

Nepal Rastra Bank (Central Bank)

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Brief History

Nepal Rastra Bank (NRB), the central bank of Nepal, was established in 1956 with the central banking responsibilities of guiding the development of the embryonic domestic financial sector. The role and responsibilities of NRB have been recast by the new NRB Act of 2002, which entails monetary and foreign exchange policies, development of a secure, healthy and efficient system of payments; supervision of the banking and financial system; and enhancement of the public confidence in Nepal's entire banking and financial system.

Involvement in Microfinance

NRB mandate incorporates supervision, regulation and monitoring of all commercial banks, development banks, finance companies, and licensed NGOs and cooperatives engaged in microfinance. More specifically, the microfinance department of NRB supervises microfinance organisations, manages development finance projects and operates a refinancing window for MFIs. NRB imposes 'priority sector' lending to commercial banks, which entails lending a certain percentage of their deposit / loan portfolio to an underserved population, including typical microfinance clients. NRB has recently decided to phase out its priority sector credit policy by 2007, but the 3% deprived sector credit requirement will stay in place, and include microfinance.

Under the priority sector lending agenda, the central bank led different initiatives, such as the Intensive Banking Program, which introduced group guarantee mechanisms instead of formal collateral, the Production Credit for Rural Women (PCRW) and Micro-Credit for Women (MCPW), which targeted low-income women, and were supported by donor agencies such as IFAD and the ADB.

Between 1992 and 1996, NRB established five Regional Rural Development Banks (RRDBs), using the Grameen Bank methodology, each one operating in a separate development region. Being the main shareholders in the RRDBs, the NRB has initiated a restructuring program to improve the performance of RRDBs, which will result ultimately in their privatization. In the Western region, the most profitable RRDB will soon be a private entity, as already 90% of its shares are sold to private investors. NRB envisages of keeping only a 10% stake. A second RRDB, operating in the Eastern region, also profitable, should be privatized by the end of 2004. The three remaining RRDBs, operating at a loss, will continue to be restructured in the coming 2 to 3 years, before being privatized as well - the NRB only keeping a minority shareholder position (10%).

NRB holds a 26% participation in the Rural Microfinance Development Centre (RMDC), which provides wholesale funds to regulated microfinance organisations, mostly to Grameen Bank replications.

NRB manages the Rural Self-Reliance Fund (RSRF) established in 1990 by the government of Nepal, and supported financially by an allocation of public funds, completed by replenishments from NRB and occasional donor support. RSRF provides wholesale funds to organisations offering financial services in rural areas, such as, Savings and Credit Organisations (SCO), NGOs, and Grameen replications. Funds lent to SCOs and NGOs are charged with 8% interest rate, which is reduced to 2% in case of 100% repayment. Funds lent to Grameen replications are indexed on the lowest re-finance rate of NRB, i.e. 4.5%. A loan portfolio of Rs. 19.2 million is outstanding as of mid January 2004, with organisations working in more than 46 of the 75 districts of the country.

NRB also acts as supervisory body and coordinator for targeted development finance project funded by donor agencies such as IFAD, CIDA, or the ADB. It includes the 'Poverty alleviation in Western

Tarai’, the ‘Community Ground Water Irrigation sector project’ and the ‘Third Livestock Development Project (TLDP)’.

Regulatory Framework

In Nepal, microfinance activities are regulated under the newly promulgated “Bank and financial ordinance 2004”, which covers category D ‘Microfinance Development Banks’, not allowed to perform regular development bank activities, and category E. ‘NGOs as financial intermediaries’. The ordinance includes the two specific acts promulgated by the parliament in recent years.

- *Development Bank Act 1996*: supervises development banks involved in microfinance, the five public Regional Rural Development Banks and the four private development banks created from the transfer of the microfinance portfolio of NGOs such as Nirdhan and CSD.
- *Financial Intermediary Societies Act 1998*, amended in 2002. This law after the first amendment in 2002 enables NGOs to collect savings from their group members. It is less restrictive than it was before the amendment. In addition, NGO directors must provide a personal guarantee for the loans taken by their NGOs from commercial banks. The Chief District Officer at the local government level has the power to take punitive action against NGOs. The transformation of NGOs into development banks was a protection for NGOs staff and directors.

Distinctive Features

NRB has been playing an unusual developmental role in managing targeted microfinance oriented programs. It justified its intervention by the limited involvement of commercial banks in rural finance, and the almost non-existence of a formal microfinance market, some years ago. NRB now aims at decreasing its direct lending in development finance, playing a more traditional role of monitoring and supervision. NRB also plans to develop a national policy on microfinance, which will improve coordination in the involvement of public organisations in microfinance and provide more focus. NRB is receiving assistance from ADB in improving the regulatory framework for microfinance.

Sources

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