

NEPAL

Rural Finance Sector Development Cluster Program



Access to reliable and affordable financial services is needed so that the rural poor in Nepal can capture the opportunities of the reviving economy and break the vicious cycle of poverty. Increased financial intermediation will enable resources to flow to the rural sector, giving the poor opportunities to invest in productive activities, reconstruct their livelihoods, and improve their incomes, as well as contribute to political and economic stability. Yet, access to formal institutional financial services in Nepal is severely limited, reaching about 33% of the total population.

Rural finance can be deepened significantly and rapidly to reduce poverty in Nepal by revitalizing and enhancing the network of rural finance institutions. The high-risk rural finance profile, repressive policy environment,

and security concerns in rural areas make private sector participation extremely difficult. Additionally, difficult terrain and topography inhibits rapid deployment of private institutional finance services on a larger scale. Wider sector reform is required to address the policy and institutional bottlenecks to growth and development of efficient and sustainable rural finance services for the poor.

The Asian Development Bank (ADB) approved the Rural Finance Sector Development Cluster Program (RFSDCP) for Nepal in October 2006. The program was designed to support the growth and development of the rural finance sector, including microfinance, to help reduce poverty, generate employment, and improve agricultural productivity, through enhanced private sector investment.

PROJECT RESULTS

Favorable policy environment. The first program has been effective in creating a favorable policy environment, through reforming repressive rural finance policies such as phasing out a priority sector lending scheme and removing interest rate ceilings; restructuring and increasing private sector participation in key rural finance institutions including the Agricultural Development Bank Limited (ADBL); enhancing rural finance outreach through the Small Farmers Development Bank (SFDB); and supporting sector capacity building by establishing a National Banking Institute (NBI) for professional banking and financial training.

Key reforms. Several key reforms of the ADBL and the SFDB have been carried out, including the sale of shares, organizational restructuring and adoption of a voluntary retirement scheme, and improvements in financial and operational performance. The restructuring and reform initiative at the ADBL was effective in transforming it into a universal bank. At the SFDB, a cadre of professional staff is being developed and the bank is becoming an independent wholesale provider of rural finance services. The performance parameters of the ADBL and the SFDB have significantly improved. Capacity building has also received a boost with NBI providing training in rural finance.

Several aspects of the program have contributed to poverty reduction, including policy actions and reforms creating an enabling policy environment; institutional restructuring and reforms in the ADBL, the SFDB, and Grameen Bikas banks— regional rural development banks; the creation of a supportive legal and regulatory framework; and sector capacity development. The latest estimates from the Nepal Planning Commission indicate that poverty incidence nationally has been reduced to 25% and the incidence of rural poverty has been reduced to 30%.

The program was also designed to address the fundamental weaknesses in the rural finance sector in Nepal, resulting from extensive politicization, repressive policies, interference

in loan collection, and market distortions—all of which discourage private sector-led rural finance intermediation. While commercial banks, including development banks, are

gradually increasing their rural presence, due to cost considerations in small transactions, their rural networks are still limited.

With a comprehensive reform agenda, the RFSDCP has five components: favorable policy environment, institutional restructuring and reforms, supportive legal and regulatory framework, sector capacity building, and product and process innovations.

The project is in line with the strategic directions of ADB's South Asia Department. The strategy focuses on sustainable infrastructure, climate change mitigation and adaptation, human development, regional cooperation and integration, public-private partnership, and good governance.



The Small Farmers Development Bank restructuring plan prioritized assistance to strengthening of microfinance and banking operations.



The program supported the divestment and transformation of Grameen Bikas banks into effective microfinance service providers.

The program promotes self-employment, and micro and small enterprise development

PROJECT AT A GLANCE

Cost and financing: Asian Development Fund (Loan), \$56.0 million; Asian Development Fund (Grant), \$8.7 million; Japan Special Fund, \$1.1 million; Counterpart, \$100,000

Project approval date: 26 October 2006

Project themes: Sustainable economic growth, governance

Status of project implementation: Completed

Loan closing date: 20 December 2007

Executing agency: Ministry of Finance

FOR INFORMATION

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Link to South Asia Project Briefs:
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Sources: Project Data Sheet. <http://www.adb.org/projects/36169-013/main>; ADB. 2013. *Completion Report for the Rural Finance Sector Development Cluster Program in Nepal*. Manila. <http://www.adb.org/projects/documents/rural-finance-sector-development-cluster-program-pcr>; ADB. 2006. *Report and Recommendation of the President to the Board of Directors: Proposed Sector Development Program Cluster of Loans, Asian Development Fund Grant, and Technical Assistance Grant for the Rural Finance Sector Development Cluster Program in the Kingdom of Nepal*. Manila. <http://www.adb.org/projects/documents/rural-finance-sector-development-cluster-program-rrp>



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