scope of operation of SME division |
| | Completion of ADBL's assessment of the performance of Small Farmers' Cooperative Limited (SFCL), which will be the basis for determining further onlending support by ADBL to SFDB | | ADBL assessed performance of 214 SFCLs ⁶ and categorize them into four: good, substandard, doubtful, and bad based on criteria such as overdue loans, interest receivables, internal resources, share capital and profits and losses. This classification provided basis for further on-lending to SFDB and determine monitoring requirements and disbursement procedures. | - |
| Transform SFDB into a model apex agency for Small Farmers' Cooperative Limited | Development and adoption of SFDB restructuring plan in consultation with ADB covering strategy, legal and governance structure, organizational and human resources development, operating policies and guidance for financial activities, partnership arrangements, performance | | SFDB BOD approved SFDB restructuring plan on 15 November 2007. Reform has been started on outreach, portfolio management and institutional capacity. As part of restructuring exercises, SFDB's BODs recruited Chief Executive Officer through open competition and prepared plan to gradually return ADBL staff working on deputation in SFDB ⁷ . SFDB prepared a business plan for its operation and introduced a policy to enhance access to financial services to non-SFCLs. A pilot project on enhancing financial | <ul style="list-style-type: none"> ▪ Technical support on client, diversification and new product development. ▪ Development of operational guidelines and training manuals for SFDB and SFCL's capacity development. ▪ Training on operational guidelines and training manuals. |

⁶These SFCLs are the clients of the SFDB.

⁷A Microfinance and Banking Operation Specialist is assisting SFDB to implement its Restructuring Plan.

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| | benchmarks and implementation schedule | | services in inaccessible hills and mountain districts through alternative modalities at the final stages of implementation. Process started on the procurement of MIS software in SFDB. | |
| Continue strengthening of GBBs | Decision to be undertaken on the future direction of the technically insolvent GBBs. | | NRB shares in four GBBs (Eastern, Central, Western and Mid-Western) were divested and divestment of Far Western GBBs suspended due to its insolvency and requirement of a substantial recapitalization and significant performance improvements. | <ul style="list-style-type: none"> ▪ Decision on privatization of far-western GBB, and ▪ Review the performance of privatized GBBs after divestment. |
| Enhance the supervision and regulation of RFIs | Decision on appropriate supervisory and regulatory framework of RFIs | | GON approved Microfinance Policy 2008 to provide an overall framework for developing RFIs that will provide strong framework for supervision and regulation of RFIs. | <ul style="list-style-type: none"> ▪ Finalize draft microfinance act, and ▪ Capacity development support to Debt Recovery Tribunal and Credit Information Bureau. |
| | Initiation of implementation of supervisory and regulatory framework of the RFIs | | NRB drafted Microfinance Act that outlines establishment of Microfinance Regulation Authority as an autonomous institution to implement the supervisory and regulatory framework for the RFIs. | <ul style="list-style-type: none"> ▪ Capacity development for supervisory and regulatory framework. |
| Develop a systemic sector capacity building mechanism | Incorporation of the training institution pursuant to Companies Ordinance, with necessary financial contribution from NRB, ADBL and other financial institutions | | National Banking Training Institute (NBTI) was established as an educational institution under the Company Act under the leadership of Bankers' Association of Nepal and with share capital from all the commercial banks. Recruitment of CEO from open market has been finalized ⁸ . | <ul style="list-style-type: none"> ▪ Finalization of technical and financial support to NBTI and ▪ Recruitment training consultant and other support staff. |
| | Develop business plans for training, course curriculum and materials, library, training of trainers, and | | Draft business plan for NBTI prepared and management for course curriculum, materials, library, training of trainers, and equipment in process. The business plan is being finalized. | <ul style="list-style-type: none"> ▪ Design of training curricula and ▪ Accreditation with universities (national, regional and global level). |

⁸International Chief Technical Advisor is providing technical backstopping support to NBTI to design operational and management system.

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| | equipment | | | |
| | Start training by the proposed training institution | | NBTI just started actual training course. | <ul style="list-style-type: none"> • Review NBTI training certification process. |
| Reduce vulnerability risks of lenders and borrowers | Development of the pilot crop insurance plan by NRB in consultation with local stakeholders (MOF letter) | | GOA/NRB, in consultation with other technical agencies (World Bank), completed a study on feasibility of crop insurance scheme. No further works has been done on this aspect. | <ul style="list-style-type: none"> ▪ Revisit and re-define scope of product and process innovation component, ▪ Training on market led-approach to new product development, and ▪ Technical support to new product development and process refinement. |