

ASIAN DEVELOPMENT BANK

TAR: NEP 29239

TECHNICAL ASSISTANCE
(Cofinanced by the Government of Germany)

TO THE

KINGDOM OF NEPAL

FOR

STRENGTHENING SELECTED RURAL FINANCIAL INSTITUTIONS

December 2003

CURRENCY EQUIVALENTS

(as of 30 November 2003)

Currency Unit	–	Nepalese rupee/s (NRe/NRs)
NRe1.00	=	\$0.013
\$1.00	=	NRs77.40

The Nepalese rupee is pegged to the Indian Rupee at NRs1.60 to Indian rupee 1.00 and is fully convertible on all current account transactions.

ABBREVIATIONS

ADB	–	Asian Development Bank
ADBN	–	Agricultural Development Bank of Nepal
APP	–	Agriculture Perspective Plan
CTI	–	Central Training Institute
GTZ	–	Deutsche Gesellschaft für Technische Zusammenarbeit (German Agency for Technical Cooperation)
IMF	–	International Monetary Fund
MIS	–	management information system
NGO	–	nongovernment organization
NPL	–	nonperforming loan
NRB	–	Nepal Rastra Bank
RF	–	rural finance
RFI	–	rural financial institution
RFSD	–	rural finance sector development
RTC	–	Regional Training Center
Restructuring Plan	–	Restructuring Plan for the Commercialization of ADBN
SFDB	–	Small Farmers Development Bank
SFDP	–	small farmers development program
TA	–	technical assistance

NOTE

In this report, "\$" refers to US dollars.

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I. INTRODUCTION

1. The Government of Nepal requested Asian Development Bank (ADB) technical assistance¹ (TA) for strengthening selected rural financial institutions (RFIs), especially the Agricultural Development Bank of Nepal (ADB), the key RFI. During fact-finding in October 2002, the Government and ADB agreed to shift the TA from 2002 to 2003 to incorporate the findings of the Financial and Operational Review of ADBN.² Subsequently, an ADB Mission in June 2003 formulated the TA in consultation with Nepal Rastra Bank (NRB), the central bank; ADBN; International Monetary Fund (IMF); and German Agency for Technical Cooperation (GTZ). The TA is included in the 2003 TA program. The TA framework is in Appendix 1.

II. ISSUES

2. Nepal is an overwhelmingly rural and agrarian economy. Over 85% of the population live in rural areas and nearly 80% of the labor force is engaged in agriculture and related activities. Smallholders and marginal farmers operate 90% of the 2.7 million agricultural holdings. Agriculture sector growth has been low and employment, either farm or nonfarm, is mainly in subsistence activities typical of poor and low-income households. This has resulted in a poverty incidence of 38.7% and a per capita gross domestic product of \$241, the lowest in South Asia. Rural poverty incidence is estimated at 44% and inequalities between rural and urban areas have increased. In addition, with a population growth rate of 2.2%, Nepal faces the challenge of absorbing about 300,000 new laborers, mostly rural, every year. Ongoing insurgency has made it difficult to maintain, let alone increase economic growth.

3. Poverty reduction is thus the key challenge for Nepal. Accordingly, the Government's poverty reduction strategy prioritizes macroeconomic policies that support poverty reduction through broad-based economic growth, especially in agriculture, along with emphasis on the social sector, disadvantaged groups, and improved governance. Within agriculture, the Agriculture Perspective Plan (APP) of the Government aims to reduce the sector's structural constraints through emphasis on five inputs—fertilizers, irrigation, roads, power, and extension services—and four outputs—high-value crops, agribusiness, forestry, and livestock. Access to rural finance (RF)³ is a critical input for realizing both poverty reduction⁴ and APP goals.

4. The Government supported the emergence of a diverse range of RFIs for meeting the financing demand⁵ of the rural sector. The formal RF sector, supervised or registered with NRB, comprises 322 rural branches of commercial banks, ADBN with 447 branches, Small Farmers Development Bank (SFDB) with 134 outlets, 10 development banks with 113 branches, 34 savings and credit cooperative societies, and 30 microfinance nongovernment organizations (NGOs). The semiformal sector comprises government-sponsored rural credit programs, about

¹ The TA appeared in *ADB Business Opportunities* (Internet edition) on 9 August 2003.

² TA 3580–NEP: Subcluster 5, *Financial and Operational Review of Agricultural Development Bank of Nepal and Nepal Industrial Development Corporation* associated with ADB. 2000. *Report and Recommendation of the President to the Board of Directors on a Proposed Loan to the Kingdom of Nepal for the Corporate and Financial Governance Project*. Manila.

³ RF in this document, includes savings credit, and payment services. From the client's perspective, RF can be classified as financial services provided to rural farm and nonfarm households, a large proportion of which are poor and low-income households. While RFIs also serve poor, low-income households, and the non-poor, the microfinance institutions exclusively focus on the poor. Microfinance is primarily rural. In this document the term "RF" or "RFI" is inclusive of "microfinance" or "microfinance institutions," respectively. The term "microfinance" or "microfinance institutions" is used only for specific microfinance related reference.

⁴ The poverty partnership agreement between Nepal and ADB aims to reduce poverty to less than 10% by 2017.

⁵ The annual aggregate demand, including that under the APP, is estimated at NRs20 billion per annum.

1,600 savings and credit cooperative societies registered under the Cooperatives Act, and about 60 multisectoral NGOs. The Rural Microfinance Development Center⁶ wholesales funds for onlending to the rural poor. The informal sector comprises moneylenders, traders, friends, relatives, and about 12,000 community organizations.

5. Despite the extensive network, the RFIs have inadequate outreach and are concentrated in the plains. They collectively disburse about NRs7 billion per annum and the outreach is estimated at 23% of the rural population. The majority of the rural households rely on informal credit. However, only 13% of such borrowings are for productive assets and the cost of credit from informal sources leaves little, if any, surplus with the households. In addition, the RF sector is characterized by weak governance, poor repayment rates, high transaction costs, recurring losses, and high nonperforming loans (NPLs).⁷ The high-risk perception of RF has deterred commercial banks from expanding their RF portfolio.⁸ The contribution of RF to rural growth through investments in agriculture and nonfarm activities for value addition and employment generation in rural economy thus remains unfulfilled.

6. Concerned about the systemic weaknesses, the Government has anchored RF sector reforms with the ongoing financial sector reforms to improve the policy and legal framework, enhance private sector participation, strengthen governance and supervision, and improve accounting and auditing. Consistent with the Government's reform agenda, ADB prioritized its assistance to enhance the access of poor households to microfinance. ADB assistance to the financial sector aims to strengthen corporate and financial governance, and includes portfolio audit, diagnostic study, and restructuring plan for ADBN (footnote 2). Building on these initiatives, the TA and the pipeline RF sector development (RFSD) loan for 2005 aim to develop sustainable RFIs.

7. With the largest branch network in the country, ADBN accounts for about 55% of the rural credit outstanding and three fourths of agriculture credit. ADBN deposits and loan outstanding amounted to NRs21 billion and NRs23 billion, respectively, at end-2002. The average outstanding loan size of NRs5,164 suggest access to low-income households. SFDB, a fully-owned ADBN subsidiary, wholesales funds to small farmers development program (SFDP) initiated by ADBN in 1975. GTZ is assisting SFDP clients to organize into small farmers cooperatives and link them with SFDB.

8. As a government-owned bank, ADBN for the most part operated under a paradigm that repressed viable financial intermediation through controls on pricing and client selection. The diagnostic study highlighted weak governance, inefficiencies, and heavy overheads. In addition, deficiencies in loan appraisal and delinquency management contributed to low repayments and accumulation of NPLs. Portfolio audit assessed ADBN's NPL at 38% of the portfolio in terms of the prudential norms applied to commercial banks in Nepal compared with the 28% reported by ADBN.⁹ On organizational and institutional aspects, the diagnostic study found that governance, transparency, corporate planning, management information system (MIS), human resource management, accounting, and auditing require significant improvements. Channelling numerous government programs diluted the core financial intermediation focus of ADBN and contributed to

⁶ Implementing agency for ADB. 1998. *Report and Recommendation of the President to the Board of Directors on a Proposed Loan to the Kingdom of Nepal for the Rural Microfinance Project*. Manila.

⁷ ADB. 2000. *Rural Finance Development in Nepal: A Medium-term Strategy*. Manila.

⁸ Nepal Bank Limited and Rastriya Banijya Bank, with 95% of commercial bank rural branches, have closed 55 rural branches. Further branch closures, mainly rural, are expected as part of the World Bank-assisted restructuring.

⁹ Restated financial statements reflect a net loss and capital erosion. NPLs are as high as 48% when internationally accepted prudential norms are applied.

poor portfolio quality. SFDB, SFDP, and small farmers cooperative-related responsibilities, which together account for about one fourth of ADBN's loan portfolio, overstretch ADBN's managerial capacity. Accordingly, the diagnostic study recommended that SFDP-related responsibilities be transferred to SFDB and the organizational and financial status of SFDB be separately evaluated to ensure its sustainability as a microfinance institution.

9. The Restructuring Plan for the Commercialization of ADBN,¹⁰ based on the portfolio audit and diagnostic study findings, and developed with ADBN and Government participation, aims to transform ADBN into a sustainable bank with the following reform framework to be implemented over a 3-year period:

- (i) **Legal, ownership, and governance.** ADBN will be incorporated under the proposed Banks and Financial Institutions Ordinance¹¹ with a board of directors drawn from professionals. The majority equity stake over the medium term will remain with the Government, as private sector participation is unlikely unless the Restructuring Plan is completed.
- (ii) **Financial restructuring.** Capitalization and adequate provisioning for bad and doubtful assets will be undertaken based on NRB norms for commercial banks.
- (iii) **Organizational restructuring.** The organization will be rationalized around a profit-center concept, and rightsized through a voluntary separation scheme.
- (iv) **Institutional strengthening.** Business processes including products, services, systems, and procedures will be reoriented; information technology and MIS system upgraded; and training capacity and staff skills enhanced.

10. ADBN has endorsed the Restructuring Plan, the implementation of which is also a requirement under IMF's Poverty Reduction and Growth Facility (footnote 11). The Restructuring Plan requires ADBN to enhance its training capacity for mainstreaming RF best practices. Priority support areas identified by the Restructuring Plan for skills development include (i) corporate planning for a structured approach to institutional transformation; (ii) credit appraisal and loan management for improving the repayment rate and minimizing NPLs; (iii) risk management for reducing credit, price, operational, and liquidity risks; and (iv) accounting, audit, and internal controls for enhancing good governance and transparency. These skills are necessary to adopt the profit-center concept, which requires decision-making capacity at regional and branch levels before personnel are realigned.

11. The TA supports implementation of the Restructuring Plan through capacity building for the Central Training Institute (CTI) and regional training centers (RTCs) for training in the priority areas (para. 10). This will contribute to the strengthening of the RF sector because a reformed ADBN, considering its nationwide network often at unserved remote rural areas, can significantly enhance outreach. The sustainability of ADBN is also important to encourage commercial banks to actively pursue RF operations (para. 5 and footnote 8). The TA will allow active ADB participation in implementing the Restructuring Plan and facilitate the design of the proposed RFSD loan.

¹⁰ Developed as part of TA 3580–NEP: Subcluster 5 (footnote 2).

¹¹ The enactment of the Banks and Financial Institutions Ordinance governing all financial institutions is a condition for the \$72 million Poverty Reduction and Growth Facility of the IMF approved on 14 November 2003.

III. THE TECHNICAL ASSISTANCE

A. Purpose and Output

12. The objective of the TA is to enhance the capacity of CTI and RTCs to offer training services for the professional development of ADBN staff. Enhanced training capacity and the resulting staff skills are critical to the successful implementation of the Restructuring Plan and to transform ADBN into a sustainable bank that can significantly contribute to poverty reduction and the APP goals. The TA will support the following:

- (i) **The corporate plan including training plan, training materials, and operating manuals.** This will cover: (a) training on developing and updating a corporate plan; (b) the corporate plan and a training plan; (c) curricula to be conducted through CTI and RTCs; (d) training materials and manuals for credit appraisal for farm and nonfarm activities and loan management procedures; (e) training materials and manuals for risk management best practices and plan for introducing risk management policies and procedures; and (f) training materials and manuals for internal audit and for mainstreaming accounting codes and practices consistent with commercial banks.
- (ii) **Training senior management and staff.** This will cover: (a) training for trainers of CTI and RTCs; and (b) training in corporate planning, credit appraisal, loan portfolio management, risk management, and internal audit and accounting procedures for 100 senior management staff and 500 operational staff of ADBN, through CTI and RTCs' trainers.
- (iii) **Financial and operational review of SFDB.** The review will cover: (i) detailed portfolio audit and diagnostic study of SFDB including SFDP; (b) assessment of the quality of ADBN loan and investment in SFDB and SFDP; and (c) restructuring options along with implementation plan for SFDB.

B. Methodology and Key Activities

13. The corporate plan including the training plan will ensure that TA inputs are consistent with and contribute to the Restructuring Plan objective (para. 9). Priority staff are the managers at all levels, who should have improved knowledge and skills both to manage the change and to lead the on-the-job training that will be essential for successfully implementing the Restructuring Plan. Implementation will allow flexibility to modify team compositions as the work progresses. Appropriate methodologies will be applied to capture the perspectives of staff for continuous improvements in design and delivery of training inputs that will qualify staff for (i) new posts, (ii) new responsibilities in current posts, and (iii) responsibilities of the next higher post. After the training of trainers, CTI and RTCs' trainers will design and conduct training courses under the supervision of the TA consultants. This activity will (i) ensure that CTI and RTCs develop skills for meeting evolving training needs, and (ii) facilitate replication of training either through ADBN funds or the proposed RFSD loan support. Similarly, SFDB review will provide restructuring options that can be considered for funding by the proposed RFSD loan.

C. Cost and Financing

14. The total cost of the TA is estimated at \$610,000 equivalent, comprising \$285,000 in foreign exchange costs and \$325,000 equivalent in local currency costs. The TA will be financed on a grant basis by the Government of Germany in the amount of \$15,000 equivalent,

to be administered by ADB, and ADB's TA funding program in the amount of \$500,000 equivalent. ADB will finance the entire foreign exchange costs and \$230,000 equivalent of local currency cost. ADBN will finance the remaining \$95,000 of the local currency cost. Cost estimates and financing plan are in Appendix 2.

D. Implementation Arrangements

15. ADBN will be the Executing Agency for the TA and will form a TA steering committee comprising the general manager; deputy general manager; division chiefs of banking operations, branch operations, and microfinance; the chief of CTI; and representatives of RTCs, SFDB, and NRB. The TA steering committee, chaired by the general manager, will be responsible for overall implementation. ADBN will provide offices at CTI for the consultants and place the equipment purchased under the TA at the disposal of the consultants for the duration of the TA. In addition, ADBN will provide, on a full-time basis for the duration of the TA, (i) one senior staff member of CTI as counterpart staff for the consultants, (ii) secretarial services, (iii) local communications facilities, (iv) one vehicle to the consultants for travel in Kathmandu, and (v) venues and assistance for all workshops and training sessions, in Kathmandu and in the field.

16. The TA will be implemented over 8 months, from February 2004 to October 2004. Tripartite review meetings involving the Government, the TA consultant, and ADB and GTZ will be organized by ADBN thrice during the TA period in conjunction with ADB missions to review implementation and resolve any outstanding issue. The general manager of ADBN will chair the meetings, and members of the TA steering committee will attend the meetings. International consulting services of 10 person-months and domestic consulting services of 30 person-months will be required. The terms of reference for consulting services are in Appendix 3. The consultants will be specialists in training, corporate planning, credit appraisal, risk management, audit and accounting, MIS, and diagnostic studies. They will be engaged in accordance with ADB's *Guidelines on the Use of Consultants* and other arrangements satisfactory to ADB for engaging of domestic consultants. The quality- and cost-based selection method with simplified technical proposals will be used in selecting the consulting firm.

17. The TA consultants will prepare (i) an inception report including a detailed work program, to be submitted within 3 weeks of the start of the TA and to be discussed at the initial tripartite review meeting; (ii) quarterly progress reports on overall work progress during the period under review, the work program for the following quarter, and any outstanding issue; (iii) an interim report presenting draft outputs, to be submitted within 6 months of the start of the TA and to be discussed at the interim tripartite review meeting; (iv) a draft final report compiling all TA activities and consultants' recommendations, to be submitted at least 1 month before TA completion and to be discussed at the final tripartite review meeting; and (v) a final report at the completion of the TA for final evaluation jointly by ADBN, ADB, and GTZ.

IV. THE PRESIDENT'S DECISION

18. The President, acting under the authority delegated by the Board, has approved (i) ADB administering a portion of the technical assistance not exceeding the equivalent of \$15,000 to be financed on a grant basis by the Government of Germany, and (ii) ADB providing the balance not exceeding the equivalent of \$500,000 on a grant basis, to the Government of Nepal for Strengthening Selected Rural Financial Institutions, and hereby reports this action to the Board.

TECHNICAL ASSISTANCE FRAMEWORK

Design Summary	Performance Indicators	Monitoring Mechanism	Risks and Assumptions
<p>Goal Transform Agricultural Development Bank of Nepal (ADB) into a sustainable bank with enhanced outreach</p>	<p>ADB Restructuring Plan implementation initiated and milestones corresponding to the end of the technical assistance (TA) achieved</p> <p>Professional skills in priority areas imparted to ADB staff and management</p>	<p>ADB Restructuring Plan implementation report</p> <p>Nepal Rastra Bank (NRB) reports</p> <p>ADB performance reports and financial statements</p> <p>TA progress reports</p> <p>Asian Development Bank (ADB) review missions</p>	<p>Commitment of the Government of Nepal, NRB, and ADB to pursue policies and practices conducive to development of the rural finance sector is sustained.</p> <p>Political and security circumstances do not worsen.</p> <p>Financial and economic reforms continue.</p>
<p>Objectives Develop the capacity of the Central Training Institute (CTI) and Regional Training Centers (RTCs) of ADBN</p>	<p>CTI and RTCs' staff trained and acquire best practices in design and delivery of training courses by April 2004</p> <p>All CTI and RTCs' trainers trained in corporate planning, credit appraisal, loan management, risk management, and accounting and auditing by May 2004</p>	<p>ADB Restructuring Plan implementation report</p> <p>CTI and RTCs' reports</p> <p>TA progress reports</p> <p>ADB review missions</p>	<p>Participation of CTI and RTCs to learn the skills for design and delivery of training is proactive.</p> <p>Conduct of training courses is timely.</p>
<p>Outputs (i) Corporate plan including training plan, training materials, and operating plans</p>	<p>Corporate plan including a training plan developed by April 2004</p> <p>Curricula and training materials developed by July 2004</p> <p>Operational guidelines and manuals for ADBN developed by July 2004</p>	<p>ADB Restructuring Plan implementation report</p> <p>CTI and RTCs' reports</p> <p>TA progress reports</p> <p>ADB review missions</p> <p>Corporate plan, including training plan</p> <p>Number and quality of training materials</p> <p>Number and quality of operational guidelines and manuals</p>	<p>CTI and RTCs are committed to skills and quality enhancement.</p> <p>Qualified and motivated trainers available at CTI and RTCs.</p> <p>Qualified consultants are available.</p>

Design Summary	Performance Indicators	Monitoring Mechanism	Risks and Assumptions
<p>(ii) Training of management and staff of ADBN</p> <p>(iii) Financial and operational review and restructuring plan for SFDB (Small Farmers Development Bank), a subsidiary of ADBN</p>	<p>100 senior management and 500 operational staff trained by October 2004</p> <p>Guidelines and manuals put into operation through trained staff by October 2004</p> <p>SFDB financial and operational aspects including ADBN's investments in SFDB analyzed by July 2004</p> <p>Findings of portfolio audit and diagnostic study confirmed by SFDB and ADBN by August 2004</p> <p>SFDB restructuring options developed by October 2004</p>	<p>ADBN Restructuring Plan Implementation report</p> <p>NRB reports</p> <p>CTI and RTCs' reports</p> <p>TA progress reports</p> <p>ADB review missions</p> <p>ADBN performance reports and financial statements</p> <p>TA progress reports</p> <p>ADB review missions</p> <p>Portfolio audit, diagnostic study, restructuring options, and implementation plan</p>	<p>Management and staff attend training courses in expected numbers.</p> <p>Willingness of ADBN staff to acquire and practice new skills for improving service quality.</p> <p>SFDB participation in terms of information disclosure is proactive.</p>
<p>Inputs</p>	<p>Consulting inputs of 10 international person-months and 30 domestic person-months in the areas of training, corporate planning, credit appraisal, risk management, portfolio management, management information system, auditing and accounting, portfolio audit, and diagnostic studies</p> <p>Financial inputs: ADB: \$500,000; GTZ: \$15,000; and ADBN: \$95,000</p>	<p>TA progress reports</p> <p>ADB review missions</p> <p>Tripartite meetings</p>	<p>Timely fielding of adequately qualified consultants.</p> <p>Government, ADBN, and SFDB commitment to TA objective.</p>

COST ESTIMATES AND FINANCING PLAN
(\$)

Item	Foreign Exchange	Local Currency	Total Cost
A. Asian Development Bank Financing^a			
1. Consultants			
a. Remuneration and Per Diem			
i. International Consultants	210,000	0	210,000
ii. Domestic Consultants	0	90,000	90,000
b. International and Local Travel	25,000	5,000	30,000
c. Report and Communication ^b	0	10,000	10,000
2. Equipment ^c	10,000	20,000	30,000
3. Workshops	0	5,000	5,000
4. Training ^d	0	60,000	60,000
5. Government Representative Contract Negotiations	0	5,000	5,000
6. Miscellaneous Administration and Support	0	15,000	15,000
7. Contingency	40,000	20,000	60,000
Subtotal (A)	285,000	230,000	515,000
B. Government Financing			
1. Office Facilities	0	40,000	40,000
2. Counterpart Staff	0	25,000	25,000
3. Local Transport	0	15,000	15,000
4. Workshops	0	5,000	5,000
5. Surveys	0	5,000	5,000
6. Others	0	5,000	5,000
Subtotal (B)	0	95,000	95,000
Total	285,000	325,000	610,000

^a Financed by the Asian Development Bank's technical assistance funding program (\$500,000 equivalent) and by the Government of Germany (German Agency for Technical Cooperation) (\$15,000 equivalent).

^b Including translation.

^c Computers and printers (5 sets x \$2,000); projectors (2 x \$5,000); and photocopiers (2 x \$5,000).

^d Budgeted at \$100 per head for 600 participants.

Source: Asian Development Bank estimates.

TERMS OF REFERENCE FOR CONSULTING SERVICES

A. Overview

1. The technical assistance (TA) will strengthen the Central Training Institute (CTI) and Regional Training Centers (RTCs) of the Agricultural Development Bank of Nepal (ADB) to support its transformation into a sustainable bank. A Restructuring Plan for the Commercialization of ADB (the Restructuring Plan) sets out the details for this transformation. The capacity of CTI and RTCs will be enhanced through training of trainers. The TA will also support portfolio audit and diagnostic study of the Small Farmers Development Bank (SFDB), a subsidiary of ADB.

B. Scope of Work

2. Consulting services comprising 10 person-months international and 30 person-months domestic will be required. The specific tasks follow:

1. **Bank Training Specialists** (international team leader, 3 person-months; domestic, 7 person-months)

3. The team leader will have at least 10 years experience in training and organization of bank training departments or institutes, or equivalent experience in a senior position in a bank training institute or the training division of a major international commercial bank. The team leader will work with ADB senior management for ensuring the smooth implementation of the TA. Working in 3 phases, the team leader, will be assisted by a domestic specialist with 5 years of relevant experience. The specialists will be responsible for the following:

- (i) Assist the corporate planning team (CPT) to integrate the recommendations of the Restructuring Plan into a corporate plan; and assist in finalizing the training plan as a subset of the corporate plan.
- (ii) Coordinate the work of the TA consultants and ensure that all training materials and courses, operational manuals and guidelines, and reports are prepared to the highest quality; and ensure that training inputs are in line with the Restructuring Plan recommendations.
- (iii) In close consultation with the general manager of ADB and the CTI director, review the qualification, experience, attitudinal characteristics, and motivation of staff members of CTI and RTCs and make recommendations as appropriate, including recruiting new staff if necessary; review the organization of the training function in ADB and recommend improvements including, as appropriate, the closure, amalgamation, or relocation of RTCs; and review ADB training materials and evaluate their relevance to ADB's transformation into a sustainable rural bank.
- (iv) Prepare a training curriculum for training CTI and RTCs' staff for their increased training responsibilities; and develop a curriculum of core banking skills and professional development to support new policies, procedures, and systems in accordance with rural finance best practices.
- (v) Supervise the preparation of (a) courses (corporate planning, credit appraisal, loan management, risk management, and accounting and internal audit); (b)

training materials (handouts, overheads, study guides, teaching aids, and timetables); and (c) operating manuals; train¹ CTI and RTCs' trainers; and guide CTI and RTCs' trainers in conducting training courses for ADBN staff.

2. Corporate Planning Specialists (international, 2 person-months; domestic, 3 person-months)

4. The international corporate planning specialist will have at least 5 years relevant international experience in a large commercial bank and will be assisted by a domestic specialist with 3 years relevant experience. The specialists will be responsible for the following:

- (i) Assist ADBN to establish a CPT and to define the roles and responsibilities of each individual in the CPT in the corporate planning process.
- (ii) Prepare corporate planning manual and associated training materials; and deliver training in corporate planning to the CPT, and CTI and RTCs' trainers.
- (iii) Through a series of workshops, assist the CTI to plan and deliver appropriate training in the elements of corporate planning to ensure broad-based participation.

3. Credit Appraisal Specialists (international, 2 person-months; domestic, 3 person-months)

5. The credit appraisal specialists will have 5 years relevant experience and will work with the related operational departments to improve lending procedures, develop appraisal techniques, and design training courses and operating manuals. Working in close coordination with the risk management specialists, the credit appraisal specialists will be responsible for the following:

- (i) Specify the requirements of credit appraisal for different types of lending, and advise ADBN on modifications necessary in the current procedures; develop credit appraisal models, test the models, and advise ADBN on improvements and problem solving during the process; and wherever applicable, provide exposure to computerized appraisal techniques.
- (ii) Prepare operating manuals on credit appraisal—including the criteria for small loans to poor women—and loan management; develop a 2-week training course including training materials; train CTI and RTCs' trainers; and guide CTI and RTCs in the delivery of credit appraisal and loan management training courses to ADBN staff.

4. Risk Management Specialists (international, 2 person-months; domestic, 3 person-months)

6. The risk management specialists will have 5 years relevant experience and will work with ADBN departments to prepare a risk management plan, develop training materials and operating manuals, and train ADBN staff. The specialists will be responsible for the following:

¹ Each specialist will conduct 2 training courses for the CTI and RTCs' staff and guide them in delivering 2 courses.

- (i) Based on the Restructuring Plan recommendations, review the credit, market, operational, pricing, and liquidity risk exposures of ADBN.
- (ii) Prepare a risk management policy, define the procedures and tools required for effectively implementing the policy at the branch and bank levels; identify additional risk exposures that may arise from development of new products and services and make recommendations for managing such risks; assist to prioritize risk management policies and procedures based on the relative exposures of ADBN to different types of risk; prepare a phased plan for the progressive introduction of improved risk management procedures over the medium term; and assist the management information system (MIS) specialist to identify information needs for incorporation in the MIS needs analysis.
- (iii) Prepare a risk management manual for enhanced risk management practices in ADBN and a 2-week training course including training in applying risk management models; train CTI and RTCs' trainers; and guide CTI and RTCs in the delivery of risk management training courses to ADBN staff.

5. Internal Audit and Accounting Specialists (international, 1 person-month; domestic, 6 person-months)

7. The internal audit and accounting specialists will have 5 years relevant experience and will work with concerned ADBN departments, CTI, and RTCs for implementing an effective internal audit system and accounting standards consistent with international accounting standards (IAS), as recommended in the Restructuring Plan. The specialists will be responsible for the following:

- (i) Determine the specific changes in statutory reporting requirements for ADBN to bring it at par with the requirements of the Nepal Rastra Bank (NRB) for commercial banks and to produce accounts to IAS; and identify additional measures necessary to meet IAS in full by end-2004.
- (ii) Determine the specifics of internal audit management systems and reporting in ADBN including the need for effective management of the loan portfolio, interest rate, foreign exchange, pricing, and liquidity risks.
- (iii) Formulate a plan for establishing an improved internal audit system and corresponding MIS that will satisfy the requirements for internal audit, IAS, and effective risk management; define reporting coverage and frequency; prepare and deliver three seminars for the CPT and senior ADBN staff on internal audit and accounting changes and subsequently develop policies for adoption by the board of directors of ADBN; develop operating manuals and training materials and train CTI and RTCs' staff for training ADBN staff on how to institute and operate the systems within the constraints of ADBN's present information technology systems; and document the requirements for future upgrading of the internal audit and accounting functions with improvements in information technology software and hardware.

6. MIS Specialist (domestic, 2 person-months)

8. The specialist will have 5 years relevant experience and will work with the Planning Department, the Accounting Department, the Informatics Center and other divisions as required to define in detail the MIS requirements for full implementation of IAS and the provision of adequate information for prudent risk management in ADBN. The specialist will be responsible for the following:

- (i) Review the needs for management reporting in ADBN including for effective risk management, accounting, and internal audit; assess the required improvements in MIS consistent with NRB and IAS requirements; formulate recommendations for establishing an improved MIS that will satisfy the requirements of IAS and effective risk management; and integrate the findings with the recommended outputs of other specialists recruited under the TA.
- (ii) Assist ADBN to identify changes that can be implemented within the constraints of its present information technology systems and prepare an implementation plan for completion in 2004.
- (iii) Prepare a phased plan for progressively introducing an improved MIS during the corporate plan period, taking into account the priorities for developing new products and services and improved risk management practices; and conduct workshops for CPT and senior ADBN staff on MIS development.

7. Portfolio Audit Specialist (domestic, 4 person-months)

9. The specialist will have 5 years relevant experience and will analyze a sample of SFDB loan portfolio, using existing audit reports, additional data, and field assessment. The specialist will be responsible for the following:

- (i) Characterize the conduct of SFDB's loan and investment activity (approval and disbursement) and outstanding over the 3 year period covered by the audit; describe the sectoral composition of loans in the outstanding portfolio; describe the performance of the portfolio in terms of loan income, dividends, cost of funds, returns from liquid asset investment taking into account adjustments made through reclassification, rescheduling, cancellations, and prepayments; and assess the quality of loan portfolio using international standards applicable to microfinance institutions.
- (ii) Analyze the quality and performance of SFDB's loan and liquid asset portfolios; assess nonperforming loans and the estimated provisioning requirements; and assess asset quality, earnings, liquidity, and capital in accordance with international standards.

8. Operational Diagnostic Specialist (domestic, 2 person-months)

10. Drawing on the analysis of the portfolio audit specialist, the operational diagnostic specialist will assess the whole gamut of institutional and operational issues to determine ways of improving efficiency. The operational diagnostic specialist will have 5 years relevant experience and will be responsible for the following:

- (i) governance, organizational structure, and administration, including institutional and incentive structures, autonomy and accountability, and staff skills and orientation;
- (ii) corporate planning process and planning and budgeting cycle;
- (iii) range of products and services, adaptability to demand; and quality;
- (iv) credit procedures and practices, including description of loan assessment and process; loan monitoring, review, and grading procedures; management of problem loans; legal environment and recovery against security; loan loss provisioning policy; and staff skills in loan portfolio management;
- (v) MIS, including management and financial information and flow and adequacy of such information for risk management;
- (vi) accounting procedures and standards used, their comparison with international accounting standards, and adequacy of accounting policies;
- (vii) cost of operation, with estimates of the degree of subsidy at each level;
- (viii) internal and external audit, and fiduciary management to assure the safety of depositors' funds; and
- (ix) liquidity in terms of deposit volatility, requirement and sources of funds, ease of conversion of noncash assets, and policies and procedures for liquidity and asset management.

11. Based on the diagnostic, the specialist will develop restructuring options for SFDB. These may include possible changes in

- (i) overall policies, laws, regulations, and relationship of ADBN and SFDB;
- (ii) organizational structure and staffing, training, and human resource arrangements;
- (iii) strategic planning, financial management, budgeting and management, and statutory financial reporting;
- (iv) savings policies and operations;
- (v) policies on credit, portfolio management, and risk management functions including credit risk, interest rate risk, and funding; and
- (vi) management information and data processing systems.