FINANCIAL STABILITY REPORT

Nepal Rastra Bank

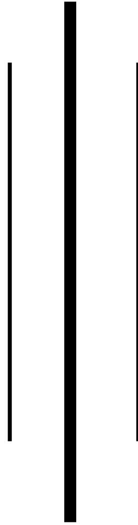
Central Office

Baluwatar, Kathmandu

July, 2015

FINANCIAL STABILITY REPORT

(Issue No. 6)



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This sixth issue of the Financial Stability Report is based on the provisional data of Bank & Financial Institutions (BFIs) and other financial institutions as of mid-January 2015. Data used in its analysis may thus differ from the most recent statistics or audited final data published by BFIs. All the findings, interpretation and conclusions expressed in this report do not necessarily reflect the views of Nepal Rastra Bank or its Board of Directors. The colors, boundaries, denominations or any other signs and symbols used in the report do not imply any metamorphic judgments. This report, unless or otherwise stated elsewhere, covers the developments and risks during the year to mid-January 2015. All the data and information in this report are retrieved from NRB depository, unless stated.

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GOVERNOR

Foreword

Financial Stability has been on the limelight since the financial crisis 2007-8. Central banks around the world have broadened their function from price stability to financial stability. Although price stability is closely linked with financial stability, latter covers broad spectrum.

Nepalese financial system is well insulated from dynamics in the world financial markets but it cannot refrain from the spillovers.

This report aims to share information and ensure transparency in the functioning of the financial system. This Report, sixth in the series of such publication, is prepared by Financial Stability Unit (FSU) and Financial Stability Working Committee (FSWC) under the guidance of the Financial Stability Oversight Committee (FSOC), which is chaired by senior Deputy Governor of this bank.

This publication has come out with the hard work of our staff and senior officials. In this context, I would like to thank the FSOC, FSWC and the Bank and Financial Institutions Regulation Department (BFIRD) of this bank, particularly the FSU for preparing this report. My special thank goes to the officials of FSU namely, Ms. Samjhana Adhikari and Assistant Director Nabin Timilsina for preparing this report in coordination with other departments and related agencies. Similarly, Executive Director Mr. Shivanath Pandey and Director Mr. Ramesh Kumar Pokharel of BFIRD deserve loads of thanks for their inspiring leadership to bring out this report in time.

I hope this report will facilitate the path of our financial stability effort and help to formulate, implement and communicate monetary and financial stability policies in the days to come. This report could also be useful for those interested in research on financial stability and macro prudential policies and in the areas of Nepalese financial economics.

Dr. Chiranjibi Nepal

Acronyms

ADBL	Agriculture Development Bank Limited
AE	Advanced Economies
ATM	Automatic Teller Machine
BAFIA	Bank and Financial Institution Act
BFIs	Bank and Financial Institutions
CAR	Capital Adequacy Ratio
CBS	Central Bureau of Statistics
CBs	Commercial Banks
CD Ratio	Credit to Deposit Ratio
CEO	Chief Executive Officer
CIT	Citizen Investment Trust
CPI	Consumer Price Index
CRR	Cash Reserve Ratio
DBSD	Development Bank Supervision Department
DOC	Department of Cooperatives
ECB	European Central Bank
FI	Financial Institution
EMDE	Emerging Market and Developing Economies
EMEs	Emerging Market Economies
EPF	Employees Provident Fund
FINGO	Financial Non-government Organization
FEMD	Foreign Exchange Management Department
FSAP	Financial Sector Assessment Program
FSI	Financial Soundness Indicators
GBBs	Grameen Bikash Banks
GDP	Gross Domestic Product
GFSR	Global Financial Stability Review
GoN	Government of Nepal
IC	Insurance Companies
IMF	International Monetary Fund
INR	Indian Rupees
IPO	Initial Public Offering
LCY	Local Currency
LS	Left Scale

LLP	Loan Loss Provision
LMFF	Liquidity Monitoring and Forecasting Framework
LoLR	Lender of Last Resort
MDDB	Microfinance Development Banks
MFFI	Microfinance Financial Institutions
NBA	Non-banking assets
NBL	Nepal Bank Limited
NEPSE	Nepal Stock Exchange
NGO	Non-government Organization
NIDC	Nepal Industrial and Development Corporation
NPA	Non-performing Assets
NPLs	Non-performing Loans
NRB	Nepal Rastra Bank
PCA	Prompt Corrective Action
RBB	Rastriya Banijya Bank
RS	Right Scale
ROA	Return on Assets
ROE	Return on Equity
RSRF	Rural Self Reliance Fund
RWA	Risk Weighted Assets
SOBs	State Owned Banks
SEBON	Security Board of Nepal
SLR	Statutory Liquidity Ratio
SOL	Single Obligor Limit
U.S	United States
WEO	World Economic Outlook
WES	World Economic Prospects

Executive Summary

1. Global growth picked up only marginally to 2.6 percent in 2014 from 2.5 percent in 2013. Some of the factors that set back activity, however, were slowly fading in the second half of the year, and growth is expected to settle at 3.0–3.3 percent for 2015-17. Partly as a result of the modest growth outlook, commodity prices are expected to remain low and trade growth weak. Growth in middle- and low-income countries slipped to 4.4 percent in 2014. The slowdown in several large middle-income economies mainly reflects cyclical factors, domestic policy tightening, and political tensions.

2. Overall, GEP states that global growth is expected to rise in 2015 to 3.0 percent, and to be sustained at 3.2-3.3 percent in 2016-17. The growth should be supported by continued recovery in the United States, a gradual acceleration of activity in the Euro Area, and receding headwinds to growth among slower growing developing regions. The sharp decline in oil prices since mid-2014 is projected to be sustained and to contribute to global growth, with significant income shifts from oil-exporting to oil-importing economies.

3. In the United States, apart from a temporary contraction at the beginning of 2014, growth has been above potential since mid-2013 and in the third quarter of 2014 reached its fastest pace since 2003. Growth is expected to reach 2.4 percent in 2014 and 3.2 percent in 2015. In the United Kingdom, growth reached 2.6 percent in 2014 and is expected to be above potential until 2016, despite slowing net exports partly as a result of weak euro area demand. Euro Area growth is forecast at 1.1 percent in 2015, and 1.6 percent in 2016–17. The current account surplus in the Euro Area remains significant, reflecting ongoing import compression, competitiveness gains in the periphery and persistent surpluses in Germany. Japanese economy grew by 0.2 percent in 2014, however, growth is expected to reach 1.2 percent in 2015 and 1.6 percent in 2016, before decelerating to 1.2 in 2017, as a second sales tax hike is implemented in April that year.

4. The baseline forecast from *GEP* assumes that the domestic headwinds that held back growth in 2014 will gradually subside. Developing countries will also benefit from the slowly strengthening recovery in high-income countries, and easing commodity prices should help commodity importers. Growth is expected to rise to 4.8 percent in 2015 and reach 5.4 percent by 2017. Growth

in South Asia strengthened in 2014. In India, export growth has been robust, and investor confidence has been bolstered by the election of a reform-minded government. Over the medium-term, growth is expected to rise steadily to 7 percent as reforms begin to yield productivity gains.

5. Inflation has started slowing in many developing countries as commodity prices declined and, in some, macroeconomic policies tightened, which also helped slow private sector credit growth and domestic demand pressures more generally. Sharp decline in oil and other commodity prices and softening growth, partly due to tighter monetary policies, is helping reduce inflation pressures in many developing countries.

6. The overall macroeconomic situation remained satisfactory in the first half of the fiscal year 2014/15. Less favorable monsoon posed some downside risks to agriculture sector but price and liquidity situation showed improvement in the review period. Also trade deficit slowed down and BoP posted a moderate surplus. There are serious concerns about the second half of the FY 2014.15, after the devastating earthquake of 25 April, 2015. It has adversely affected almost all sectors of the economy. Consequently, the real GDP at basic price is expected to grow by 3.0 percent in 2014/15 compared to the growth of 5.1 percent in 2013/14.

7. It is estimated that the total value of disaster effects (damages and losses) caused by the earthquakes is NPR 706 billion or its equivalent of US$ 7 billion. Of that amount, NPR 517 billion (or 76 percent of the total effects) represents the value of destroyed physical assets, and Rs. 189 billion (24 percent of the total effects) reflects the losses and higher costs of production of goods and services arising from the disaster. The effects of the disasters illustrate that the estimated value of total damages and losses (changes in flows) is equivalent to about one third of the Gross Domestic Product (GDP) in FY 2013-2014. According to the World Bank's simulations, the earthquakes will end up pushing an additional 2.5 to 3.5 percent Nepalese people into poverty in FY 2015-2016 which translates into at least 700,000 additional poor.

8. The y-o-y inflation as measured by the consumer price index stood at 6.8 percent in mid-January 2015 compared to 9.7 percent a year earlier. The indices of food and beverages group and non-food and services group increased by 9.0 percent and 5.1 percent, respectively during the review

period. Such indices had increased by 12.9 percent and 6.9 percent respectively in the corresponding period of the previous year. In the first half of 2014/15, the fiscal position of the government showed mixed outcomes. Total government expenditure, on cash basis, increased by 14.4 percent to Rs 153.71 billion in the review period, while government revenue mobilization increased by 16.6 percent to Rs. 190.52 billion during the first six months of 2014/15.

9. Merchandise exports decreased by 3.9 percent to Rs. 43.39 billion during the first six months of 2014/15 while merchandise imports increased by 13.3 percent to Rs. 378.22 billion in the review period. Given the high growth of imports relative to exports, the ratio of export to import declined to 11.5 percent during the first six months of 2014/15. The overall BOP recorded a surplus of Rs. 34.26 billion during the first six months of 2014/15. During the first six months of 2014/15, total foreign exchange reserve increased by 5.9 percent to Rs. 704.44 billion.

10. Broad money supply (M2) increased by 5.8 percent in the six months of 2014/15 whereas narrow money supply (M1) rose by 1.6 percent in the review period. Similarly, domestic credit increased by 5.6 percent in the review period.

11. According to GFSR 2015 April, financial stability risks have increased since the *October 2014.* Central banks have responded to increased downside risks to price stability. Since October, the Bank of Japan (BOJ) and the European Central Bank (ECB) have announced bold new monetary measures designed to ward off deflation pressure and move their economies closer to their inflation objectives. Emerging market financial stability risks have increased. The easing of inflation pressure is benefiting many emerging market economies, giving them monetary policy space to combat slowing growth. Credit risks are broadly unchanged. Apart from these recent development, continuous plunge in crude oil prices also have a significant impact on overall financial stability.

12. Banking system dominates Nepalese financial system in terms of assets and intensity both. As of mid-Jan 2015 there are altogether 270 financial institutions in the country (excluding government licensed cooperatives). BFIs have added 169 branches during first six months of FY 2014/15,

resulting growth of 4.89 percent. Total assets of BFIs have increased by 6.82 percent to Rs. 1973 billion during first six of the fiscal year.

13. Credit flows form NRB regulated A, B and C class financial Institutions account about 66 percent of the GDP of the country. Bank credits have been growing over the years to reach Rs.1248 billion in mid-January 2015. Wholesale and retail sector topped the chart for highest credit flow among identified sectors, while agriculture, forestry and beverage production came second. Registering a growth of 6.16 percent during the first six months of the FY 2014/15, deposits stood at Rs.1569 billion. Data from mid-January 2015 show that assets and deposits have grown at similar paces (6.82 percent and 6.18 percent) while credit grew by almost twice (11.51 percent) than deposits.

14. Overall capital adequacy of BFIs stood at 11.98 percent which shows majority of BFIs are enough to maintain regulatory requirement. Banking sector witnessed an increase in NPA during the six months period to mid-January 2015; however, it remained below five percent. The provisions for possible loan losses at BFIs are adequate to cover up losses from NPL. The credit to deposit (C/D) ratio of the BFIs during the six month period to mid-January 2015 was 79.5 percent. Excess liquidity problem seemed to be easing during the review period with BFIs liquidity coming down to 28.2 percent, from 32.7 percent in mid-July 2014. Most of BFIs are able to make impressive returns in FY 2014/15. Annualized ROE and ROA figures of BFIs calculated as 18.94 percent and ROA at 1.8 percent respectively. As of mid-January 2015, total real estate exposure of BFIs stand at Rs. 82.8 billion, a slight increase from Rs.82.45 billion in mid-July 2014.

15. Commercial banks have predominantly high share is total financial system as well and NRB regulated BFIs. As in mid-Jan 2015, share of total assets and liabilities of commercial banks on NRB regulated BFIs was 81.0 percent. Total deposit and credit of commercial banks stood at 81.4 percent of the total deposits and credits of NRB regulated BFIs and 65.4 percent of GDP in mid-Jan 2015. Capital fund of commercial banks rose by 13.9 percent to Rs. 123.9 billion in mid-Jan 2015. NPL to total loan ratio of commercial banks decreased to 2.7 percent in mid-Jan 2015 in comparison to the ratio of 2.9 percent in mid-July 2014. Commercial banks are still struggling to fulfill regulatory requirements in productive sector lending. Net Profit of the

commercial banks stood at Rs.15.4 billion as of mid-Jan 2015. Out of total 30 commercial banks, only one incurred net loss in the review period. Average base rate of commercial banks was 7.5 percent, recording a reduction of 78 basis points over the rate calculated on mid-July 2014. Average interest spread of commercial bank fell to 4.6 percent from 4.7 in mid-July 2015.

16. Total assets of development banks rose by Rs. 2.35 billion during the review period to reach Rs. 261.3 billion in mid-January 2015. Deposits in development banks grew by Rs.2.75 billion or 1.4 percent while credits grew by 4.2 percent to Rs.168.7 billion. The ratio of NPL to total gross loan was at 4.1 percent whereas loan loss provisioning of development banks stood at Rs. 6.9 billion. The average base rate of 20 national level development banks stood 9.9 percent in mid-January 2015 and average interest spread of development banks was 8.1 percent in mid-January 2015.

17. Balance-sheets of finance companies expanded by 1.93 percent to reach Rs.112.5 billion on mid-January 2015. Similarly, deposit collections of finance companies grew by 2.0 percent to reach Rs.74.9 billion while, credit flows from the finance companies decreased by Rs.149 million to Rs.65.7. Non-performing loan of finance companies moved further by 60 basis points from its level of 14.3 percent on mid July 2014. Annualized ROA and ROE of finance companies during first six months of current FY 2014/15 were 1.10 percent and 10.56 percent respectively.

18. As of mid-January 2015, total members of MFFIs were 13,89,625, recording a fall of 6.5 percent during the review period. The total loan disbursed by the MFFIs as of mid-January 2015 accounted to Rs.230.2 billion. Out of the total loan, wholesale MFFIs disbursed Rs. 37.9 billion and NGBBL disbursed Rs. 44.5 billion during the review period. Capital of MFFIs increased by 16.4 percent from the level in mid-July 2014 to reach Rs. 5.5 billion. Total asset of MFFIs in the review period rose by 37.9 percent to Rs. 58.4 billion. Total saving of deposit mobilization of MFFIs grew by 43.5 percent to Rs. 13.1 billion.

19. A total of 31,705 cooperatives are operating throughout the country till mid-January 2015. They account for around 10 percent of total deposit of NRB regulated financial institutions, while they share same percentage of total loans and advances. As of mid-January 2015, deposits of cooperatives totaled to Rs.176.1 billion whereas total credit flow stood at Rs.160.3 billion.

20. Total assets/liabilities of insurance companies rose by 8.92 percent to Rs.110.10 billion during six months to mid-January 2015. Provident fund of EPF stood at Rs. 179.4billion as of mid-March 2015, while total assets/liabilities stood at Rs. 186.3 billion. The savings in EPF equals around 9 percent of total deposits of NRB regulated BFIs while total assets of EPF weights equal to 7 percent of total assets held by NRB regulated BFIs. Similarly, fund collections at Citizen Investment Trust (CIT) stood at Rs.58.44 billion, recording a growth of 12.81 percent over the six month period from mid-July 2014.
21. Three-month Treasury bill secondary market rate on discount basis remained highly volatile within the band of 0.01 percent to 0.05 percent range during the review period. Exchange rate has remained volatile since the recovery in US economy while US dollar remaining strong against most of the major currencies. The US dollar index appreciated from 79.8 in beginning of July 2014 to 94.8 at end of January 2015.
22. The weighted average 91-day Treasury bill rate decreased to 0.15 percent in mid January 2015 from 0.47 percent a year ago. Similarly, average inter-bank transaction rate among commercial banks remained at 0.15 percent in mid January 2015 down from 0.21 percent a year ago. Nepalese currency depreciated by 3.3 percent against US dollar during the first six months of 2014/15. During the first six-months of the fiscal year 2014-15, SEBON approved public offerings for nine companies amounting Rs. 6.3 billion. The secondary market index NEPSE rose by 19.4 percent to 939.5 points in mid-January 2015 on y-o-y basis.
23. Nepal Rastra bank issued a circular to promote credit in agriculture sector. The circular comprehends government strategy to promote agriculture as a business among youth. Similarly, it also issued working procedure for agricultural credits which was prepared of Ministry of Finance. According to the working procedure, an individual can avail the facility on loans up to Rs 10 million. The working procedure, which came into effect immediately, has identified 12 priority areas eligible for the facility. In a bid to increase resilience in licensed financial institutions, NRB has added a layer to its prevailing credit classifications issuing a directive on maintaining “watch list” of loans.
24. NRB issued a circular regarding financial consumer protection guidelines to licensed institutions to make people aware about financial services and

increase transparency in availing fees and charges from customers for services of financial institutions. The circular aims to improve financial literacy and bolster consumer confidence in the financial institutions of the country.

25. NRB took bold steps to provide banking services after the major earthquake that rattled the country on April 23 2015 by instructing all licensed institutions to keep providing services considering safety of theirs staff and assets. Similarly, it announced zero cost refinancing loan facilities through licensed BFIs to the individuals whose houses were demolished by the earthquake. NRB also eased current policy by allowing restructuring of home loans extended to affected people.

Chapter - One

MACROECONOMIC DEVELOPMENT

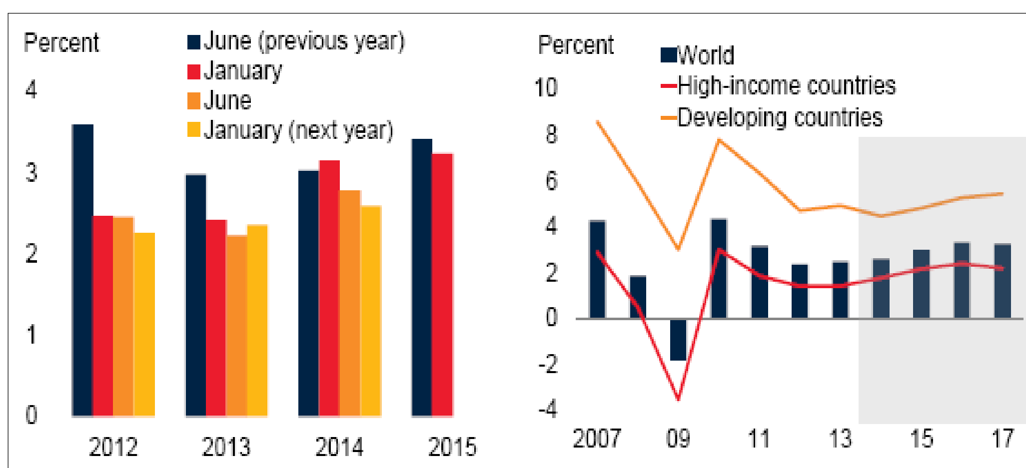
Global Economic Development

1.1 Global Economic Prospects (*GEP)* January, 2015 issue states that world economy is still struggling to gain momentum as many high-income countries continue to grapple with the legacies of the global financial crisis.

1.2 The flagship report from World Bank underlines that the recovery has been weaker than anticipated in June 2014, partly for one-off reasons, with a string of disappointing growth outturns in the Euro Area, Japan, parts of emerging Europe (especially Russia) and Latin America. The Euro Area and Japan accounted for more than half of the downward revisions to global growth in 2014

1.3 Global growth picked up only marginally to 2.6 percent in 2014 from 2.5 percent in 2013. Some of the factors that set back activity, however, were slowly fading in the second half of the year, and growth is expected to settle at 3.0–3.3 percent for 2015-17. Partly as a result of the modest growth outlook, commodity prices are expected to remain low and trade growth weak.

Figure 1.1: Global Growth Forecasts (Right) and actual and projected growth (Left)



Source: World Economic Prospects January 2015

1.4 Growth in middle- and low-income countries slipped to 4.4 percent in 2014. The slowdown in several large middle-income economies mainly reflects cyclical factors, domestic policy tightening, and political tensions.

1.5 GEP presumes that three global influences that are expected to affect developing economies significantly. First, an eventual increase in the monetary policy rate in the United States is expected to result in gradually tightening global financial conditions from 2015 onward. Diverging cyclical positions and, as a result, prospects for asynchronous monetary policies in the major economies, have already been accompanied by U.S. dollar appreciation and pressure on some developing-country currencies. Second, commodity prices are expected to remain soft on concerns about weak global growth and rising supply as well as a shift in market expectations about Organization of the Petroleum Exporting Countries (OPEC) policy objectives.

1.6 Third, developing countries' exports will be differentially impacted by the recovery in high-income economies. While faster growth in the United States is expected to propel some developing countries, others could be held back by the anemic recovery in the Euro Area and Japan.

1.7 Overall, GEP states that global growth is expected to rise in 2015 to 3.0 percent, and to be sustained at 3.2-3.3 percent in 2016-17. The growth should be supported by continued recovery in the United States, a gradual acceleration of activity in the Euro Area, and receding headwinds to growth among slower growing developing regions. The sharp decline in oil prices since mid-2014 is projected to be sustained and to contribute to global growth, with significant income shifts from oil-exporting to oil-importing economies.

1.8 The report has highlighted three major policy challenges faced by developing countries. First, monetary and exchange rate policies might have to adapt to the more normal (i.e., less easy) financial conditions that will eventually accompany the recovery in high-income countries. Second, some developing countries that face benign cyclical environments should rebuild fiscal space, which would allow them to use countercyclical fiscal policy when needed. Third, developing countries need to implement structural reforms that promote job creation, growth, and trade. Such policies would mitigate the long-run adverse effects from less favorable demographics in many developing countries and weak global trade. Moreover, they will be

instrumental in achieving higher growth rates that are necessary to achieve poverty targets.

Table 1.1: Global Growth Projections (percentage change from previous year)

	2012	2013	2014e	2015f	2016f	2017f
REAL GDP [1]						
World	**2.4**	**2.5**	**2.6**	**3.0**	**3.3**	**3.2**
High income	**1.4**	**1.4**	**1.8**	**2.2**	**2.4**	**2.2**
United States	2.3	2.2	2.4	3.2	3.0	2.4
Euro Area	-0.7	-0.4	0.8	1.1	1.6	1.6
Japan	1.5	1.5	0.2	1.2	1.6	1.2
United Kingdom	0.7	1.7	2.6	2.9	2.6	2.2
Russia	3.4	1.3	0.7	-2.9	0.1	1.1
Developing countries	**4.8**	**4.9**	**4.4**	**4.8**	**5.3**	**5.4**
East Asia and Pacific	7.4	7.2	6.9	6.7	6.7	6.7
China	7.7	7.7	7.4	7.1	7.0	6.9
Indonesia	6.3	5.8	5.1	5.2	5.5	5.5
Thailand	6.5	2.9	0.5	3.5	4.0	4.5
Europe and Central Asia	1.9	3.7	2.4	3.0	3.6	4.0
Kazakhstan	5.0	6.0	4.1	1.8	3.2	4.7
Turkey	2.1	4.1	3.1	3.5	3.7	3.9
Romania	0.6	3.5	2.6	2.9	3.2	3.9
Latin America and the Caribbean	2.6	2.5	0.8	1.7	2.9	3.3
Brazil	1.0	2.5	0.1	1.0	2.5	2.7
Mexico	4.0	1.1	2.1	3.3	3.8	3.8
Argentina	0.9	2.9	-1.5	-0.3	1.6	3.1
Middle East and North Africa	1.4	0.5	1.2	2.5	3.0	3.5
Egypt[2]	2.2	2.1	2.2	3.5	3.8	4.0
Iran	-6.6	-1.9	1.5	0.9	1.0	2.2
Algeria	3.3	2.8	3.0	3.3	3.5	3.5
South Asia	5.0	4.9	5.5	6.1	6.6	6.8
India[2,3]	4.7	5.0	5.6	6.4	7.0	7.0
Pakistan[2,3]	3.5	4.4	5.4	4.6	4.8	4.9
Bangladesh[2]	6.5	6.0	6.1	6.2	6.5	7.0
Sub-Saharan Africa	4.0	4.2	4.5	4.6	4.9	5.1
South Africa	2.5	1.9	1.4	2.2	2.5	2.7
Nigeria	4.3	5.4	6.3	5.5	5.8	6.2
Angola	8.4	6.8	4.4	5.3	5.0	5.2

Source: Global Economic Prospectus, World Bank, January 2015.

Notes: PPP = purchasing power parity; e = estimate; f = forecast.

1. Aggregate growth rates calculated using constant 2010 U.S. dollars GDP weights.

2. In keeping with national practice, data for Bangladesh, Egypt, India, and Pakistan are reported on a fiscal year basis in table 1.1. Aggregates that depend on these countries are calculated using data compiled on a calendar year basis.

3. Real GDP at factor cost, consistent with reporting practice in Pakistan and India.

Recent Developments and Outlook

Major Economies

1.9 In the United States, apart from a temporary contraction at the beginning of 2014, growth has been above potential since mid-2013 and in the third quarter of 2014 reached its fastest pace since 2003. Growth is expected to reach 2.4 percent in 2014 and 3.2 percent in 2015 percent before gradually decelerating to 2.4 percent in 2017. The recovery has been supported by highly accommodative monetary policy, which bolstered capital market valuations, and easing fiscal consolidation.

1.10 In the United Kingdom, the recovery has gained momentum, supported by robust housing markets and expanding credit. Growth reached 2.6 percent in 2014 and is expected to be above potential until 2016, despite slowing net exports partly as a result of weak euro area demand.

1.11 In the Euro Area, activity has been weaker than anticipated, especially in France, Germany, and Italy. Financial market indicators suggest that investors expect a prolonged period of below-target inflation. Euro Area growth is forecasted to be at 1.1 percent in 2015, and 1.6 percent in 2016–17. Concerns about long-term prospects and the legacies of the crisis (especially impaired balance sheets and high unemployment) weigh on a fragile recovery and diminish expected growth benefits from sustained low oil prices. In Greece, political uncertainty continues to fray investor sentiment. In contrast, in Ireland and Spain, a pickup appears underway, helped by gains in cost competitiveness and strengthening corporate balance sheets. The current account surplus in the Euro Area remains significant, reflecting ongoing import compression, competitiveness gains in the periphery and persistent surpluses in Germany.

1.12 Japanese economy grew by 0.2 percent in 2014, significantly lower than expectations as the economy struggled to recover from a sales tax increase in April 2014, and, until mid-2014, exports remained subdued despite a weak yen. This export weakness reflected soft global demand, the relocation of production facilities overseas and rising cost of energy imports since the shutdown of nuclear reactors. Looking forward, however, soft oil prices should help contain the cost of energy imports and support the recovery. However, growth is expected to reach 1.2 percent in 2015 and 1.6 percent in

2016, before decelerating to 1.2 in 2017 as a second sales tax hike is implemented in April that year.

1.13 In China, growth is expected to slow below 7 percent by 2017 from 7.4 percent in 2014, broadly in line with the objectives of the current five-year plan. For 2015, soft oil prices are expected to boost activity and reduce the need for additional policy stimulus. Reflecting excess capacity, weakening domestic demand, and reduced import costs, inflation is expected to remain below the central bank's indicative ceiling of 3 percent. China has adopted measures aimed at containing financial vulnerabilities and unwinding excess capacity (including in construction, shipping, and renewable energy sectors) and, at the same time, stemming a slowdown. Actions to rein in credit growth have slowed the real estate market and investment while dampening growth, especially in early 2014. As the authorities have balanced the competing goals of reducing vulnerabilities with supporting growth, the medium-term growth outlook has been revised downwards.

Developing Economies

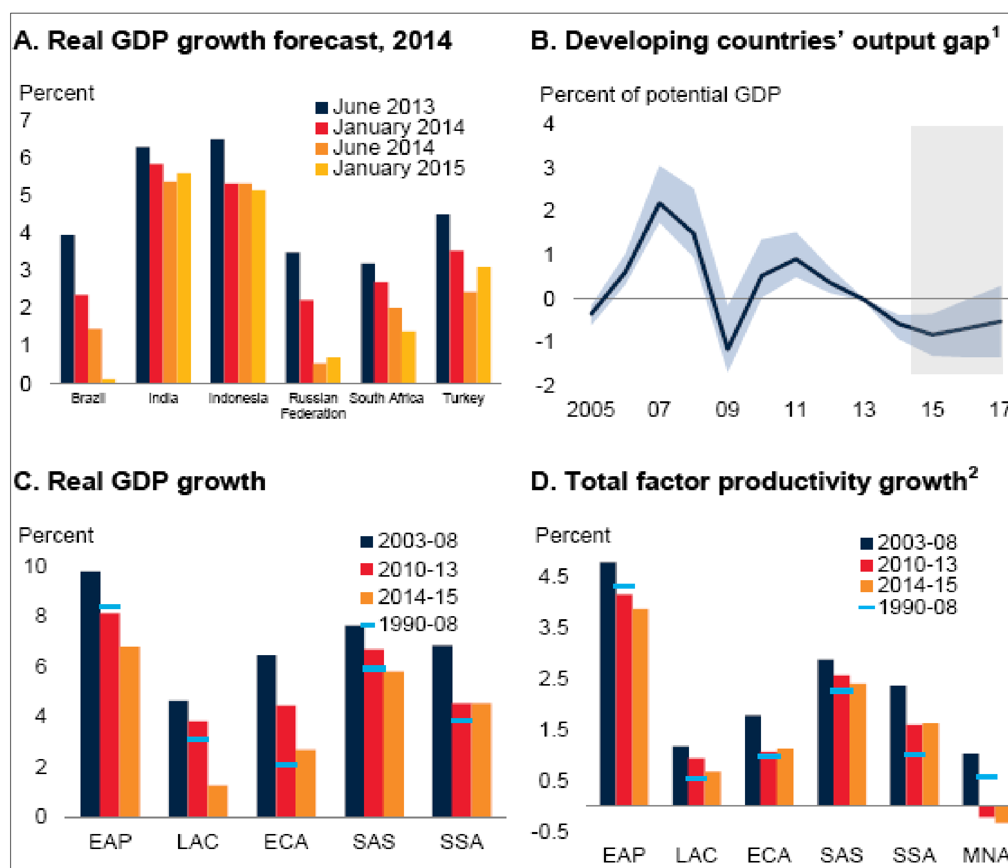
1.14 The baseline forecast from *GEP* assumes that the domestic headwinds that held back growth in 2014 will gradually subside. Developing countries will also benefit from the slowly strengthening recovery in high-income countries, and easing commodity prices should help commodity importers. Growth is expected to rise to 4.8 percent in 2015 and reach 5.4 percent by 2017.

1.15 *East Asia and Pacific, excluding China:* As a result of political tensions; tightening monetary, fiscal, and macro-prudential policies in 2013 and early 2014; and soft commodity prices, activity, credit growth and inflation slowed (in most countries).

1.16 This has allowed several central banks to keep policy rates on hold for the time being but monetary policy room remains constrained by high domestic debt. Recent volatility in global financial markets put some pressure on asset prices and currencies in commodity-exporting economies. Although the region has so far been resilient to the growth slowdown in China from post-crisis peaks (with the exception of some commodity exporters, such as Indonesia), a sustained slowdown in China may feed through via integrated supply chains. Nevertheless, growth is expected to gain momentum as the investment cycle turns (Indonesia), political unrest subsides (Thailand), and countries integrated into global value chains (Cambodia, Malaysia, Thailand,

and Vietnam) benefit from the pickup in the United States and other major markets for manufactures. Adjustment to softer commodity prices will continue to weigh on growth of the commodity exporters of the region but should help commodity-importing countries.

Figure 1.2: Growth in Developing Countries



Source: WEP January 2015

1. Output gap estimates using production function approach, Hodrick-Prescott filter, and band-pass filter. The shade indicates the range of output gap estimates.

2. Total factor productivity growth estimates are based on a production function approach.

1.17 *Europe and Central Asia:* Weak activity in the Euro Area; a severe slowdown in Russia combined with a sharp depreciation of the ruble against the U.S. dollar between January and mid-December 2014; and a sharp contraction in Ukraine present difficult headwinds to the region. Some Central Asian countries already experienced double-digit declines in exports to Russia and sharp drops in the value of remittances. Additional monetary

policy accommodation and a gradual, though weak, recovery in the Euro Area would support strengthening growth in Central and Eastern Europe. In contrast, despite a gradual tilt toward increased ties to China, contraction in Russia, low commodity prices and an unfinished domestic reform agenda will hold back activity in CIS countries. In Turkey, despite robust exports and government spending, growth slowed somewhat in 2014 as election-related uncertainties and geopolitical tensions dampened confidence and policy tightening slowed credit growth. In 2015–16, growth is expected to gradually accelerate on the back of strengthening consumption growth, and lower oil prices will reduce current account deficits.

1.18 *Latin America and the Caribbean:* Growth decelerated sharply in 2014, as a consequence of domestic difficulties and declining commodity prices. A number of the larger economies are currently grappling with low growth, high or rising inflation, and weak investor confidence. Over the next two years, negative terms of trade effects should taper off in commodity-exporting countries and domestic constraints should ease to some extent. But growth is expected to remain modest by pre -crisis standards. Productivity-enhancing reforms, and the extensive trade exposure to the United States, should support growth in Mexico. Prospects of a rapid rebound in Brazil, however, are constrained by an unfinished reform agenda and weak confidence. Since Brazil is a significant importer from the rest of the region, this may weigh on growth in neighboring countries. Macroeconomic imbalances and soft prices of key commodities dampen growth prospects in Argentina (compounded by the unresolved dispute with some bondholders) and República Bolivariana de Venezuela. Should República Bolivariana de Venezuela's preferential energy export arrangements with countries in the Caribbean, Central America and South America be altered, external financing needs could rise sharply in recipient countries and funding for some related social programs could be affected.

1.19 *Middle East and North Africa:* The recovery is strengthening, in particular in oil-importing countries, but it remains fragile and uneven. Substantial official assistance from Gulf Co-operation Council countries has helped firm consumption, investor confidence, and raise investment in Egypt and Jordan. Some oil-exporting countries, however, will face weak growth, and deteriorating fiscal and external balances as a result of low oil prices or continue to struggle with security concerns (Iraq, Libya, and the Republic of

Yemen) that have prevented them from restoring full production. Although activity in the region should pick up and softening commodity prices should help dampen inflation, unemployment remains high—partly as a result of recessions after the Arab Spring uprisings—and government service delivery as well as the business environment has been chronically weak. Energy subsidies, which are often a poorly targeted way of assisting those in need, burden budgets. Domestic security concerns as well as spillovers from conflicts in Iraq and Syria (including refugee flows and militant incursions) add to the challenges.

1.20 *South Asia:* Growth in South Asia strengthened in 2014. In India, export growth has been robust, and investor confidence has been bolstered by the election of a reform-minded government. The current account deficit and elevated inflation—both persistent vulnerabilities—have declined considerably. Over the medium-term, growth is expected to rise steadily to 7 percent as reforms begin to yield productivity gains. This is expected to benefit other countries in the region which receive remittances from India. In Pakistan, political tensions in the second half of 2014 and a difficult security situation are projected to continue to weigh on activity. In contrast, in Bangladesh, continued reform efforts and robust remittances have helped and should continue to promote domestic demand and activity more generally.

1.21 *Sub-Saharan Africa:* The region expanded moderately in 2014 but the pace of expansion was slower in many of the larger economies (Angola, Ghana, Kenya, and South Africa) as a result of subdued global demand, soft commodity prices, weak foreign direct investment flows, low business confidence, and capacity shortages, especially infrastructure constraints. The Ebola epidemic has severely disrupted activity in Guinea, Liberia, and Sierra Leone. Economic losses in these countries, however, should begin diminish as effective containment strategies are put in place. Regional spillovers from Ebola should then remain modest. The sharp oil price decline will benefit oil importing countries but adversely affect several countries in Sub-Saharan Africa that are oil exporters.

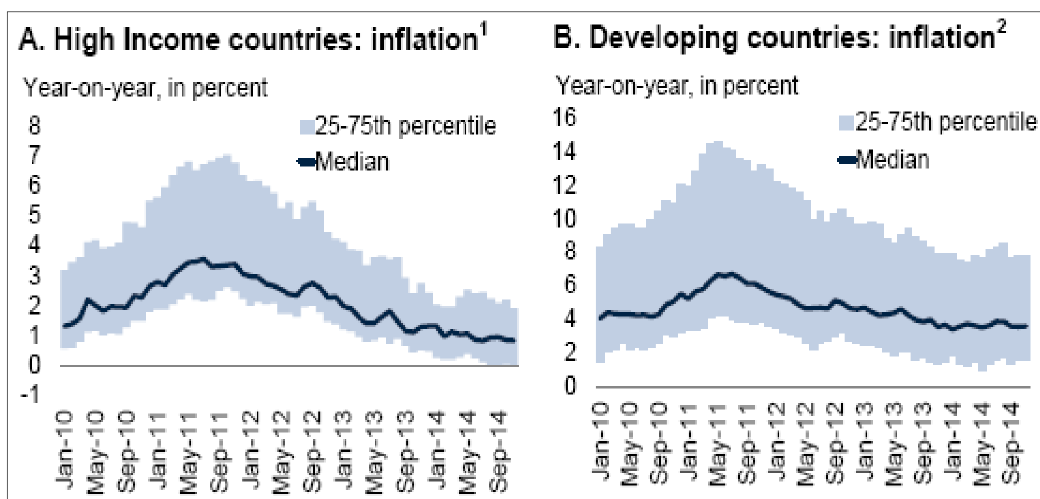
Inflation

1.22 Inflation has started slowing in many developing countries as commodity prices declined and, in some, macroeconomic policies tightened, which also helped slow private sector credit growth and domestic demand pressures

more generally. Falling commodity prices, particularly oil prices, amplified this disinflation pressure, and the inflation rate in many advanced economies fell below inflation target.

1.23 Sharp decline in oil and other commodity prices and softening growth, partly due to tighter monetary policies, is helping reduce inflation pressures in many developing countries (Figure 1.3). More emerging market economies than advanced economies have headline inflation above their inflation goals, although many major Asian economies are at their lowest inflation cycles.

Figure 1.3: Inflation in high income and developing countries



Source: WEP January 2015

1. The sample includes 55 high-income countries. Latest data is November 2014.

2. The sample includes 121 developing countries. Latest data is November 2014.

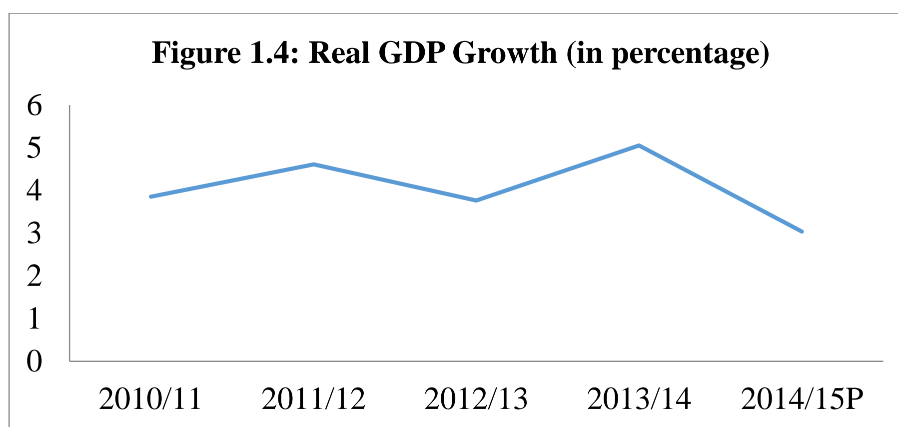
Domestic Macroeconomic Development

1.24 The overall macroeconomic situation remained satisfactory in the first half of the fiscal year 2014/15. Less favorable monsoon posed some downside risks to agriculture sector but price and liquidity situation showed improvement in the review period. Also trade deficit slowed down and BoP posted a moderate surplus. Timely announcement of government budget, improvement in business climate and increase in productive sector lending in the review period are likely to strengthen financial sector stability. However, a devastating earthquake of April 25, 2015, and its aftershocks have significantly altered the growth outlook and posed new challenges to the economy.

Economic Growth

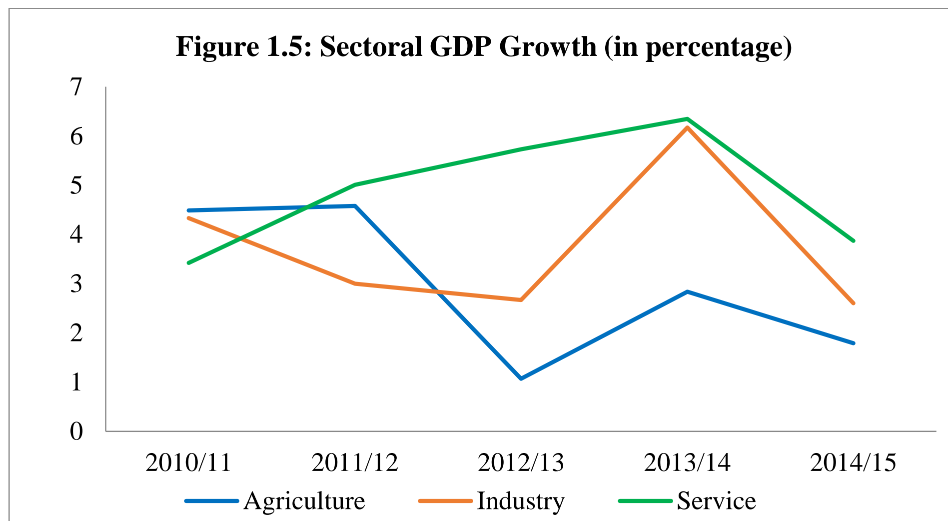
1.25 The devastating earthquake of 25 April, 2015 has adversely affected almost all sectors of the economy. Consequently, the real GDP at basic price is expected to grow by 3.0 percent in 2014/15 compared to the growth of 5.1 percent in 2013/14[1]. The initial growth target anticipated in the government budget was 5.5 percent. The loss of properties caused by this catastrophe is discussed in Box 1.1.

Figure 1.4: Real GDP Growth (in percentage)



1.26 Agriculture sector, which was adversely affected by the late monsoon, has been further affected by the earthquake. The agriculture sector is now estimated to grow by mere 1.9 percent in 2014/15 compared to a growth of 2.9 percent last year. Considering the adverse effects of power-shortage, earthquake and political uncertainties, growth in industrial sector is estimated to decelerate to 2.6 percent in this fiscal year. The real estate and tourism sector have been hit hard by the earthquake. Medium size enterprises, wholesale and retail trade; transport, storage and communication; and financial intermediatio0 have been adversely affected by the event. Services sector, therefore, is estimated to grow by 3.9 percent in 2014/15 compared to the growth of 6.3 percent in the previous year.

[1] As per preliminary estimates of Central Bureau of Statistics (CBS).



BOX 1.2 April Earthquake damages and losses calculated at Rs.706 billion

On Saturday, 25 April 2015 at 11:56 local time, a 7.6 magnitude earthquake as recorded by Nepal's National Seismological Centre (NSC), struck Barpak in the historic district of Gorkha, about 76 km northwest of Kathmandu. Nepal had not faced a natural shock of comparable magnitude for over 80 years.

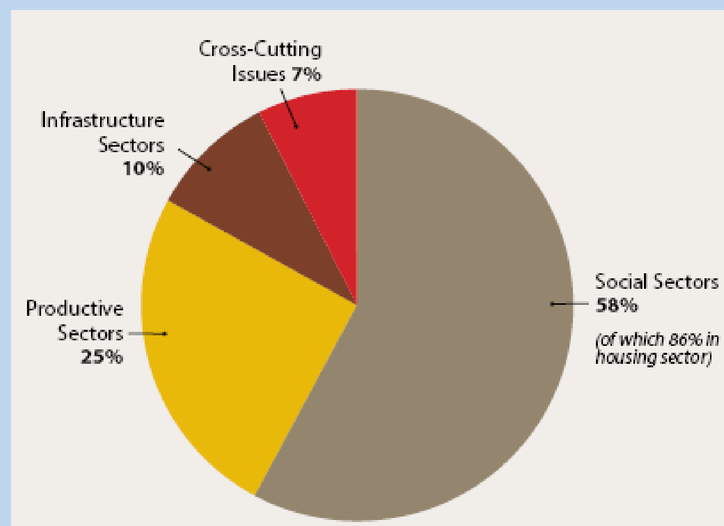
It is estimated that the total value of disaster effects (damages and losses) caused by the earthquakes is NPR 706 billion or its equivalent of US$ 7 billion. Of that amount, NPR 517 billion (or 76 percent of the total effects) represents the value of destroyed physical assets, and NPR 189 billion (24 percent of the total effects) reflects the losses and higher costs of production of goods and services arising from the disaster (see Table 1.1). These estimates are based on the aggregation of information and data collected across sectors of social and economic activity and checked to avoid duplication of numbers.

Loss of a third of GDP

The effects of the disasters illustrate that the estimated value of total damages and losses (changes in flows) is equivalent to about one third of the Gross Domestic Product (GDP) in FY 2013-2014. In addition, the estimated value of damage is equivalent to more than 100 percent of the Gross Fixed Capital Formation (GFCF) for FY 2013-2014. To put it differently, if all other capital

formation activities were stopped, it would take Nepal more than one year to rebuild the fixed capital that was destroyed by the earthquakes.

Figure 1.6: Share of Disaster effects across sectors



Furthermore, the estimated production losses represents about 10 percent of the added value of all goods and services produced in one year in the country, which will result in a slowdown of the economy in the short term, despite the fact that the estimated losses for some sectors like cultural heritage and environment, among others, would unfold over several years. Disaster effects are spread unevenly between public and private sectors. The private sector has sustained about 3.3 times the value of damages and losses in comparison with the public sector (see Figure 4), which provides a first indication of the relative efforts that each sector must invest during recovery and reconstructions. While the government plans to utilize most of its resources to assist the poorer strata and rural population to revive the social and productive sectors, it is critical to ensure availability of finance through banking and non-banking institutions including cooperatives for the recovery of the private sector.

More People slipped into Poverty

Preliminary assessment of incidence and impact suggests that the earthquakes have disproportionately affected the poorer, rural locations relative to the urban and less poor areas.

Table 1.2: Summary of Disaster Effects

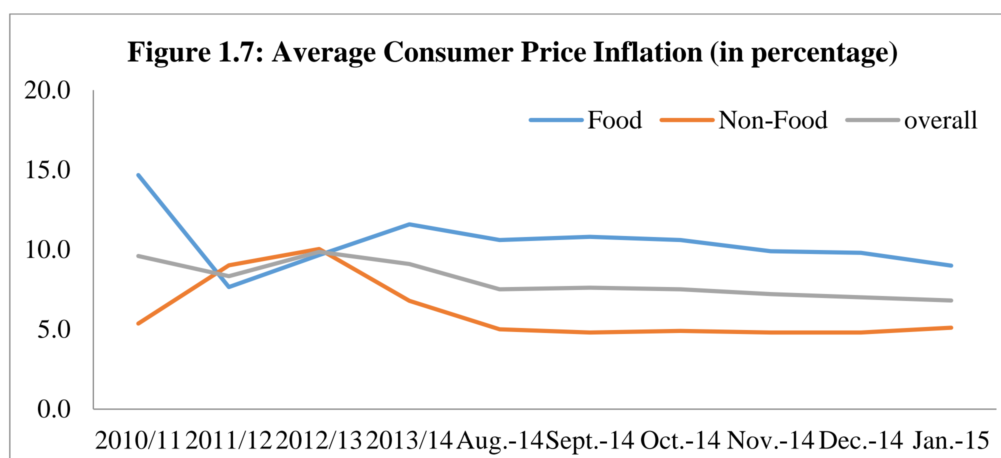
	Disaster Effects (NPR million)			Distribution of Disaster Effects (NPR million)		Losses in personal income (NPR million)
	Damages	Losses	Total	Private	Public	
Social Sectors	**355,028**	**53,597**	**408,625**	**363,248**	**45,377**	**-**
Housing and Human Settlements	303,632	46,908	350,540	350,540	-	-
Health	6,422	1,122	7,544	1,394	6,150	-
Education	28,064	3,254	31,318	2,365	28,953	-
Cultural Heritage	16,910	2,313	19,223	8,948	10,274	-
Productive Sectors	**58,074**	**120,046**	**178,121**	**158,079**	**20,043**	**17,124**
Agriculture	16,405	11,962	28,366	25,813	2,553	4,603
Irrigation	383	-	383	-	383	
Commerce	9,015	7,938	16,953	16,953	-	2,667
Industry	8,394	10,877	19,271	19,271	-	3,654
Tourism	18,863	62,379	81,242	75,105	6,137	6,200
Finance	5,015	26,890	31,905	20,937	10,969	-
Infrastructure Sectors	**52,460**	**14,323**	**66,783**	**17,281**	**49,502**	
Electricity	17,807	3,435	21,242	15,569	5,673	-
Communications	3,610	5,085	8,695	1,712	6,983	
Community Infrastructure	3,349	-	3,349	-	3,349	-
Transport	17,188	4,930	22,118	-	22,118	
Water and Sanitation	10,506	873	11,379	-	11,379	-
Cross-Cutting Issues	**51,872**	**1,061**	**52,933**	**1,755**	**51,178**	**-**
Governance	18,757	-	18,757	-	18,757	-
Disaster Risk Reduction	155	-	155	-	155	-
Environment and Forestry	32,960	1,061	34,021	1,755	32,267	-
Total	**517,434**	**189,027**	**706,461**	**540,362**	**166,100**	**17,124**
Total (US$ million)	**$5,174**	**$1,890**	**$7,065**	**$5,404**	**$1,661**	**$171**

Even within the relatively prosperous areas that have been affected, for example the Kathmandu Valley, households that were already either poor or vulnerable have been particularly exposed. According to the World Bank's simulations, the earthquakes will end up pushing an additional 2.5 to 3.5 percent Nepalese people into poverty in FY 2015-2016 which translates into at least 700,000 additional poor. Roughly 50 to 70 percent of the increase in poverty will come from rural central hills and mountains where overall vulnerability prior to the earthquake was already high. Additionally, the deterioration of water and sanitation services, disruption of schools and health services, and the possible increase in food insecurity may lead to a bigger impact on multidimensional poverty.

Source: Post Disaster Needs Assessment Report 2015, National Planning Commission

Inflation

1.27 Fall of oil price in the international market; slow down of inflation in India and the efforts undertaken by NRB to maintain monetary aggregates within desired limit, among others can be attributed for keeping inflation at moderate level in the review period. The y-o-y inflation as measured by the consumer price index stood at 6.8 percent in mid-January 2015 compared to 9.7 percent a year earlier. The indices of food and beverages group and non-food and services group increased by 9.0 percent and 5.1 percent, respectively during the review period. Such indices had increased by 12.9 percent and 6.9 percent respectively in the corresponding period of the previous year.



1.28 Lower growth rate of food and beverage price index can be attributed to deceleration in the price of cereal grains and their products; vegetables; meat and fish; ghee and oil; and fruits while slow down in prices of housing and utilities, health, transport, and education helped reduce the non-food and services index.

1.29 Despite the structural bottlenecks resulting from the April earthquake devastation, it is expected that inflation will be contained within single digit in the current fiscal year.

Government Finance

1.30 The structure of the government expenditure and the size of budget deficit have important implications to the financial stability. While increase in the share of capital expenditure in the review period can be considered as a sign

of an improving fiscal policy, the decline in the growth of revenue mobilization, and importantly, huge unspent cash balance of the government at the NRB in the review period is a matter of concern.

1.31 Total government expenditure, on cash basis, increased by 14.4 percent to Rs 153.71 billion in the review period compared to a growth of 25.4 percent in the corresponding period of the previous year. In the total expenditure, the share of recurrent, capital and financial expenditures stood at 75.5 percent, 9.0 percent and 15.5 percent, respectively in the review period compared to 82.4 percent, 6.9 percent and 10.7 percent, respectively in previous year.

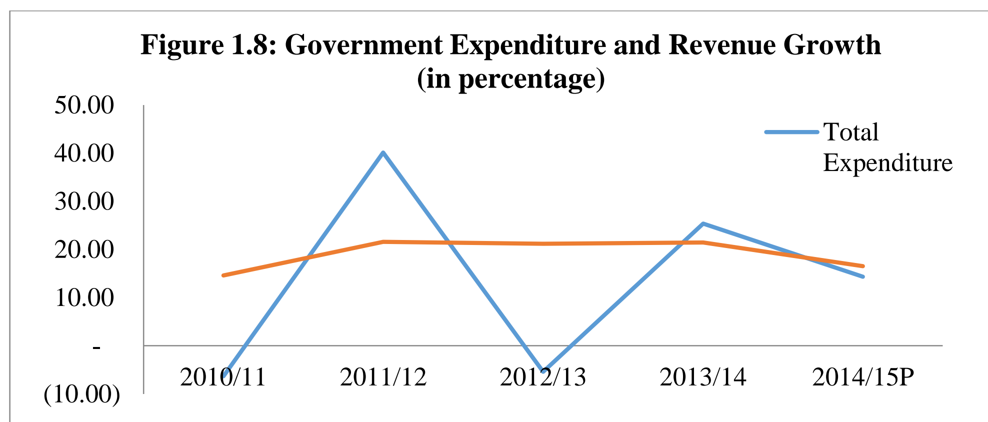


Figure 1.8: Government Expenditure and Revenue Growth (in percentage)

1.32 The government revenue mobilization increased by 16.6 percent to Rs. 190.52 billion during the first six months of 2014/15. Such revenue had increased by 21.5 percent in the corresponding period of the previous year.

1.33 The budget surplus (on cash basis) surged to Rs. 64.95 billion in first six months of 2014/15 compared to Rs. 56.10 billion in the corresponding period of the previous year. Lack of elected representatives at local level, cumbersome procurement laws, and existing political transitional phase, among others have hindered the timely spending of the allocated capital expenditure.

1.34 Outstanding domestic debt stood at Rs 189.52 billion as of mid-January 2015. Such debt had stood at Rs 212.73 billion in mid-January 2014. The government has settled Rs. 12.30 billion of domestic debt in the first half of 2014/15.

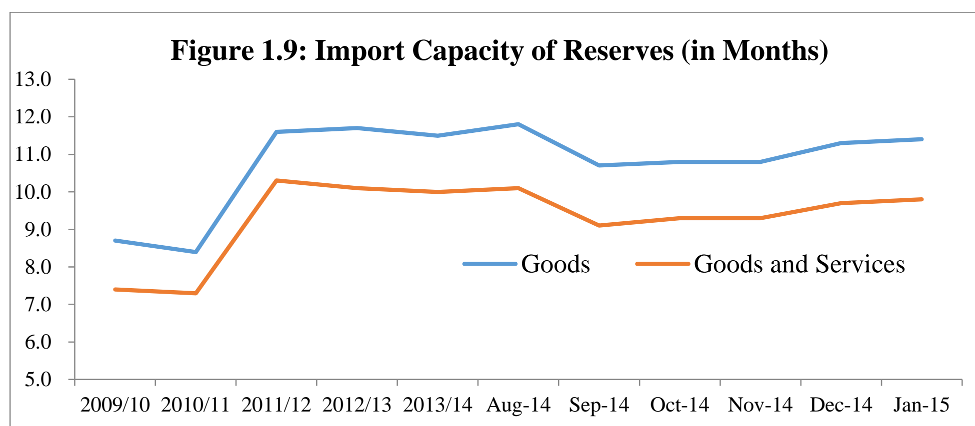
1.35 Given the huge expenditure required for post quake rehabilitation and reconstruction, both recurrent and capital expenditures are likely to surge in

coming years. Significant mobilization of domestic and foreign debt is likely to occur, which may have important implication for the financial stability. Nevertheless, the risks associated with rise in public debt are modest as the outstanding debt to GDP ratio is around 26 percent at present.

External Sector

1.36 Merchandise exports decreased by 3.9 percent to Rs. 43.39 billion during the first six months of 2014/15 compared to its growth of 15.0 percent during the corresponding period of the previous year. Likewise merchandise imports increased by 13.3 percent to Rs. 378.22 billion in the review period. Such imports had risen by 23.1 percent during the corresponding period of the previous year. Consequently, total trade deficit went up by 16.0 percent to Rs. 334.83 billion during the review period. Given the high growth of imports relative to exports, the ratio of export to import declined to 11.5 percent during the first six months of 2014/15. Such ratio stood at 13.5 percent in the corresponding period of the previous year. The share of India in total foreign trade stood at 63.6 percent during the first six months of 2014/15.

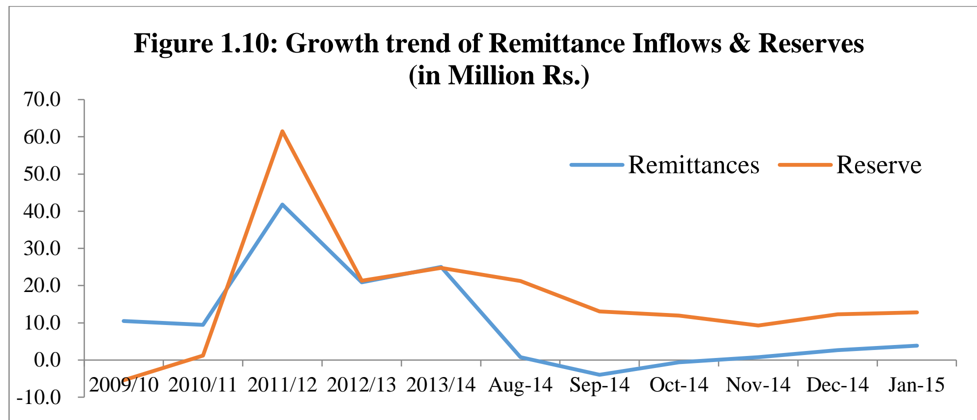
Figure 1.9: Import Capacity of Reserves (in Months)



1.37 The overall BOP recorded a surplus of Rs. 34.26 billion during the first six months of 2014/15 compared to a surplus of Rs. 77.19 billion during the same period of the previous year. Existing foreign exchange reserve is sufficient for financing merchandise imports of 11.4 months and merchandise and service imports of 9.8 months as at mid-January 2014.

1.38 The current account and BOP performance of Nepalese economy is largely driven by the volume of merchandise imports and inflow of remittances. Workers' remittances grew by 3.9 percent to Rs 275.96 billion in the first half

of 2014/15 compared to 34.4 percent of the corresponding period of the previous year.



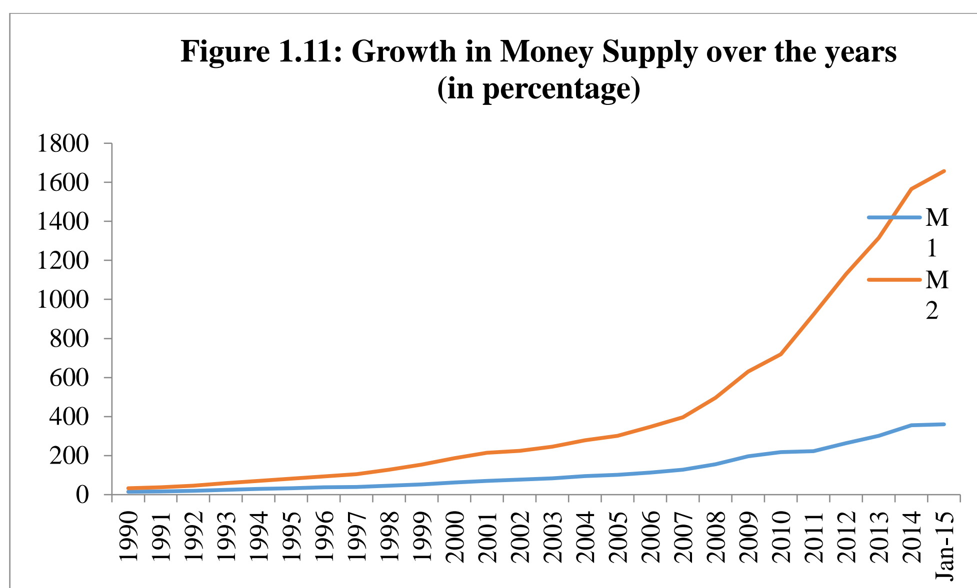
1.39 During the first six months of 2014/15, total foreign exchange reserve increased by 5.9 percent to Rs. 704.44 billion. Such reserve had grown by 17.1 percent in the corresponding period of the previous year. The growth rate of reserve is closely linked with growth of remittances in Nepal since the last few years. Remittance inflow is also contributing to the expansion of financial sector and deposit mobilization; hence remittance inflow correlated with the liquidity situation of the banking sector. The fluctuation in the remittance inflow creates uncertainty to the foreign exchange reserve position. However, given the widening base and frequent flow of the Nepalese workers visiting working abroad, external sector is expected to remain resilient.

Monetary Situation

1.40 The monetary policy for 2014/15 is directed to contain inflation originating from aggregate demand side and maintain external balance as well as financial sector stability. In addition, the monetary policy is also focused on increasing credit flows to the productive sectors for sustainable economic and financial sector development, and on expanding financial services and financial inclusion.

1.41 Broad money supply (M2) increased by 5.8 percent in the six months of 2014/15 compared to an increase of 9.0 percent in the corresponding period of the previous year. Likewise, narrow money supply (M1) grew by 1.6 percent in the review period compared to a growth of 8.9 percent in the same

period of the previous year. On year-on-year (y-o-y) basis, M2 and M1 expanded by 15.6 percent and 9.8 percent respectively, in mid-January 2015.



1.42 Net foreign assets (after adjusting foreign exchange valuation gain/loss) increased by Rs. 34.26 billion (5.7 percent) during the review period compared to an increase of Rs. 77.19 billion (16.5 percent) in the corresponding period of the previous year. A decelerated growth of remittance inflows accompanied by a decline in grant inflows resulted in a slower growth of net foreign assets in the review period.

1.43 Domestic credit increased by 5.6 percent in the review period compared to a growth of 1.1 percent in the same period of the previous year. On y-o-y basis, domestic credit increased by 17.8 percent in mid-January 2015.

1.44 During the first six months of 2014/15, claims on private sector increased by 11.5 percent compared to a growth of 8.9 percent in the corresponding period of the previous year. On y-o-y basis, the claims on the private sector increased by 21.1 percent in mid-January 2015.

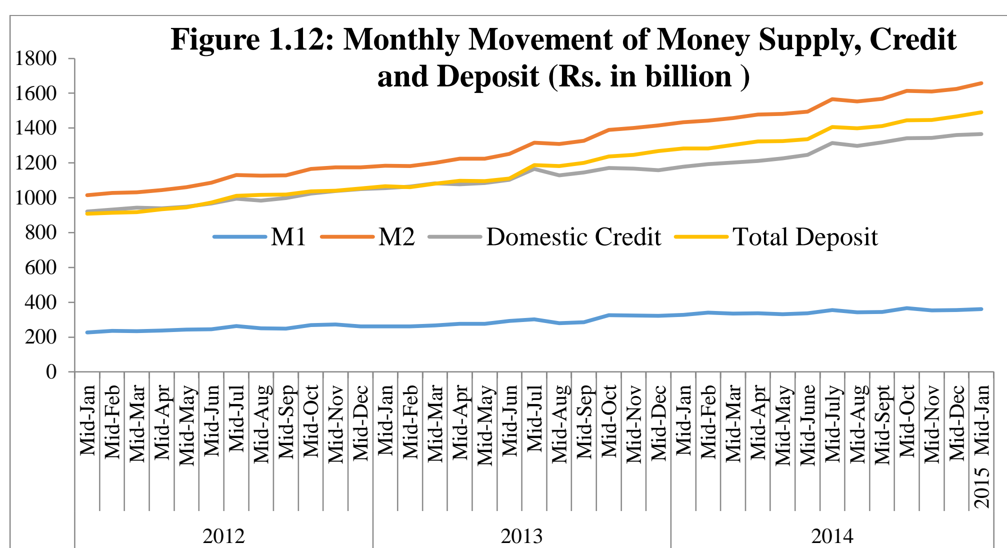


Figure 1.12: Monthly Movement of Money Supply, Credit and Deposit (Rs. in billion)

1.45 Reserve money decreased by 12.4 percent during the first six months of 2014/15 as against an increase of 2.2 percent in the corresponding period of the previous year. Decrease in deposits of BFIs and other deposits at Nepal Rastra Bank (NRB) contributed to the decline in reserve money in the review period.

Liquidity Situation

1.46 In the six months of 2014/15, the NRB mopped up liquidity of Rs.75.0 billion through deposit auctions and Rs. 260.50 billion through reverse repo auction on cumulative basis. In the corresponding period of the previous year, Rs. 118.50 billion was mopped up through reverse repo auction. The deposit auction introduced on monetary policy 2014-15 has been used as a new instrument to mop up liquidity since the second month of 2014/15. In the review period, the NRB injected net liquidity of Rs. 157.20 billion through the net purchase of USD 1.66 billion from foreign exchange market (commercial banks). Net liquidity of Rs. 168.93 billion was injected through the net purchase of USD 1.69 billion in the corresponding period of the previous year. NRB purchased Indian currency (INR) equivalent to Rs. 171.10 billion through the sale of USD 1.74 billion in the review period. INR equivalent to Rs. 143.06 billion was purchased through the sale of USD 1.44 billion in the corresponding period of the previous year.

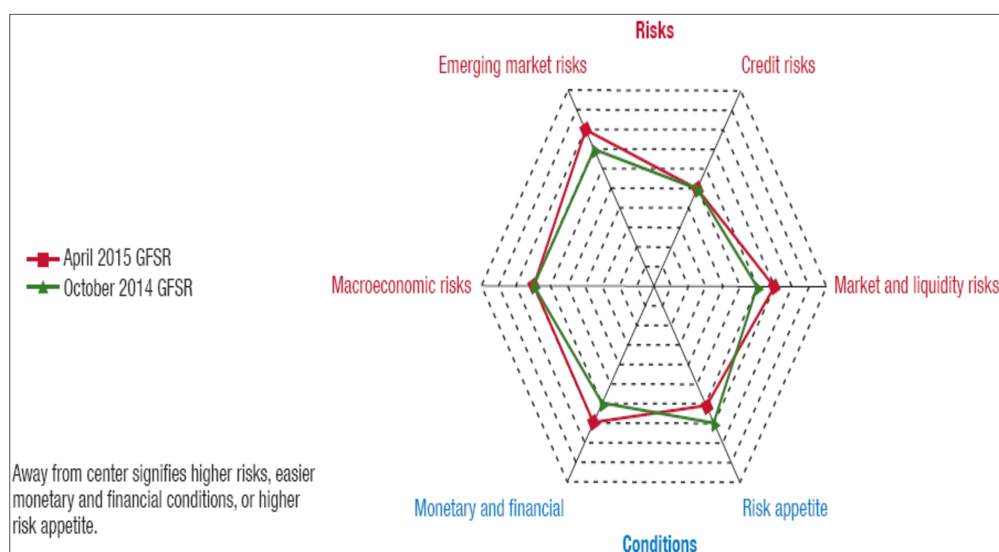
CHAPTER - TWO

FINANCIAL SYSTEM PERFORMANCE AND STABILITY

Global Financial Stability Overview

2.1 Global Financial Stability Report (*GFSR*) April 2015 states that financial stability risks have increased since the *October 2014* which is also reflected in the Global Financial Stability Map (Figure 2.1). Weaker inflation and greater uncertainty are weighing on the macroeconomic outlook. But these forces are broadly offset by favorable developments in high-frequency indicators, reflecting the expected benefits of lower oil prices and additional monetary accommodation, leaving *macroeconomic risks* broadly unchanged since October.

Figure 2.1: Global Financial Stability Map



Source: Global Financial Stability Report, April 2015

2.2 The U.S. economy is expanding, with rising employment and an improving investment outlook, as economic risk taking has taken hold. U.S. monetary authorities have clearly communicated that a process of monetary normalization could begin this year with an increase in policy rates. The bad news is that lower growth prospects elsewhere, relative to October 2014, and disinflationary forces have continued to exert a strong influence on the global economy.

2.3 Central banks have responded to increased downside risks to price stability. Since October, the Bank of Japan (BOJ) and the European Central Bank (ECB) have announced bold new monetary measures designed to ward off deflation pressure and move their economies closer to their inflation objectives. Other central banks have cut rates or loosened their monetary policy stances, and markets are generally pricing in lower policy rates by the end of 2015 for a number of countries. The policy easing has offset modestly tighter real interest rates and thus loosened monetary and financial conditions overall.

2.4 Financial stability risks have increased in Emerging market. The easing of inflation pressure is benefiting many emerging market economies, giving them monetary policy space to combat slowing growth. However, recent global shocks—including higher political risks—leave several emerging market economies more vulnerable.

2.5 Reflecting the challenges facing emerging markets, risk appetite is lower as currency volatility and adjustments have prompted a pullback of capital flows by foreign investors. Lower allocations of global funds to risky assets and lower excess returns also indicate slightly lower risk appetite compared to October, although appetite remains above its historical average.

2.6 Credit risks are broadly unchanged. Although the macroeconomic benefits of lower energy prices may have a favorable impact on household balance sheets, the immediate credit impact of oil and commodity price declines on firms in the energy sector is negative. Furthermore, the fall in nominal yields—should it be sustained—raises a serious threat to the life insurance and pension fund sectors, especially in Europe.

2.7 These developments have created various tensions in global financial markets, raising market and liquidity risks. Asynchronous monetary policies have led to a sharp increase in volatility in foreign exchange markets amid a rapid appreciation of the U.S. dollar. Despite the prospect of gradual U.S. policy rate tightening, longer-term U.S. bond yields and term premiums remain compressed as the ECB and Bank of Japan ramp up their asset purchases.

2.8 Asset valuations remain elevated relative to the past 10 years as monetary policies continue to exert downward pressure on spreads. Market volatility has increased across the asset spectrum, rising from the record lows at the

time of the *October 2014 GFSR*. The structural features that have contributed to reduced market liquidity and warns that economic and policy tensions leave global markets vulnerable to bouts of illiquidity that could prove systemic.

2.9 Apart from these recent development, continuous plunge in crude oil prices also have a significant impact on overall financial stability. Box 2.1 explains about the impact of recent oil price fallout and its implication to the financial sector.

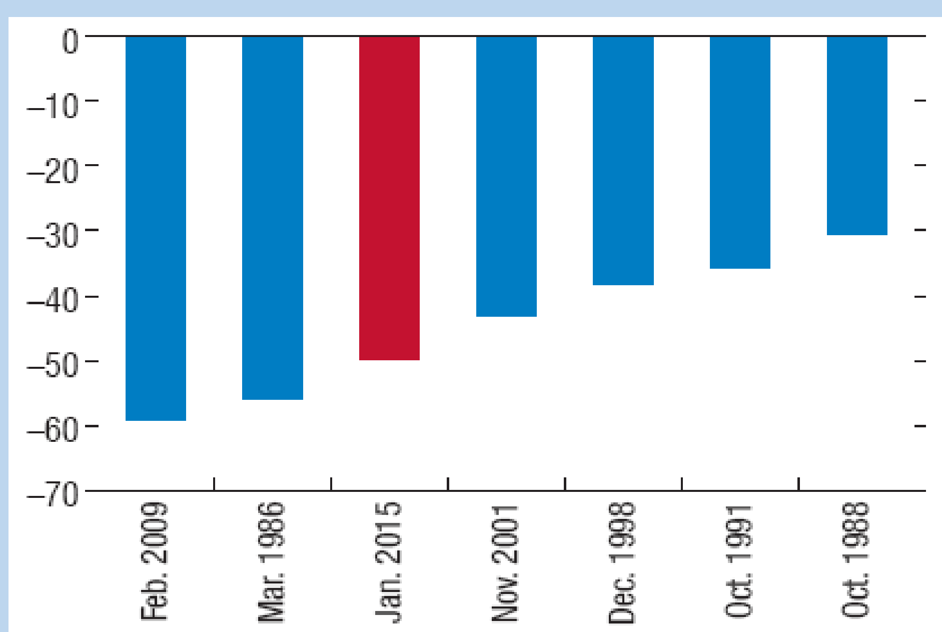
BOX 2.1: The Oil Price Fallout—Spillovers and Implications for the Financial Sector

As one of the steepest on record, the recent decline in oil prices appears to reflect supply factors, a net benefit to the global economy over the medium term. Nevertheless, the speed and magnitude of the movement in oil prices may produce financial strains in selected areas as markets adjust to a new pricing environment. This box discusses three channels through which such an adjustment could potentially contribute to an increase in market volatility.

Amplification of credit risk: Countries and companies dependent on oil revenues have already been significantly repriced by investors since summer 2014, as reflected in bond spreads, equity prices, and currency movements. Although risk premiums have widened, however, the impact has probably not yet fully hit in several areas. These effects include refinancing risk for energy-producing sovereigns and firms, and the reduction in bank funding lines to energy companies in response to breaches in lending covenants.

Country refinancing risk: Fiscal breakeven prices vary widely across oil-producing countries in emerging markets, from $54 a barrel for Kuwait to as much as $184 a barrel for Libya. Barring spending cuts, new sources of revenue, or tapping fiscal buffers, the loss in oil revenue will require new sources of financing. U.S. dollar–based bond spreads for emerging market oil exporting countries have already doubled since summer 2014, which suggests that refinancing conditions are now more problematic. Local currency depreciation may also put upward pressure on inflation where domestic inflation expectations are not well anchored, further raising the risk premium on sovereign debt.

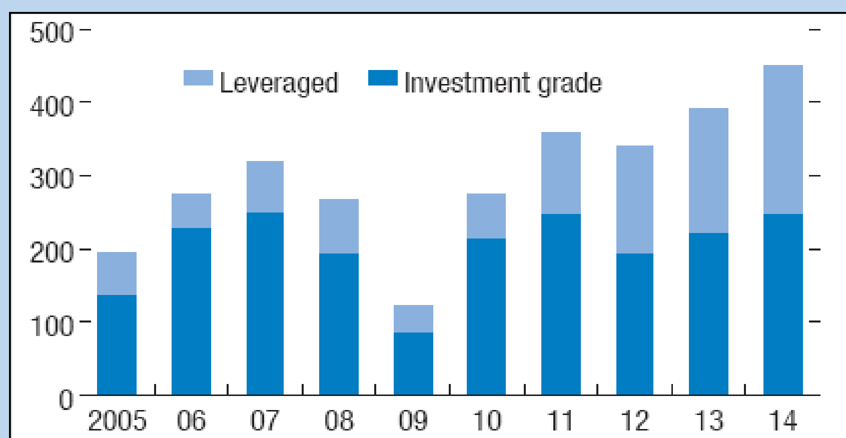
Figure 2.2: Largest Annual Oil Price Declines (in percentage)



Corporate refinancing in the energy sector: Scaled back energy sector exposure by banks and corporate bond investors could amplify strains associated with falling revenue and higher funding costs. Historically, corporate defaults in the energy sector have tended to pick up in response to falling oil prices, with a lag of about 12 months, (Fitch 2015b) likely reflecting a typical one-year hedging horizon by producers. Since the downdraft in oil prices did not begin to accelerate until September 2014 (at which point Brent and West Texas Intermediate prices were still higher than $100 a barrel), aftershocks for the corporate sector may not yet have fully filtered through.

The outstanding worldwide notional value of bank loans and corporate debt extended to the energy sector amounts to about $3 trillion, $247 billion of which is attributable to the U.S. high-yield bond market alone. Global syndicated loan issuance in the oil and gas sector has risen markedly in recent years; with €450 billion in issuance in 2014 alone; almost double that of the previous cycle peak in 2007.

Figure 2.3: Global Syndicated Loan Issuance from the Oil and Gas Sector (in Billions of Euros)



In addition, the leveraged (that is, high-yield) share of syndicated oil and gas loan issuance has steadily increased, from 17 percent in 2006 to 45 percent in 2014. The majority of global systemically important banks have about 2 to 4 percent of their total loan book exposures devoted to the energy sector. Available data suggest that there are higher exposures by selected banks in emerging markets and among some U.S. regional banks (although firm estimates are difficult to determine). A prolonged period of low oil prices will jeopardize the debt-servicing capacity of exploration and production firms that have high cost bases.

Oil surpluses and global liquidity: Foreign exchange reserves accumulated by net oil-exporting countries have increased $1.1 trillion, or almost fivefold, over the past decade accounting for about 15 percent of the cumulative rise in world foreign exchange reserves since 2004. These funds have been an important source of funding for the global banking sector and capital markets more broadly. Deposits from oil-exporting countries in Bank for International Settlements–reporting banks have doubled to $972 billion since 2004, and this group of countries (private and public sector) now holds more than $2 trillion in U.S. assets, spread across equities ($1.3 trillion), Treasuries ($580 billion), credit ($230 billion), and agency debt ($21 billion). Following the $88 billion contraction in oil-exporter reserves in 2014, sensitivity analyses point to further significant declines in 2015 if oil prices follow the path implied by futures markets. In principle, the decline in investable oil surpluses is part of global rebalancing and ought to be counterbalanced—at least to some extent—by wealth gains on the part of oil importers.

But such redistribution between agents with potentially varying savings and portfolio preferences may also have market repercussions, particularly if the pace of adjustment creates market dislocations.

Strains on financial infrastructure: Oil and other commodity markets have attracted much greater focus from the institutional investment community over the past decade. For example, noncommercial (that is, speculative) investors held about 45 percent of West Texas Intermediate futures contracts in 2014, about triple the level held during the 1990s. Banks have also retreated from their market-making and structuring roles in energy markets, with a shift in trading activity to centrally cleared contracts (as desired by regulators) and physical commodity trading houses. With such major changes in market structure, questions have been raised as to whether an additional wave of selling pressure might destabilize markets. There has already been substantial selling—net investment exposure is nearly what it was at its peak in early 2014, and mutual fund data suggest that U.S. high-yield bond funds are already underweight in energy compared with the benchmark. Assets under management in commodity funds, combined with commodity-linked exchange-traded products, are nearly half their 2010 peak. Implied volatility (a measure of insurance value) has increased, but only to levels recorded in 2011–12 and well shy of levels reached in 2008. On balance, few indicators point to severe dislocations in oil markets. Commodity exchanges have a long history of managing counterparty risk during heightened volatility (through changes in margining requirements and circuit breakers). Nevertheless, financial intermediaries should remain on the alert for threats to efficient market functioning.

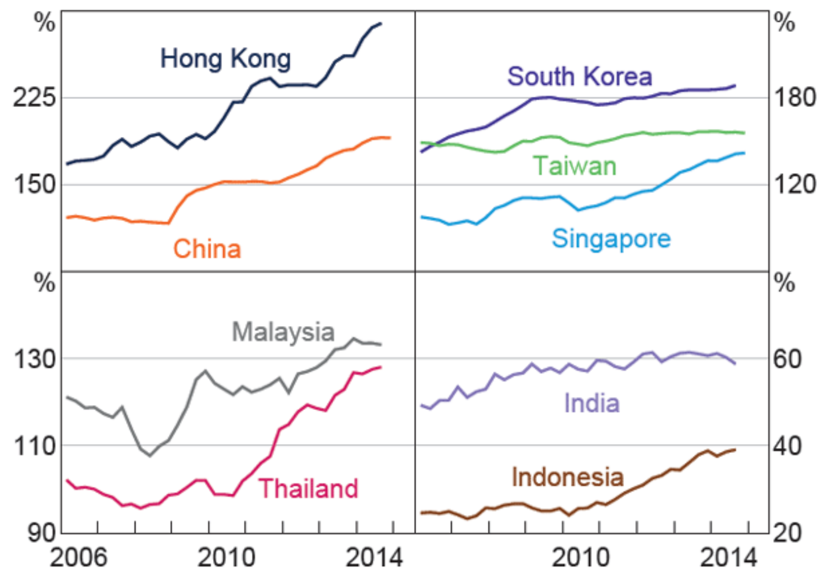
Source: Global Financial Stability Report April 2015

Credit Growth in Asia

2.10 Credit flows have been growing in Asia since 2006. In China, credit flows have continued to grow, albeit at a slower pace, as the authorities have implemented measures to put non-bank and off-balance sheet financing on a more sustainable footing and economic growth has continued to slow (Figure 2.4). Concerns about the Chinese shadow banking sector include that exposures may be to marginal borrowers – particularly property developers – unable to obtain financing through the banking system, and that the sector has a number of linkages with banks that are not well understood. To address these risks, the authorities have recently put in place further policy measures

to address aspects of the Chinese financial system that contributed to growth in the shadow banking sector. These measures include relaxing ceilings on deposit interest rates, draft regulations to constrain entrusted loans from being funded by debt or invested in most financial instruments and announced deposit insurance scheme.

Figure 2.4: Credit Growth in Asia (percent of nominal GDP)



Source: Financial Stability Review, Reserve Bank of Australia

Overview of Nepalese Financial System

2.11 Nepalese financial system comprises of banking, insurance, securities markets, contractual saving institutions and other service sectors. The system has different regulators. Banking system, which has significant shares in number (around 89 percent), dominates significantly to financial system in terms of assets as well. The common characteristics of Nepalese banking system include poor corporate governance, inadequate risk management practices, high real estate credit exposure, and compliance based supervision with inadequate supervisory resources and loan ever-greening practices of BFIs. Similarly, with the huge expansion in the network of banking sector, NRB is facing challenges in allocation of its limited resources for risk-based supervision.

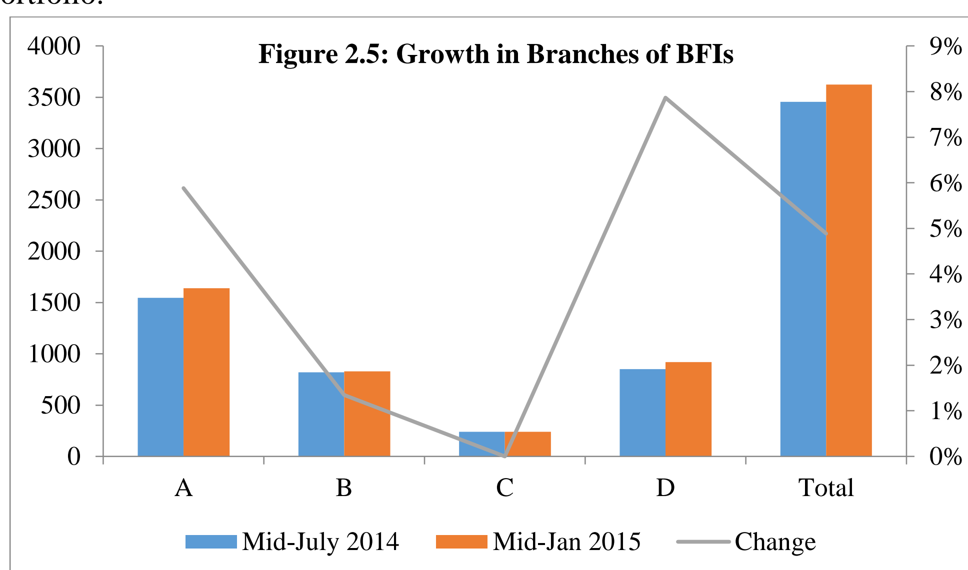
2.12 General overview of the financial system is shown in table 2.1. As of mid-Jan 2015 there are altogether 270 financial institutions in the country (excluding government licensed cooperatives). During six months to mid-Jan 2015 number of development bank and finance companies decreased by two each due to merger among BFIs.

Table 2.1: Number of BFIs and Other Institutions (mid-January 2015)

Banks and Financial Institutions	Mid-July 2012	Mid-July 2013	Mid-July 2014	Mid-Jan 2015
Commercial Banks	32	31	30	30
Development Banks	88	86	84	81
Finance Companies	70	58	53	51
Microfinance Development Banks (MFDBs)	23	31	37	35
Sub-Total	**213**	**206**	**204**	**197**
NRB Licensed Cooperatives	16	16	15	15
NRB Licensed FINGOs	34	31	29	29
Insurance Companies	25	25	25	26
Contractual Saving Institutions				
Employees Provident Fund (EPF)	1	1	1	1
Citizen Investment Trust (CIT)	1	1	1	1
Postal Saving Bank	1	1	1	1
Total	**292**	**282**	**276**	**270**

Structure and Performance of Banks and Financial Institutions

2.13 The central bank has been adopting the policy of merger and acquisition to attain its objectives of consolidating some FIs to efficient and strong FIs in the financial system. A stable financial system is determined by a sound and strong banking system which holds dominant role in the national economy. BFIs are extending branches in different parts of the country which helps to achieve the goal of inclusive growth of the nation. During the six months to the mid-January, BFIs have added significant number of branches to their portfolio.



2.14 As the above picture shows, BFIs have added 169 branches during first six months of FY 2014/15, resulting growth of 4.89 percent. Overall growth in numbers of branches is propelled by significant growth in branches A and B class BFIs. Number of BFIs across the development regions is presented in table below.

Table 2.2: Distribution of BFIs across the region

Region/BFI Class	A	B	C		Total
Eastern	304	109	26		439
Central	812	317	136		1265
Western	284	298	66		648
Mid-western	146	77	9		232
Far-western	92	28	2		122
Total	1638	829	239		2706

Size of Nepalese Banking System

2.15 The total assets and liabilities of BFIs have continued to increase. As of mid-Jan 2015, total assets of BFIs have increased by 6.82 percent to Rs. 1973 billion during first six of the fiscal year. Balance sheets of BFIs expanded mainly due to growth in deposits and credits. The liabilities side of the balance sheet also magnified on account of the increasing deposits as well as paid up capital which is raised by issuance of right shares and bonus share to meet their minimum regulatory capital.

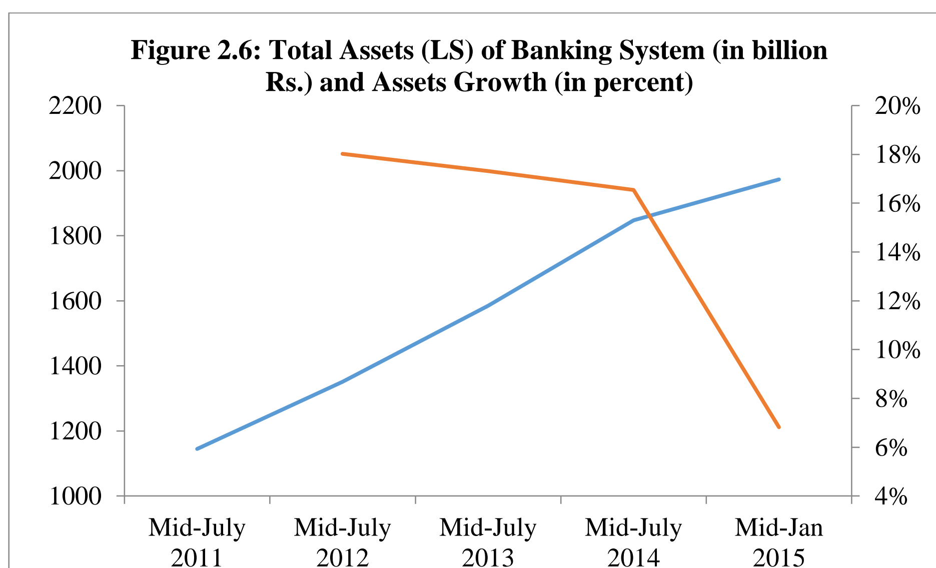
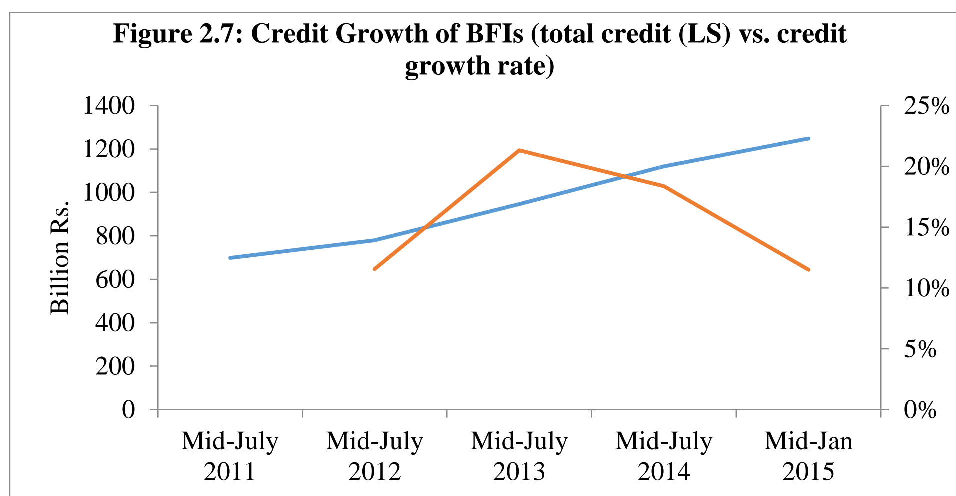


Figure 2.6: Total Assets (LS) of Banking System (in billion Rs.) and Assets Growth (in percent)

Credit Expansion

2.16 The credit flows form NRB regulated A, B and C class financial Institutions account about 66 percent of the GDP of the country. Bank credits have been growing over the years to reach Rs.1248 billion in mid-January 2015 from Rs.1119 billion in mid-July 2014. However, rate of credit growth has been volatile since mid-July 2012. The slower credit growth in recent period can be attributed to weak business confidence resulting from the prolonging political uncertainty.



Sectoral Credit Flow of BFIs

2.17 The credit flow is highest in wholesale and retail business among the identified sectors while agriculture, forestry and beverage production stands the second position. Credit flow to the wholesale and retail accounted to 21.89 percent of the total credit flow as of mid-January 2015. Similarly, agriculture, forestry and beverage production related credit flow accounted to 20.31 percent. While the credit flows for industries in primary sector are significant, credit flows in agricultural and forest related sectors are minimal at 4.30 percent of total credit. This has been major concern for regulators as lax growth in credit flow in primary sector has been hindering overall economic growth of the country.

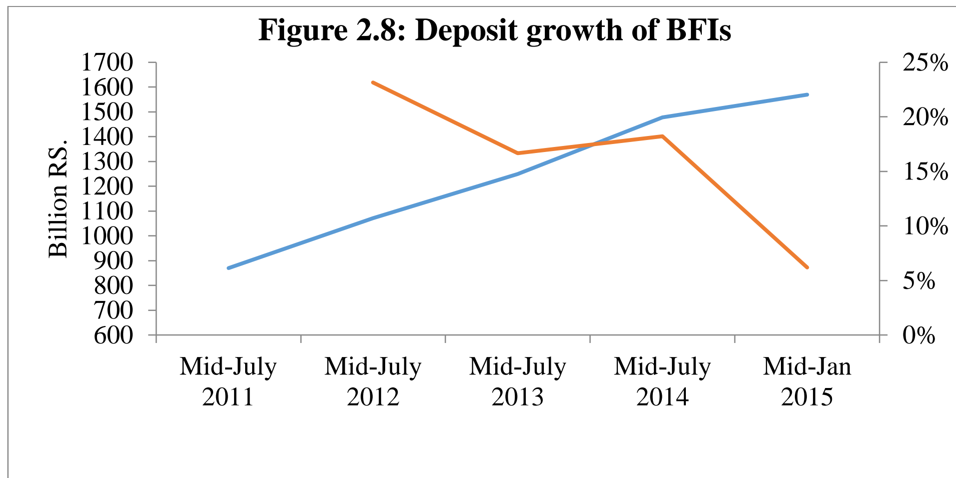
Table 2.3: Sectoral Credit Flow of BFIs (in Billion Rs.)

Sectors	Mid-July 2012	Mid-July 2013	Mid-July 2014	Mid-Jan 2015	Share in Mid-Jan 2015
Wholesaler & Retailer	159.51	198.32	243.97	276.67	21.89%
Agriculture, Forestry & Beverage Production Related	156.34	190.58	222.49	256.7	20.31%
Others	103.35	124.83	141.31	158.26	12.52%
Construction	82.31	96.07	118.63	135.65	10.73%
Finance, Insurance and Real Estate	80.17	84.68	90.35	94.33	7.46%

Consumption Loans	49.31	69.44	87	94.04	7.44%
Other Services	38.9	46.72	54.15	57.22	4.53%
Agricultural and Forest Related	28.58	39.15	48.15	54.39	4.30%
Transport, Communication and Public Utilities	39.37	41.3	43.71	44.46	3.52%
Hotel or Restaurant	20.94	25.09	32.91	38.88	3.08%
Electricity, Gas and Water	14.21	20.69	25.61	29.66	2.35%
Metal Products, Machinery & Electronic Equipment & Assemblage	10.85	13.05	13.99	15.38	1.22%
Mining Related	2.71	3.9	3.58	3.54	0.28%
Fishery Related	1.83	0.66	2.75	2.96	0.23%
Local Government	1.36	1.26	1.18	1.58	0.12%
TOTAL	**789.7**	**955.7**	**1129.8**	**1263.7**	**100**

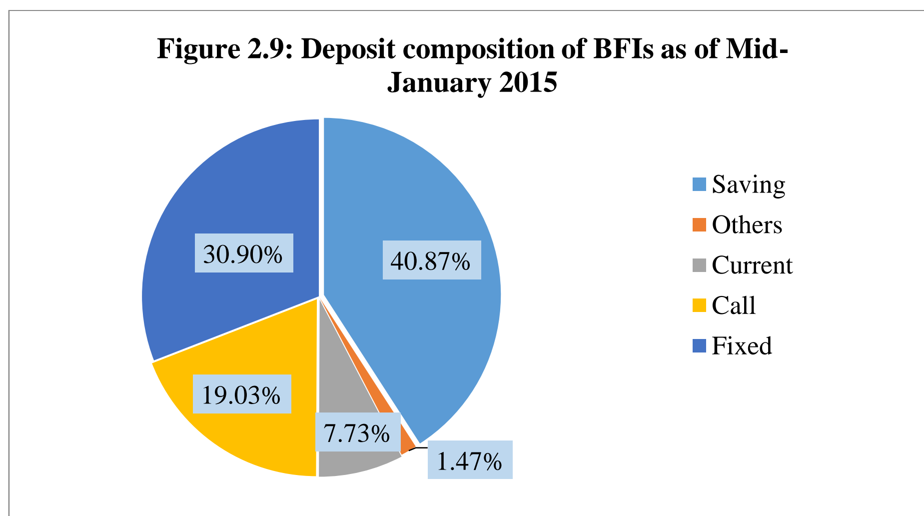
Deposit Collections

2.18 Deposits of BFIs have been increasing in recent years to stack up 81.37 percent against GDP of the country. Increases in deposits are mainly driven by ever increasing remittance inflows and expansion of branches in interior parts of the country. Furthermore, the government and NRB have been taking steps to increase banking channel for business and trading activities by introducing new provisions and rules. As of mid-January 2015, deposits reached to Rs.1569 billion from Rs.1478 billion, registering a growth of 6.16 percent during the first six months of the FY 2014/15.



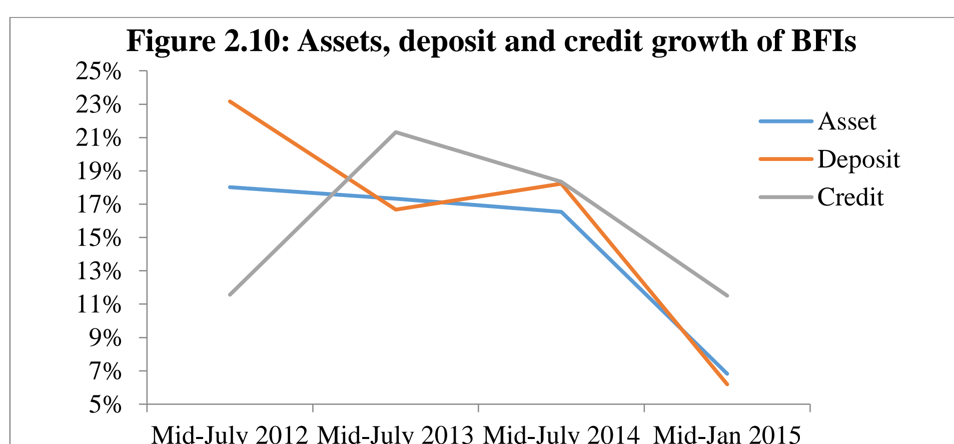
Composition of Deposit Collection

2.19 Saving deposits have higher share in the total deposits of BFIs, followed by fixed deposits, call deposits, current deposits and other deposits respectively. Having a high proportion of saving deposits is not bad for the BFIs as they have relatively lower interest rates but these funds cannot be invested for longer term as they might be withdrawn by the depositors any given day. Although, fixed deposits have higher interest rate, they are dependable sources for long term credits because of their elongated term. Thus, having a large chunk of fixed deposit is good for the financial system stability but there are more to be done to convert savings to fixed deposits. As of mid-January 2015, BFIs have Rs.641.38 billion savings while fixed deposits amount Rs. 484.84 billion.



Assets vs. Deposit and Credit Growth

2.20 Total assets, deposits and credit of the BFIs have been growing over the years but they are not in tandem with each other. Principally, they should have close to same growth rates but in practice that has not happened except in FY 2013/14. Data from mid-January 2015 show that assets and deposits have grown at similar paces (6.82 percent and 6.18 percent) while credit grew by almost twice (11.51 percent) than deposits.



Financial Soundness Indicators

Capital Adequacy

2.21 Capital adequacy of BFIs has come down from the level of mid-July 2014 due to relatively higher credit growth. The CAR of BFIs stood at 11.98 percent which was 12.74 percent in mid-July 2014. However, capital funds of BFIs rose by healthy margin, as of mid-January 2015, the capital fund of BFIs rose by Rs. 18.81 billion to Rs 164.67 billion during first two quarters of the fiscal year. The fund is composed of paid-up capital of Rs. 137.71 billion, statutory reserves of 36.13 billion and other reserves of Rs. 12.29 billion. It also comprises of retained earnings of Rs.21.77 billions in negative figure.

2.22 CAR of BFIs are enough to maintain regulatory requirement. CAR of commercial banks came down to 11.3 from the level of 12.03 on mid-July 2014. Similarly, CAR of development bank marginally shifted downward from 15.61 to 15.4 and fiancé companies' CAR dropped by two percentage points to settle at 13.96 on mid-January 2015.

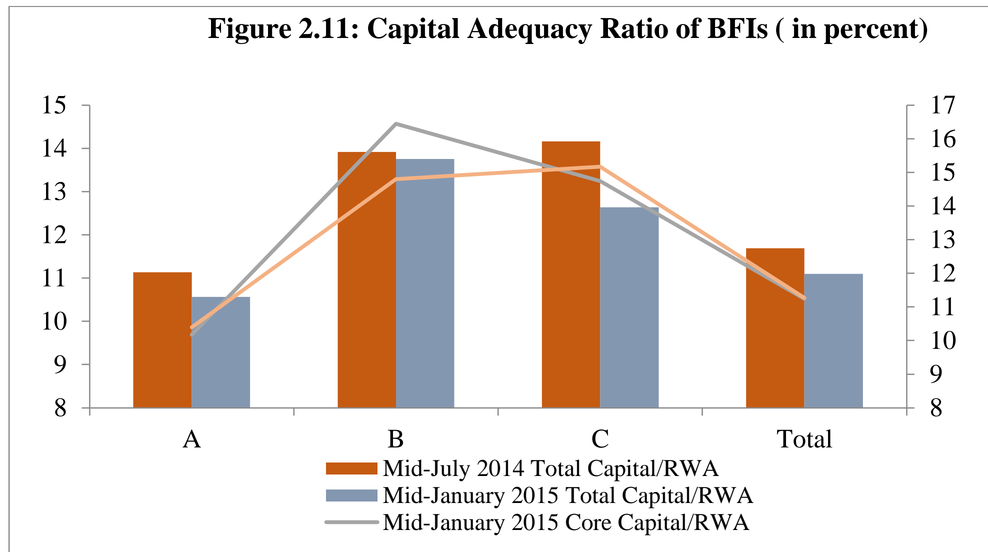


Figure 2.11: Capital Adequacy Ratio of BFIs (in percent)

Asset Quality

2.23 Banking sector witnessed an increase in NPA during the six months period to mid-January 2015; however, it remained below five percent. As of mid-January 2015, total NPAs of A, B and C class financial institution stood at 3.6 percent of total credit. Albeit the overall ratio remains below regulatory level of 5 percent, NPL of finance companies is staggeringly high at 14.9 percent. Such notorious level of NPL in finance company might cause a major setback in maintaining stability in banking system. NPLs of commercial bank and development banks remained below five percent at 2.93 percent and 4.01 percent respectively.

2.24 The provisions for possible loan losses at BFIs are adequate to cover up losses from NPL. As of mid-January 2015, total provisions of A, B and C class institutions was Rs.51.44 billion, or 4.07 percent of total loan.

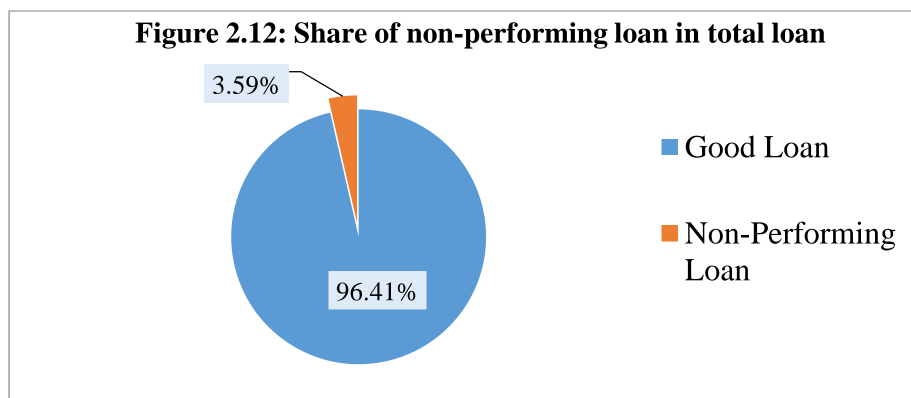


Figure 2.12: Share of non-performing loan in total loan

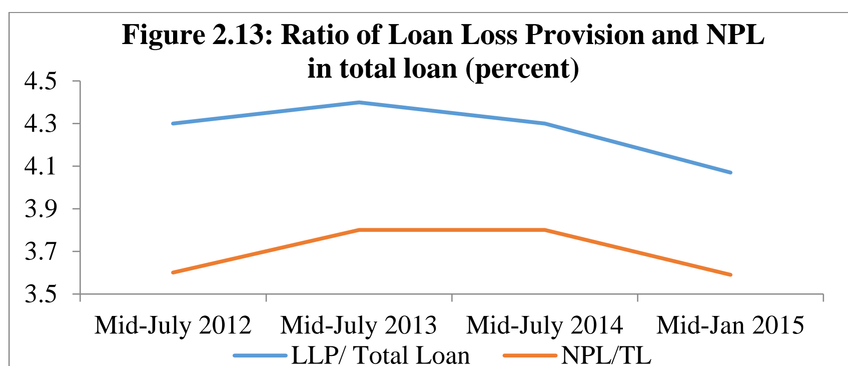


Figure 2.13: Ratio of Loan Loss Provision and NPL in total loan (percent)

Credit to Deposit Ratio

2.25 The credit to deposit (C/D) ratio of the BFIs has significantly grown during the six month period to mid-January 2015 to 79.5 percent from 75.7 percent on mid-July 2014. This growth was propelled by double digit growth in credit during the period while deposit growth being struck at six percent. While overall C/D ratio is quite healthy, class wise ratio tells a murky picture. Commercial banks have C/D ratio below 80 percent, but the ratio for development bank and finance companies are 83.2 percent and 87.7 percent respectively. NRB has restrained the BFIs to exceed C/D ratio above 80 percent but it has provided some leverage by adding core capital to the credit.

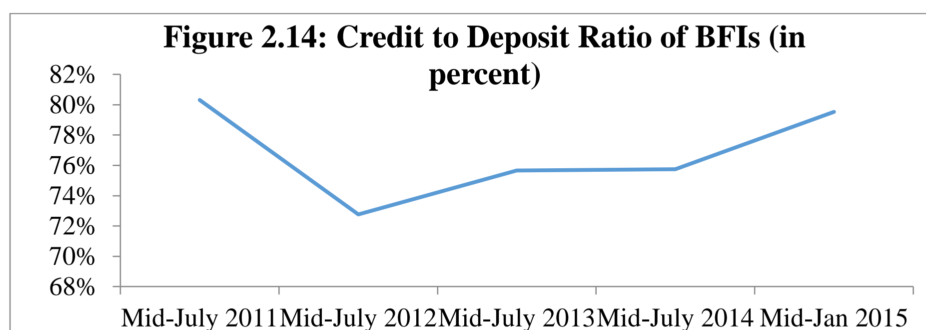
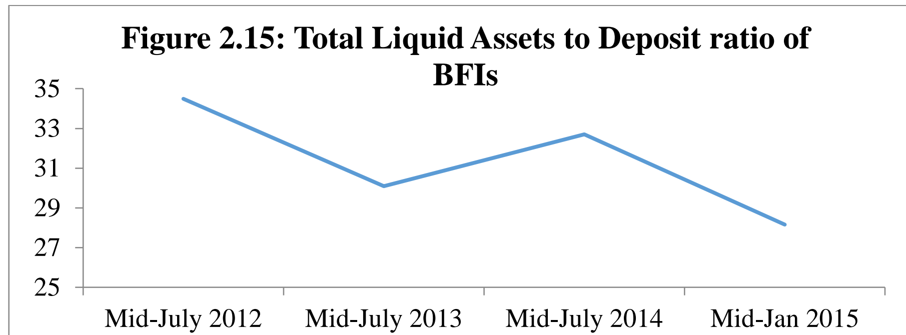


Figure 2.14: Credit to Deposit Ratio of BFIs (in percent)

Liquidity

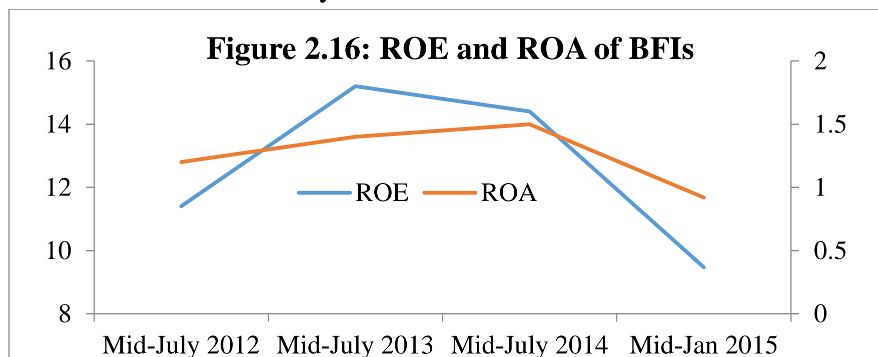
2.26 Nepalese banking system has been experiencing excess liquidity for around three years and there was no respite during last six months to mid-January 2015. Excessive liquidity is often blamed for lack of investment opportunities for BFIs due to stagnant political scenario. As of mid-January 2015, total liquid asset to deposit ratio of BFIs was at 28.2 percent, a slight improvement (in terms of easing excessive liquidity condition) from previous level of 32.7 percent in mid-July 2014. The liquid asset to deposit ratios for "A", "B" and "C" class institutions were recorded at 26.5 percent, 34.8 percent and 38.3

percent respectively. Hence, the ratios for all BFIs stood above the regulatory requirement but it is still high which have been causing to increase the cost of fund for BFIs.



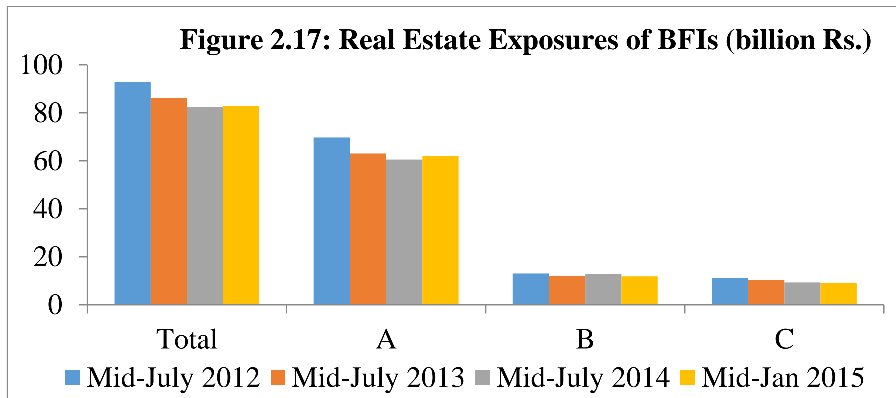
Profitability

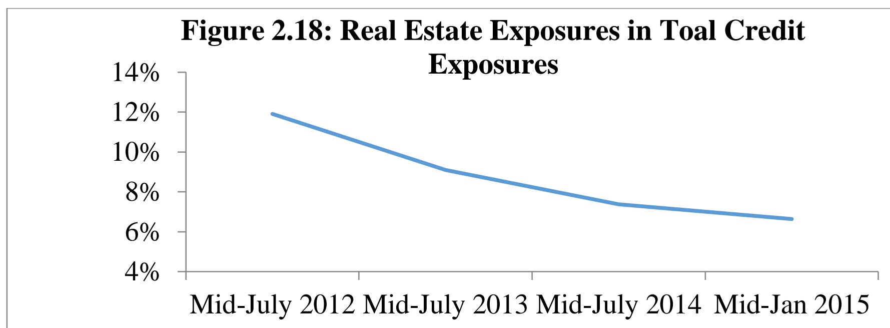
2.27 Most of BFIs are able to make impressive returns in FY 2014/15. As of mid-July 2015, ROE of BFIs are calculated at 9.5 percent, while ROA stands at 0.92 percent. Annualizing these six months figure returns for the ROE comes at 18.94 percent and ROA at 1.8 percent respectively. The annualized figures show that if everything remains same as in first six months period, BFIs would be able to make normal growth in returns over the period. However, yearend figures tend to be higher than annualized figures due to extended efforts in bad debt recovery.



Real Estate Exposures

2.28 Real estate exposures from A, B and C class BFIs have come down to tamable level after the central bank adopted stringent policies measures few a years back. As of mid-January 2015, total real estate exposure of BFIs stand at Rs. 82.8 billion, a slight increase from Rs.82.45 billion in mid-July 2014. These exposure accounts for 6.6 percent of total credit exposure as of mid-January 2015 from 7.4 percent in mid-July 2014. This was mainly because of increase in credits to other sectors of the economy.





2.29 Out of total real estate exposures, commercial bank have highest share of 74.8 percent (Rs.62 billion) as of mid-January 2015, development banks have 14.2 percent (Rs.11.8 billion) and finance companies have 10.92 percent (Rs.9 billion). It is obvious that commercial bank have large chunk of real estate exposures because of their size and capacity. However, if we look at the exposures as percentage of total credit, finance companies are highly exposed to the real estate sector with 13.7 percent of total credit. Commercial banks have only 6.11 percent and development banks have seven percent of total credit in realty sector.

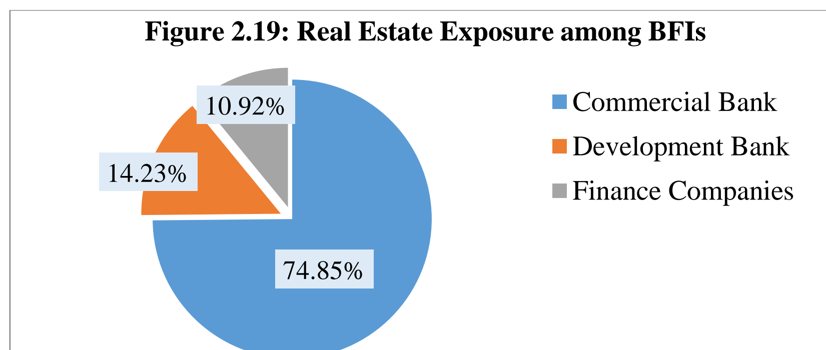


Table 2.4: Stability Indicators (Mid-January, 2015)

Indicators	A	B	C	Tota
Capital Adequacy Ratios				
Regulatory capital to risk-weighted assets	11.3	15.4	13.9	11.9
Regulatory Tier - 1 capital to risk-weighted assets	9.69	14.5	13.2	10.5
Non-performing loan to total gross loan	2.80	4.01	14.9	3.59
Non-performing loan net of provisions to capital	4.89	4.96	1.65	4.70
Sectoral Distribution of Loans to Total Gross Loan (percentage)				
Agricultural and Forest Related	4.12	5.94	2.99	4.30
Fishery Related	0.26	0.16	0.07	0.23
Mining Related	0.31	0.14	0.16	0.28
Agricultural, Forestry and beverage Production Related	23.5	6.47	5.93	20.3
Non food Production Related				
Construction	9.98	12.9	16.9	10.7
Electricity, Gas and Water	2.46	2.45	0.33	2.35
Metal Products, Machinery & Electronic Equipment &	1.19	1.46	1.07	1.22
Transport, Communication and Public Utilities	2.44	7.86	9.20	3.52
Wholesaler & Retailer	23.2	17.4	12.6	21.8
Finance, Insurance and Real Estate	7.61	6.78	6.95	7.46
Hotel or Restaurant	3.07	3.29	2.60	3.08
Other Services	4.62	4.44	3.39	4.53
Consumption Loans	7.29	8.05	8.24	7.44
Local Government	0.14	0.03	0.10	0.12
Others	9.80	22.5	29.4	12.5
Total	100.	100.	100.	100.
Returns on Assets	0.95	0.93	0.55	0.92
Returns on Equity	10.2	7.35	5.28	9.47
Interest Margin to Gross Income (percent)	68.3	80.3	76.8	70.3
Non-interest Expenses to Gross Income (percent)	37.7	42.2	46.9	38.7
Liquid Assets to total Assets	22.1	27.0	25.4	22.9
Liquid Assets to total Deposits	27.4	34.8	38.2	28.8
Credit to Deposit Ratio	79.6	83.2	87.7	80.5

CHAPTER –THREE

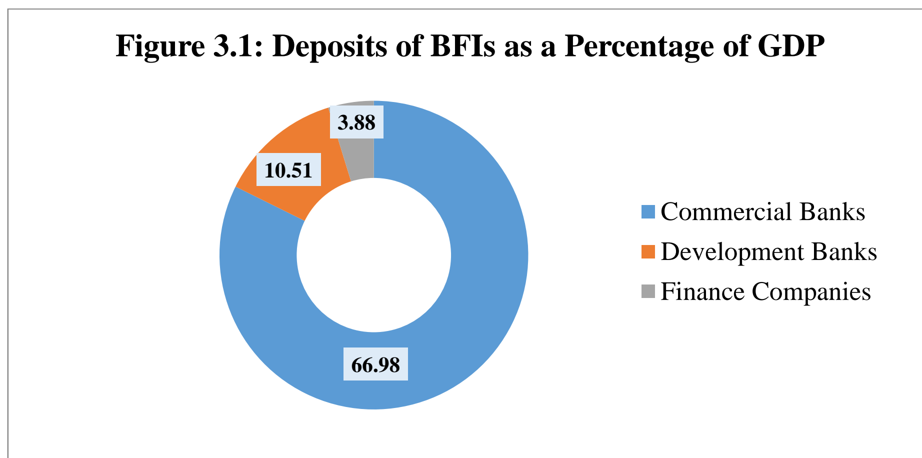
DEPOSIT TAKING INSTITUTIONS

Performance of Commercial Banks

3.1 Commercial banks have predominantly high share is total financial system as well and NRB regulated BFIs. As in mid-Jan 2015, share of total assets and liabilities of commercial banks on NRB regulated BFIs was 81.0 percent which increased by 7.9 percentage point from mid-July 2014. Similarly, share of total assets and liabilities of commercial banks on total GDP reached to 80.8 percent from 76.1 in mid-July 2014. The dominance of commercial banks in total banking sector in terms of assets and liabilities as well as in terms of balance sheet component has broadly remained stable with slightly upwardly movement. The total assets and liabilities of commercial banks increased by 17.2 percent to Rs. 1599.30 billion in mid-Jan 2015 from Rs. 1365.0 billion in mid-Jan 2014.

3.2 Total deposit and credit of commercial banks stood at 81.4 percent of the total deposits and credits of NRB regulated BFIs and 65.4 percent of GDP in mid-Jan 2015. Total deposits grew by 17.7 percent to Rs. 1291.7 billion during the period of mid-Jan 2014 to mid-Jan 2015, slightly lower than previous growth rate of 18 percent. Likewise, total credit flows grew by 24.4 percent to Rs. 1013.7 during the review period.

Figure 3.1: Deposits of BFIs as a Percentage of GDP



3.3 After loan and advances, investment in government securities emerged as a second best option for the commercial banks to utilize the excess liquidity. Investment in government securities increased by 2.6 percent to Rs. 159.2

billion in mid-Jan 2015 from Rs. 155.9 billion in mid-July 2014. In the context where major balance sheet indicators such as capital, deposits, lending, investments, liquid funds etc. are showing positive growth. Borrowing increased by a noticeable rate of 46.0 percent to Rs. 22 billion in mid-Jan 2015 in comparison to that in mid-July 2014. Such increase is due to excess liquidity prevailing in the financial system.

3.4 Capital fund of commercial banks rose by 13.9 percent to Rs. 123.9 billion in mid-Jan 2015 from Rs. 108.2 billion in mid-July 2014. Of which, paid up capital rose by 9.3 percent, whereas statutory reserves and other reserves rose by 11.1 percent and 8.3 percent respectively, during mid-July 2014 and mid-Jan 2015. However, retained earnings remained negative on mid-Jan 2015 due to negative net worth of RBB and NBL by Rs.12 and Rs.7 billion respectively.

Table 3.1: Overview of Commercial Banks (As of mid-January 2015)

S.N.	Titles	Figures
1.	Number of Banks	30
2.	Number of Branches	1638
3.	Number of ATMs	1433
4.	Number of Debit Cards	3738713
5.	Number of Credit Cards	53042
6.	Number of Deposit Accounts	10621935
7.	Number of Loans	681467
8.	Weighted Average Interest on Deposit	3.75
8.a.	(a) Saving	2.92
8.b.	(b) Fixed	6.03
8.c.	(c) Call	3.71
	Weighted Average Interest on Credit	9.74

3.5 Aggregate NPL to total loan ratio of commercial banks decreased to 2.7 percent in mid-Jan 2015 in comparison to the ratio of 2.9 percent in mid-July 2014. Aggregate NPL of three states owned commercial banks stood at 4.5 percent whereas that of private commercial banks is only 2.3 percent in mid-Jan 2015. As in mid-July 2014, average NPL ratio of three state owned commercial banks was 4.9 percent, whereas such ratio for private commercial banks was 2.5 percent. NPL ratio is below accepted threshold limit of 5.0

percent, which does not warrant financial stability risk while measuring in terms of assets quality.

Table 3.2: Major Financial Indicators of Commercial Banks (Mid-January 2015)

Indicators	Commercial Banks (percent)	Private-Sector Banks (percent)	SOBs (percent)
Tier 1 & Tier 2 Capital /RWE	11.66	11.87	10.82
Tier 1 Capital/RWE	10.06	10.21	9.48
NPL/Total Loan	2.66	2.27	4.61
Return on Equity	15.83	14.62	19.32*
Net Interest Spread	3.89	3.67	4.86
Total Credit to Total Deposit	79.69	81.03	73.87
Liquid Assets/Total Deposit	27.40	25.76	34.56
Base Rate	7.50	7.48	7.60

**ROE of State-owned banks are higher than average commercial bank due divestment of NIBL share by RBB.*

3.6 Despite the directive of NRB to BFIs to invest at least 12.0 percent of total loan in agricultural and energy sector, only 6.96 percent of total loans of commercial banks had been disbursed in agricultural sector and 2.2 percent in energy sector. Manufacturing (production) related sector availed 23.4 percent of total loan and retailer and wholesaler sector utilized 23.3 percent of total loan. Likewise, 6.0 percent and 7.2 percent of total loans went to real estate sector and consumption sector respectively.

3.7 While comparing the product-wise loan with the previous year, commercial banks found discouraged to invest in real estate lending (including other real estate loan) and as such lending has declined to 9.0 percent in mid-Jan 2015. Purpose wise loans in business sector increased by 12.2 percent, 13.9 percent and 19.8 percent respectively from the level in mid-July 2014. Bills purchased have seen a highest growth rate of 26.2 percent with respect to mid July 2014.There was remarkable growth in residential, hire purchase loan which shows that banking sector; especially the CBs have still higher attraction in such loans (retail lending) for the short term profitability and performance. Similarly, commercial banks have forwarded 4.5 percent of total loan in deprived sector in the review period. Collateral-wise, loan against real estate as collateral has been in the increasing trend. Out of total

loan, 81.5 percent of total loan has been disbursed against the collateral backup of fixed and current real assets.

3.8 Net Profit of the commercial banks stood at Rs.15.4 billion as of mid-Jan 2015 compared. Out of total 30 commercial banks, only one incurred net loss in the review period. Contribution of interest income is 75.84 percent of total income coming from interest payments on lending.

Base Rate of Commercial Banks

3.9 NRB introduced provision of base rate for BFIs since 2013. Initially, it was applicable to commercial bank and later it was expanded to national level development banks and finance companies too. Base rate is aimed at promoting transparency in setting interest rate for different products offered by these FIs to the clients and ensure sustainability of BFIs as they are suggested not to lend below the base rate. BFIs are required to publish their base rate on monthly basis in their websites and quarterly on national dailies for general public consumption.

3.10 As of Mid-January 2015, average base rate of commercial banks was 7.5 percent, recording a reduction of 78 basis points over the rate calculated on mid-July 2014. The reduction shows efficiency of commercial banks in delivering services. During the six months period to mid-January 2015, NCC bank slashed base rates by highest margin of 209 basis points to settle at 7.8 percent. While ten banks were able to reduce their base prices by more than one percentage point, four banks ended up increasing base prices during the review period.

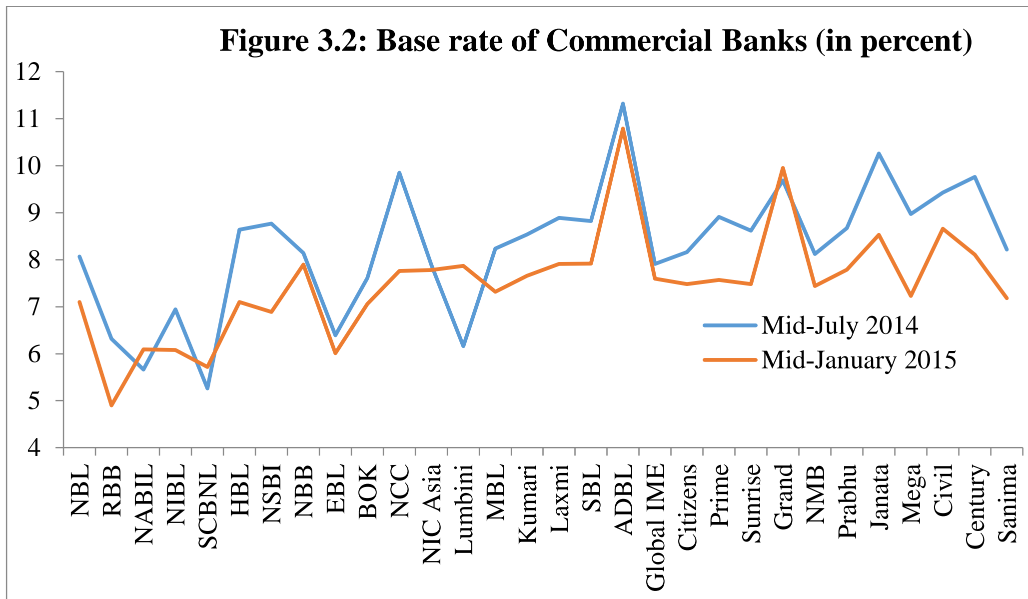
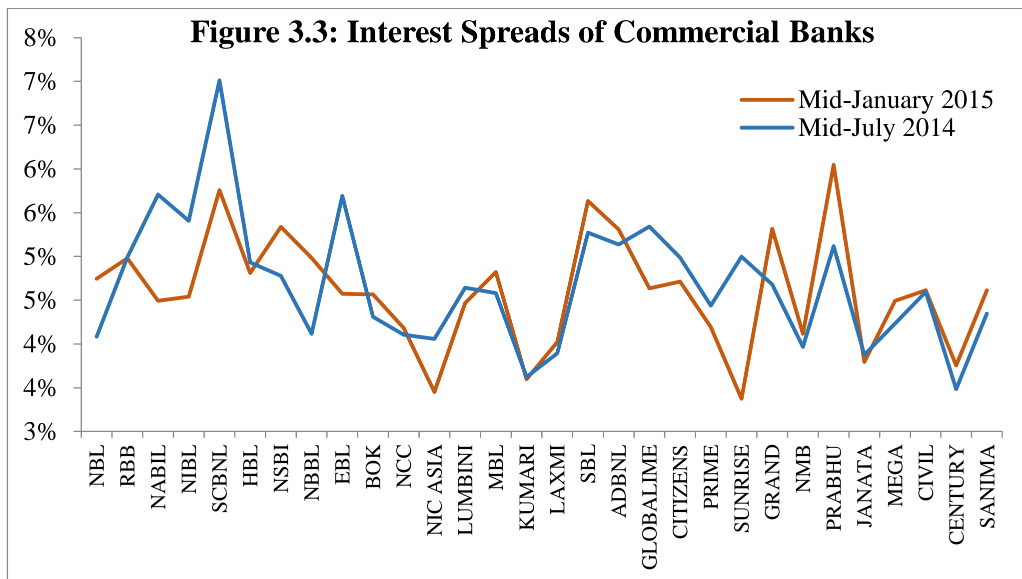


Figure 3.2: Base rate of Commercial Banks (in percent)

Interest Spreads in commercial banks

3.11 Spread is defined as the difference between average interest incurred and average interest earned. As of mid-January, 2015, the average interest spread of commercial bank was 4.6 percent, down from 4.7 percent in mid-July 2014. Reduction in spreads is considered beneficial for the economy as it helps to stimulate credit flow. Similarly, lesser spread may induce new savings. Out of the all 30 commercial banks, 16 were able to reduce their spreads, while 16 others are reported to increase the spread during mid-January 2015. Among the spread reducers, four banks were able to slash the spread by more than one percentage point. Sunrise Bank topped the performance with spread reduction of 163 basis points, while Prabhu Bank's spread went further by 93 basis points to 5.0 percent. According to the figures of mid-January, 2015, Prabhu Bank had highest spread of 6.05 percent.



Stress Testing of Commercial Banks

Credit Shock

3.12 Stress test results show that there is growing risk in credit among commercial banks. Stress testing results based on data of Mid Jan 2015 obtained from 30 commercial bank revealed that a combined credit shock of 15 percent of performing loans deteriorated to substandard, 15 percent of substandard loans deteriorated to doubtful loans, 25 percent of doubtful loans deteriorated to loss loans and 5 percent of performing loans deteriorated to loss loans would push the capital adequacy ratio of 29 commercial banks below the minimum regulatory requirement of 10.0 percent. The numbers of such banks were 29 in mid-July 2014 and 28 in mid-Jan 2014.

3.13 Stress testing results under the scenario of all non-performing loans under substandard category downgraded to doubtful and all non-performing loans under doubtful category downgraded to loss underscores a pessimistic scenario as the number of banks capable of withstanding such shock without deteriorating capital adequacy to below 10 percent went down to three, down from four in mid-January 2014. Similarly, stress testing results under the scenario of 25.0 percent of performing loans of real estate and housing sector directly downgraded to substandard showed deterioration of capital adequacy of two banks to below minimum requirement of 10 percent. However, another scenario of 25.0 percent of performing loans of real estate and

housing sector directly downgraded to loss loans showed some good signs as 5 banks had failed the stress testing in mid-July 2014. The results showed that majority of commercial banks have continued to improve their resilience towards realty sector during last six months.

3.14 In an another credit shock test, under the scenario of top two large exposures (loans) were downgraded from performing to substandard category, the capital adequacy ratio of two commercial banks would fall below the required level in mid-Jan 2015 a much better improvement as compared to six in mid-July 2014 and three in mid-January 2014. Decrease in number of such banks shows they are strengthening their position by decreasing dependency on such exposures.

3.15 The overall credit shock scenario revealed that banks’ credit quality has slightly improved due to various measures taken during the review period. In this scenario if banks continue to be more watchful and vigilant then they might have a comfort zone even if there is a slight difficult situation of slowdown in recovery, downgrade of loans to loss category of NPLs and increase in provisioning.

Liquidity Shock

3.16 Results from stress tests under liquidity shock show alarming indications in terms of liquidity resilience among commercial banks. The stress test under scenario of withdrawal of customer deposits by 2, 5, 10, 10 and 10 percent for five consecutive days results showed that all banks could sustain liquidity withdrawal up to third day and on the fourth day 5 banks would fail while on 5th day only 7 out of 30 commercial banks could sustain a positive liquidity situation showing that most banks are vulnerable towards liquidity crisis.

3.17 Ten banks were prone to liquidity shock of withdrawal of 5 percent of deposits in a single day, while eighteen banks' liquidity ratio would drop below 20 percent after withdrawal of 10 percent deposit in a single day. The number of banks seeing their liquidity ratio drop below 20 percent would grew to 26 if the single day deposit withdrawal increased to 15 percent. The numbers of banks prone to liquidity shock under single day deposit withdrawal of 5, 10 or 15 percent were 2, 12 and 15 respectively on mid-January 2014 and Nil, 7 and 17 in mid July 2015. This shows that the banks are working under stressful liquidity situation in the comparison period indicating a venerable liquidity scenario.

3.18 With the shock of withdrawal of deposits by top 2, 3 or 5 institutional depositors, liquid assets to deposit ratio of 16, 20 and 28 commercial banks would be below 20.0 percent in mid-Jan 2015 and 5 banks would be short of liquid funds in case 5 institutional depositors withdrew their deposit. The numbers were 11, 15 and 20 in mid-January 2014 and 8, 11 and 18 in mid-July 2014. Only one bank was vulnerable among all commercial banks in case of deposit withdrawals from top 2, 3 or 5 individual depositors. These findings of liquidity shock show that liquidity position of commercial banks has deteriorated over the period from mid-January 2014 and mid-July 2014.

Market and Combined Credit and Market Shock

3.19 The stress testing result under market shock revealed that 28 commercial banks have maintained enough CAR to absorb the interest rate shock and maintain it above the regulatory requirement as compared to 26 in mid-July 2014. The interest rates were calibrated by changes in deposit and credit interest rates from 0.5 to 2.0 percent.

3.20 All commercial banks found to be safe from exchange rate risks as the net open position to foreign currency was lower for a majority of them. Furthermore, since commercial banks have nominal equity investments, the impact of fluctuation in equity price is near to Zero same as earlier period.

3.21 Going through market shock, 28 out of 30 commercial banks could maintain their capital adequacy ratio above the regulatory requirement of 10.0 percent.

3.22 As usual, the banks did not bear interest rate risks as they pass it directly to their clients; so, they are found to be less affected by interest rate shock as well.

3.23 The combined credit and market shocks based on a scenario of 25.0 percent of performing loan of real estate and housing sector directly downgraded to substandard category of NPLs and fall of the equity prices by 50.0 percent showed that CAR of only 2 banks would fall below 10 percent as compared to four as on mid-July 2014. Under a more adverse scenario of 15.0 percent of performing loans deteriorated to substandard, 15.0 percent of substandard loans deteriorated to doubtful loans, 25.0 percent of doubtful loans deteriorated to loss loans and the equity prices fall by 50.0 percent, the CAR of only 2 banks fell below the regulatory minimum level.

3.24 The resilience of commercial banking system of Nepal towards key stress testing scenario analyses showed a sound and strong financial system through all three kinds of credit, liquidity and market shocks.

Performance of Development Banks

3.25 Total assets and liabilities of development banks rose by Rs. 2.35 billion to Rs. 261.3 billion in mid-January 2015 from the figure of 258.9 in mid-July 2014. Likewise, the capital fund of development banks increased to Rs.29.4 billion in mid-July 2015 compared to Rs. 27.7 billion in mid-July 2014. The capital adequacy ratio of development bank was 15.4 percent in mid-January 2015 which had decreased by 40 basis points from the level in mid-July 2014. Similarly, paid-up capital of development banks rose to Rs. 25.9 billion in mid-January 2015 from Rs.25.6 billion in mid-July 2014.

3.26 During the first six months of the fiscal year, deposits in development banks grew by Rs.2.75 billion or 1.4 percent from the level in mid-July 2014 to reach Rs.202.7 billion. Credit flows from the development bank grew by 4.2 percent to Rs.168.7 billion. The ratio of credit to domestic deposit stood at 83.2 percent in mid-January 2015 which was 81.3 percent in mid-July 2014 while credit to deposits and core capital ratio stood at 71.7, well below regulatory requirement of 80. The ratio of credit to domestic deposit and core capital was 70.4 in mid-July 2014.

3.27 Loan loss provisioning of development banks stood at Rs. 6.9 billion, broadly unchanged during the period of six months to mid-January 2015. Stable non-performing loans helped to manage the provisioning at the same level as non-performing loans were also remained largely unchanged at Rs.6.7 billion from the level in mid-July 2014. In percentage terms, the ratio of NPL to total gross loan was at 4.1 percent in mid-January 2015 compared to 4.2 percent in mid-July 2014.

3.28 In terms of income, development banks recorded Rs. 11.0 billion as interest income during the six months of fiscal year 2014/15. Development Banks were able to record net profit of 2.5 billion during the review period. Annualized figures for interest income and net profit would be Rs.22.0 and 5.0 billion respectively which were Rs.22.1 billion and Rs.4.7 billion on mid-July 2014. The ROE and ROA of development banks for six months period of current fiscal were 0.9 percent and 7.3 percent, while annualized figure

would be 1.7 percent and 14.7 percent, slightly improved from the returns calculated as 14.0 and 1.4 percent respectively in mid-July 2014.

Table 3.3: Major Indicators of Development Banks (as of mid-January 2015)

Particulars	Ratios (in percent)
Capital Adequacy Ratio	15.4
Credit to Deposit (LCY) and Core Capital	72.7
Non-Performing Loan to Total Loan	4.0
Liquid Asset /Total Deposit	34.8
Return on Assets (ROA)	0.9
Return on Equity (ROE)	7.3

Base Rate

3.29 As per the circular issued by Nepal Rastra Bank in 2013, National level development banks have started to calculate and publish their base rate from mid-April, 2014. The average base rate of 20 national level development banks stood 9.9 percent in mid-January 2015, whereas it was 11.5 percent in mid-July 2014. Improvement in base rates show operating efficiency among development banks. Out of 20 national level development banks, base rate of two development banks increased from the level in mid-July 2014, while remaining others were able to reduce base rates during the six months period to mid-January 2015.

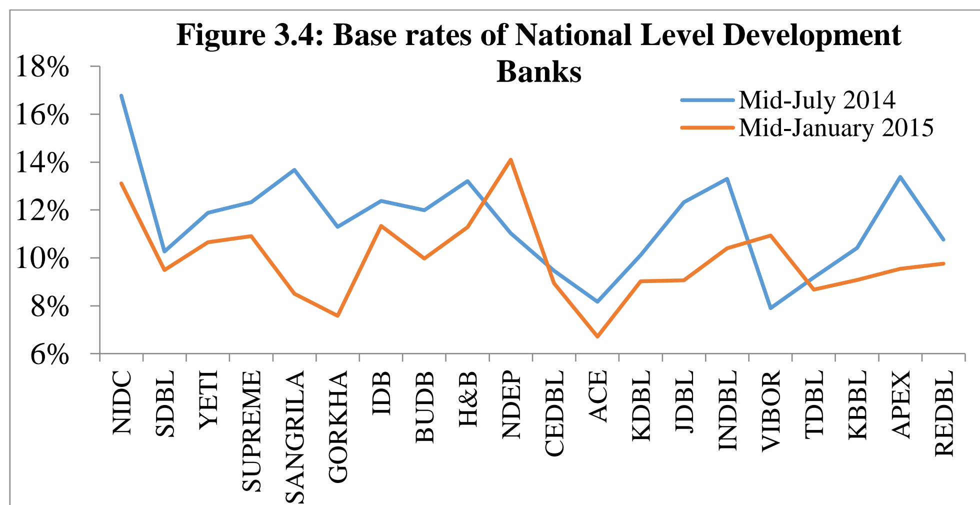


Figure 3.4: Base rates of National Level Development Banks

Spread Rate of Development Banks

3.30 Nepal Rastra Bank has issued the circular to all "A", "B" and "C" class licensed institutions regarding spread rate in 2013 to calculate and publish the spread rate from mid-January, 20145. However, Development banks have started this process only from mid-April 2014. As per the circular, it is not mandatory for the development banks to maintain spread rate. The average spread rate reported by 1, 3, 10 districts and national level development banks are presented in table 3.3. As of mid-January 2015, average interest spread of development banks rose by 78 basis points to 8.1 percent. The rise was due to increase in spreads of 3-districts level and 10-districts level development banks.

Table 3.4: Average Spread Rates of Development Banks

S.N.	Banks Level	Mid-July 2014	Mid-January 2015
1.	1- District	8.3%	8.2%
2.	3 - District	7.4%	8.1%
3.	10 - District	7.0%	7.3%
4.	National Level	6.3%	5.7%
5.	Average (all development banks)	7.3%	8.1%

Stress Testing of Development Banks

3.31 The NRB has introduced stress testing system to national level development banks from fiscal year 2012/13. Stress testing practice is used to evaluate the potential impact of specific events on a bank and the impact of such events on a set of financial variables. All the national level development banks have been advised to carry out stress testing on a quarterly basis. The development banks need to assess their soundness in the key risk areas such as credit risk, market risk, and liquidity risk. Based on the data as of mid-January 2015, the stress testing results of 20 national level development banks on various shocks have been observed as follows.

Credit Shock

3.32 The stress testing results of national level development banks as of mid-January 2015 revealed that a standard credit shock would push the capital adequacy ratio of 4 out of total 20 national level development banks below the regulatory minimum benchmark of 10 percent as per the Basel II core principle. The number of such banks was 5 in mid-July 2014 and 1 in mid-

July 2013. Stress testing is conducted based on different scenarios: deterioration of various categories of loan to substandard, doubtful and loss loans, among others. It has been found that in case of 25 percent of performing loans of real estate and housing sector is directly downgraded to loss loans, capital adequacy ratio of 1 bank will come below the required level of 10 percent. The degradation of top 5 large exposures from performing to substandard category has not significance impact on capital adequacy ratio of the banks in mid-January 2015 while capital adequacy ratio of 2 banks would come below the required level in mid-July 2014.

Liquidity Shock

3.33 Though the liquid assets to deposit ratio of whole banking system as well as the national level development banks showed an improving trend over the period, the stress test results found that only more than half of the banks may turn into a vulnerable situation in case of withdrawal of deposits by 15.0 percent or more. The number of banks that may turn illiquid after withdrawal of deposit by 2, 5, 10, 10 and 10 percent for five consecutive days has decreased to 2 in mid-January 2015 from 4 in mid-July 2014.

3.34 Similarly, if there is a withdrawal of deposit by 5.0 percent, 10.0 percent and 15.0 percent the number of bank's whose liquid assets to deposit ratio below the regulatory minimum of 20.0 percent stood at 0, 2 and 10 in mid-January 2015. The numbers of such banks were 1, 1 and 7 in mid-July 2014 and 0, 2 and 8 in mid-July 2013. With the shock on withdrawal of deposits by top 3 to 5 institutional depositors, liquid assets to deposit ratio of 2 banks' will be below 20 percent in mid-January 2015 while the number of such bank was only one in mid-July 2014. These liquidity shock show that liquidity position of national level development banks have improved in review period.

3.35 The stress testing results revealed that 18 out of the 20 national level development banks' CAR was above the regulatory requirement when calibrating through interest rate, exchange rate and equity price shocks. Similarly, since development banks are not allowed to make equity investments except in their subsidiaries, the impact of fluctuation in equity price is also lower. The banks do not bear interest rate risks as they pass it directly to their clients, so that they are found to be less affected by interest rate shock as well.

3.36 The resilience of national level development bank towards key stress tests analysis showed an improved, sound and strong financial system through from all three kinds of credit, liquidity and market shocks in stress testing analysis. The overall vulnerability test in aggregate of all 20 national level development banks found less vulnerable position except the Gurkha Development Bank which is undertaken by Nepal Rastra Bank.

Issues and Challenges

The following observations have been found in some institutions during the course of onsite inspections:

- Improper loan classification and inadequate loan loss provision
- Improper utilization or misuse of loan amount by borrower
- Loan provided to dummy projects/clients
- Weak follow-ups regarding credit utilization monitoring
- Weak corporate governance
- Lack of internal policies and its weak implementation
- Poor credit documentation
- Weak financial analysis of borrower regarding their repayment capacity
- Creation of new loan limit to repay existing loans
- Credit concentration in real estate sector (although heading is different)
- Wrong reporting of loan products
- Practices of insider lending
- Poor internal control mechanism
- Insufficient collateral backup/poor collateral and over valuation of collateral
- Lack of proper business and strategic plan
- High deposit concentration
- Related parties are not reported in same group to avoid the single obligor limit regulation

Issues/Challenges of Supervision

- Enhancing good corporate governance
- Institutional set-up and arrangements
- Lack of competent human resources
- Increasing operational risks
- Promoting self-regulation
- Practice of presenting two different audited financials for tax purpose and internal use
- Multiple banking

- Practice of loan ever greening
- High exposure on personal overdraft loans

Issues/Challenges of Development Banks:

- Low capital backup (limited capital or small capital base)
- High cost of fund
- Competition with commercial banks and other financial institutions
- Lack of qualified manpower (as most of them are regional & district level)
- Lack of qualified/experienced board members

Performance of Finance Companies

3.37 The combined balance-sheets of finance companies expanded by 1.93 percent to reach Rs.112.5 billion on mid-January 2015. Similarly, deposit collections of finance companies grew by 2.0 percent to reach Rs.74.9 billion which accounted 3.9 percent of GDP of the country. Similarly, credit flows from the finance companies decreased by Rs.149 million to Rs.65.7 which accounted 3.41 percent of GDP. Of total loan and advances, private sector accounted for more than 97 percent, followed by financial institutions, with 3.0 percent.

3.38 Capital fund of finance companies accounted to Rs. 11.3 billion in mid-January 2015, from 10.0 billion in mid-July 2014, which is roughly 16 percent of risk weighted exposure of the same period. Increase in capital fund in the review period can be attributed to bonus and right share distribution by finance companies and improvement in retained earnings in same period.

3.39 As of mid-January, credit to deposit ratio of finance companies was 87.72 percent while credit to deposit and core capital which NRB takes in account for regulatory purpose was 76.5 percent, broadly stable from its level in mid-July 2014 and below the regulatory limit of 80 percent.

3.40 Non-performing loan of finance companies went up slightly during the six months of FY 2014/15. NPLs moved further by 60 basis points from its level of 14.3 percent on mid July 2014. NPLs have been real concerns for finance companies since long. It has come down in recent year but it is still difficult to reduce NPLs below 5 percent standard. However, finance companies have maintained adequate balance for loan losses to weather the potential risk to be emanated from the high NPLs.

3.41 Finance companies remained profitable despite the sluggish growth in credit and high level of NPL. ROA and ROE of finance companies during first six

months of current FY 2014/15 were 0.55 percent and 5.28 percent, resulting to annualized figures of 1.10 percent and 10.56 percent respectively. Similarly, semi-annual profits of the finance companies stood Rs. 1.07 billion. However, the fiscal year end figure may rise further from the level in mid-July 2014 as finance companies speed up loan and interest recovery programs in latter quarters to showcase healthy fiscal end balance-sheets.

3.42 As of mid-January 2015, finance companies were seem to be comfortable with liquidity as the ratio of total liquid assets to total deposit was 38.3 percent, up from previous level of 35.8 percent in mid-July 2014. In terms of productive lending, finance companies seemed to be less interested. As of mid-January 2015, agricultural and forestry related loan and advances were mere around three percent of the total credit. On the other hand, share of construction and wholesale and retail loans and advances accounted to 16.9 and 12.6 percent respectively. Similarly, these companies floated 29.4 percent loan into uncategorized others sectors, most of them would fall into non-productive sectors.

3.43 In terms of product wise lending, the preferred sector for finance companies was demand and working capital loan. As of mid-January 2015, finance companies disbursed 19.8 percent or around Rs.13 billion under this heading, followed by real state (13.7 percent) and term loans (10.14 percent). As of mid-January, finance company lent Rs.2.2 billion (3.33 percent of total credit) to the deprived sector; falling short of mandatory level of 3.5 percent in aggregate. That shows finance companies failed to flow credit at required level on deprived sector lending. Majority of the loans from finance company were uncategorized and labeled as others that accounted roughly 20 percent of total credit.

3.44 Number of finance companies has decreased to 51 in mid-January 2015 from 54 in mid-July 2014. The reduction was due to merger of these companies with other banks. As of mid-January 2015, there are seven finance companies being labeled as problematic and another one is under prompt corrective action.

3.45 There are different types of financial institutions in Nepalese financial system and most of these institutions are competing for closely competitive product and services. Similarly, involvement of non-banking intuitions, like credit cooperatives in same type of product and services have added further

pressure on finance companies. In such adverse market condition, most of the finance companies are squeezed between the option of lowering the cost of fund or merge with financial institutions with strong capital base.

Table 3.5: Overview of Finance Companies (As of mid-January 015)

S.N.	Indicators	Figures
3.1	Numbers of Finance Companies	51
3.2	Numbers of Branches	239
3.3	Numbers of ATM	30
3.4	Numbers of Debit Card	23740
3.5	Numbers of Credit Card	0
3.6	Numbers of Deposit Accounts	610158
3.7	Numbers of Loan	50195

Performance of Micro Finance Development Banks (MFDBs)

3.46 As of mid-January 2015, there were altogether 35 micro finance development banks (MFDBs) operating as "D" class financial institutions. They consist of one Grameen Bikas Bank namely Nepal Grameen Bikas Bank Limited, 30 private sector micro finance development banks replicating the 'Grameen Banking Model' and 4 wholesale lending micro finance institutions (MFDBs). The number of branches of MFDBs reached 998, creating employment for 5184 persons as of mid-January 2015. Out of these, the wholesale MFDBs are operating 10 branches with the 95 staffs. Likewise, Nepal Grameen Bikas Banks Limited (NGBBL) has 170 branches in 65 districts operating with 912 employees. As of mid-January 2015, total members of MFDBs were 13,89,625, after falling by 6.5 percent from the number in mid-July 2014 . Out of total members, NGBBL has 1,90,946 (13.7 percent) members in its portfolio. The total loan disbursed by the MFDBs as of mid-January 2015 accounted to Rs.230.2 billion. Out of the total loan, wholesale MFDBs disbursed Rs. 37.9 billion and NGBBL disbursed Rs. 44.5 billion during the review period.

Table 3.6: Major Indicators of MFDBs

S. N.	Particulars	(Rs. '000)	
		Mid-July 2014	**Mid-January 2015**
1.	No. of MFDBs	35	35
1.2	*No. of Wholesale MFDBs*	*4*	*4*
2.	No. of Branches of MFDBs	776	998
2.1	*No. of Wholesale MFDBs*	*10*	*10*
2.2	*No. of Branches of GBB*	*170*	*178*
3.	Total Members of MFDBs	1486128	1389625
3.1	*Members of GBB*	*190134*	*190946*
4.	Total Capital of MFDBs (Rs.)	4749569.45	5526931.75
4.1	*Capital of Wholesale MFDBs (Rs.)*	*2454011.24*	*2676986.22*
4.2	*Capital of GBB (Rs.)*	*546155.01*	*5162.21*
5.	Total Paid-up Capital of MFDBs (Rs.)	2768875.95	3425427.25
5.1	*Paid-up Capital of Wholesale MFDBs (Rs.)*	*910000.00*	*910682.30*
5.2	*Paid-up Capital of GBB (Rs.)*	*407067.00*	*557500.00*
6.	Total Assets of MFDBs (Rs.)	42339035.34	58388907.08
6.1	*Assets of Wholesale MFDBs (Rs.)*	*12019564.00*	*14879334.21*
6.2	*Assets of GBB (Rs.)*	*5664041.86*	*6229910.08*
7.	**Total Loan and Advances of MFDBs (Rs.)**	**28211900.17**	**44174843.30**
7.1	*Loans and Advances of Wholesale MFDBs (Rs.)*	*7269095.58*	*11844388.16*
7.2	*Loan and Advances of GBB (Rs.)*	*3578170.86*	*4408511.14*
8.	**Total Deposit of MFDBs (Rs.)**	**9140449.95**	**13119571.50**
8.1	*Deposit of GBB (Rs.)*	*1099190.00*	*1284890.01*
9.	Total Overdue (Loan & Interest) of MFDBs (Rs.)	913957.15	951657.23
9.1	*Overdue (Loan & Interest) of Wholesale MFDBs (Rs.)*	*11145.00*	*6160.00*
9.1	*Overdue (Loan & Interest) of GBB (Rs.)*	*754301.00*	*755389.00*

3.47 As of mid-January 2015, total capital of MFDBs increased by 16.4 percent from the level in mid-July 2014 to reach Rs. 5.5 billion. Out of total capital fund, capital fund of wholesale MFDBs stood at Rs. 2.7 billion while NGBBL's capital fund stood at Rs. 5.2 million. The paid-up capital of MFDBs increased by 23.7 percent to Rs.3.4 billion. The ratio of paid-up

capital to total capital stood at 61.9 percent. The paid-up capital of wholesale MFDBs stood at Rs. Rs. 910.7 million while NGBBL's paid-up capital stood at Rs. 557.5 million. Based on risk-weighted asset, MFDBs are required to maintain at least 4.0 percent as core capital and 8.0 percent as the capital fund.

3.48 Total asset of MFDBs in the review period rose by 37.9 percent to Rs. 58.4 billion. In this category, the share of wholesale MFDBs stood at 25.5 percent and NGBBL's asset share stood at 10.7 percent. Out of the total assets, loan and advances registered a growth of 56.6 percent to Rs. 44.2 billion during the six months to mid-July 2015. Out of the total loans and advances; the wholesale loan shared 26.8 percent while individual loans shared remaining part. NGBBL's share in this category stood at 9.9 percent. The ratio of loan and advances to the total assets stood at 75.6 percent. MFDBs have not booked any asset as non-banking assets during the review period. Likewise, investment of these banks during the review period reduced by 25.6 percent to Rs. 2.4 billion. In this category, the share of GBBs stood at 9.2 percent. Out of total investment, the ratio of investment in government and NRB securities stood at 4.8 percent.

3.49 Total saving of deposit mobilization of MFDBs grew by 43.5 percent to Rs. 13.1 billion during first six months of FY 2014/15. Out of the total deposit, NGBBL's mobilized Rs.1.3 billion sharing 9.8 percent stake. As compared to total liabilities of these institutions, the share of deposit mobilization remained at 22.5 percent. Out of total deposits, compulsory deposits shared 39.0 percent. Total borrowing of these banks during the review period increased by 35.3 percent to Rs. 31.8 billion. NGBB borrowed Rs. 3.6 billion contributing 11.5 percent in total borrowing. As compared to total liabilities of MFDBs, the share of borrowed amount remained at 54.4 percent.

3.50 The total amount of overdue loan including interest of these institutions decreased by 4.1 percent to Rs. 951.7 million as compared to figure in mid-July 2014. The overdue of wholesale MFDBSs stood at 6.2 million. NGBBL's overdue loan was Rs.755.4 million with a significant share of 79.4 percent of total overdue of MFDBs. The number of borrower with overdue loan in MFDBs has also decreased by 11.6 percent to 34,168 persons during the review period. Out of this, the number of overdue loanees of NGBBL share 70.9 percent. Likewise, the amount of loan loss provision of these

institutions increased by 21.1 percent to Rs. 912.1 million during the review period. NGBBL had loan loss provision of Rs. 278.8 million with a share of 30.6 percent.

Issues and Challenges in Microfinance

3.51 Although the rapidly expanding micro finance sector is being widely accepted as an effective tool of enhancing access to finance, reducing poverty, empowering women and uplifting the living standards of the poor and under-privileged groups; their concentration mostly in urban and accessible areas accompanied with multiple financing and duplication in some cases, duplication even among the donors in other cases, comparatively higher interest rates being charged with the poorest section of the society, deviation from the social responsibility in many cases and more concentration of the loan on the middle and upper middle class rather than the deprived sector are some of the major weaknesses witnessed in this sector, which need to be addressed. Arrangements should be made to accommodate the credit information of MFIs by the Credit Information Bureau so that problem of multiple financing and duplication is addressed properly.

3.52 Increasing trend of shadow banking practices by some of the larger cooperatives around the urban areas has posed more challenges to the Nepalese financial system. This kind of activities conducted by the cooperatives could also increase risk in the system as their deposit mobilization is rapidly increasing. Lack of stringent regulatory and supervisory mechanism for various types of micro finance institutions established and operated under different Acts is also emerging as another challenging issue. Saving and credit activities of larger cooperatives in urban areas should be monitored on a regular basis. There is a need of an strong and separate regulatory body (II Tier Institution) to ensure the compliance of minimum financial standards by the larger cooperatives operating in urban and accessible areas.

3.53 Financial viability is necessary for the long run sustainability of MFIs. They are generally resource deficient. The capital base of most of the MFIs is comparatively small as compared to other BFIs. As MFIs generally borrow fund from BFIs, the price they charge for their financial services is relatively high. At the same time MFIs mostly engage in small-sized business transactions with relatively higher overhead cost. As the interest rate in

conventional banking system increases, it further pushes up the interest rate of MFIs, making micro finance services more costly to the poor and needy people. This is another major challenging issue of this sector which needs to be addressed by an effective policy response.

3.54 Code of conducts and good governance practices guidelines are necessary for developing professionalism, healthy competition and uniform practices in micro finance sector.

3.55 Some policy incentives to encourage MFIs to invest in the productive sectors particularly in the remote and inaccessible areas are also felt necessary. Besides, legal framework regarding the client protection, a separate mechanism for credit information sharing, and a kind of institutional arrangement for the capacity enhancement of the employees working with the MFIs are some other important issues that need to be addressed. All these measures may enhance the activities of the MFIs in a more productive and effective way in the rural credit sector and there by rural financing effort.

CHAPTER – FOUR
COOPERATIVES, FINGOS AND OTHER FINANCIAL INSTITUTIONS

Cooperatives

NRB Licensed Cooperatives

4.1 The number of cooperatives permitted for conducting limited-banking activities by the NRB is 16 as of mid-January 2015. Out of these cooperatives, National Cooperative Development Bank (NCDB) is involved in the wholesale lending activities while remaining cooperatives are involved in retail businesses. The total asset of these 16 cooperative institutions increased by 22.3 percent to Rs.21.0 billion during the review period. Total capital of these institutions increased by 19.2 percent to Rs. 2.1 billion during the review period. Out of the total capital fund, the share capital covers 71.1 percent.

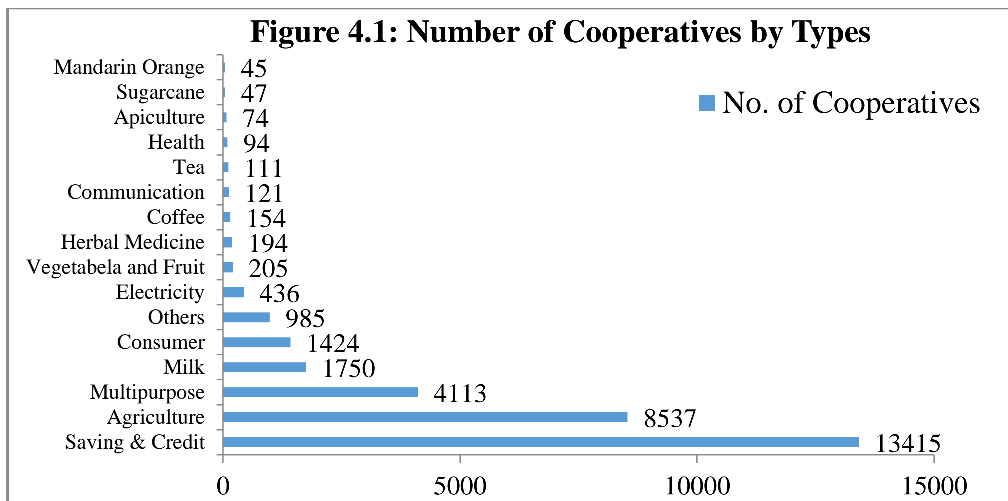
4.2 Similarly, total deposit of these 16 cooperatives increased by 22.5 percent to Rs. 15.4 billion during the review period. Likewise, their loans and advances rose by 16.1 percent to Rs. 12.4 billion. Similarly, the total investment of these cooperatives increased by 33.4 percent to Rs. 1.7 billion during the review period. Of this total investment, 17.7 percent was fixed deposits and rest of the amounts was invested on other instruments like government bonds, share and debenture etc.

GON Registered Cooperatives

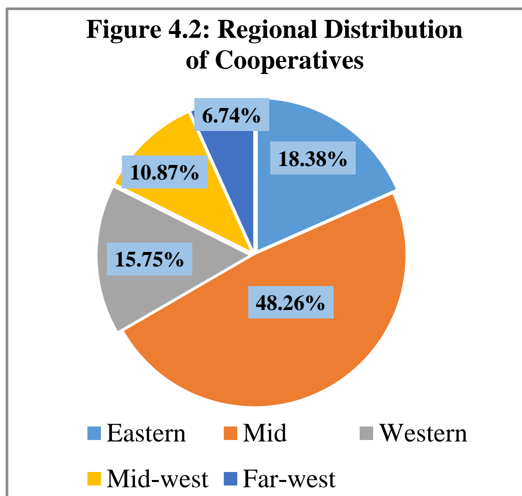
4.3 Cooperatives are considered as an important pillar of the economy due to their significant contribution in rural economies of the country. Cooperative sector has been providing direct employment to 55,994 people as staffs, while indirect employments through micro-entrepreneurship remain unaccounted. On financial front, cooperatives account for around 10 percent of total deposit of NRB regulated financial institutions, while they share same percentage of total loans and advances.

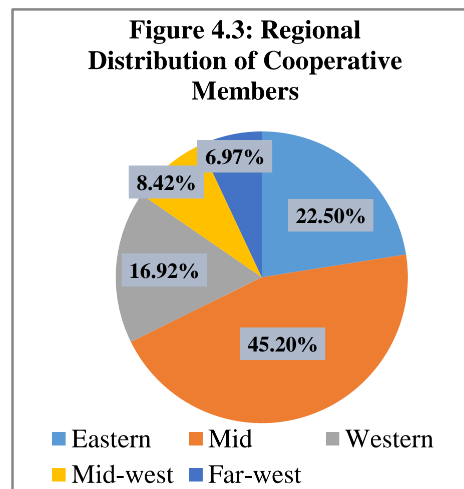
Cooperative Penetration

4.4 Information from Department of Cooperative reveals that, 31,705 cooperatives are operating throughout the country till mid-January 2015. Of the total numbers, savings and credit cooperatives account for 42.3 percentages.



4.5 The regional distribution of cooperatives shows that cooperatives have flourished in Central Development Region while they are yet to make significant presence in Mid-west and Far-west Development Region.





Financial Activities of Cooperatives

4.6 As of mid-January 2015, deposits of cooperatives totaled to Rs.176.1 billion whereas total credit flow stood at Rs.160.3 billion. Deposits at cooperatives grew by 2.1 percent over six months to mid-Jan 2015 while credits on the same period grew by 3.8 percent. Total capital of cooperatives stood at Rs.63.1 billion and different funds of cooperatives were accounted to Rs.6.50 billion.

Table 4.1: Key Figures of Cooperatives (As of Mid-January 2015)

Indicators	Figures
No. of Cooperatives	31,705
Members	4,786,201
Male	*2,566,041*
Female	*2,223,871*
Total Employment	55,994
Total Capital (in Rs.)	63,090,534,000
Total Fund (in Rs.)	6,493,943,000
Deposit (in Rs.)	176,122,676,000
Credit (in Rs.)	160,298,299,000
Other Investment (in Rs.)	347,162,000
Credit to Deposit Ratio	91.0%
Credit to Capital and Deposit Ratio	67.0%

Financial Non-Government Organizations

4.7 NRB has been gradually depleting the numbers of Financial Intermediary Non-Government Organizations (FINGOs) by allowing these institutions to transform as microfinance development banks. This step has been taken to better the regulatory practices in FINGOs and allow them to expand their horizon for expanding and deepening financial assess. Deadline for this transformation has been set for mid-July 2015.

4.8 As of mid-January 2015, there were altogether 27 Financial NGOs (FINGOs) with their 288 branches operating throughout the country. In the previous year, there were 30 FINGOs operating with their 282 branches. Since all the FINGOs have been requested by the NRB to transform themselves into 'D' class MFDBs within a stipulated time frame, their number is gradually decreasing annually. The FINGOs registered under the Institutions Registration Act, 1977 and are carrying out microfinance activities permitted by the NRB in accordance with the provision of the Financial Intermediary Act, 1999. The number of members of such institutions as of mid-January 2015 has been increased by 9.3 percent to 5,13,025. As of the review period, the outstanding loan of these institutions increased by 113.3 percent to Rs.

9.16 billion. Likewise, total deposits of these institutions increased by 77.7 percent to Rs. 4.34 billion.

Rural Self-Reliance Fund (RSRF)

4.9 The Rural Self Reliance Fund (RSRF) was instituted in 1991 with the joint efforts of NRB and the Government of Nepal. The objectives of the Fund is to work for gradual poverty reduction by providing wholesale credit to those cooperatives and the NGOs which are involved in providing lending needs of the poor section of the people at subsidized rate of interest. The total capital of the Fund of as of mid-January 2015 reached Rs. 793.4 million with Rs. 540.0 million contributed by the government and Rs. 253.4 million by the central bank. The loan limit per individual borrower has been set at Rs. 90 thousand. As of mid-January 2015, total loan of Rs. 1.6 billion has been disbursed through this Fund to 988 institutions throughout 68 districts benefitting 48 thousand deprived-households. The recovery rate of the fund was more than 94 percent during the review period.

Insurance

4.10 The insurance sector comprises of 26 companies – 17 non-life and 9 life insurance companies. According to the data received from Insurance Board of Nepal, total assets/liabilities of insurance companies rose by 8.92 percent to Rs.110.10 billion during six months to mid-January 2015. However, the growth was slower for no-life companies at 6.29 percent whereas life insurance companies' assets grew by 9.53 percent.

Table 4.2: Sources and Uses of Funds of Insurance Companies (in billion Rs.)

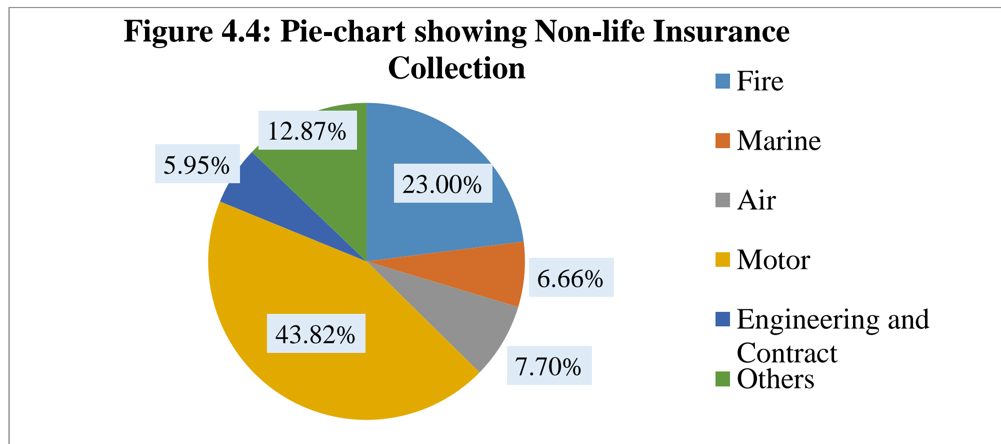
Sources	Life			Non-Life		
	2012/13	2013/14	2014/15*	2012/13	2013/14	2014/15*
Paid-up Capital	2.79	4.66	4.67	1.80	3.17	3.54
Reserve Funds	57.07	71.08	78.33	8.85	8.23	8.94
Other Liabilities	4.99	6.26	6.82	5.67	7.69	7.80
Total	64.85	82.01	89.82	16.33	19.08	20.28
Uses						
Cash and Bank	1.77	2.78	2.90	1.45	1.33	1.40
Investment	57.11	70.97	77.36	9.89	12.11	13.03
Fixed Assets	1.44	1.42	1.54	1.11	1.06	1.15
Other Assets	4.50	6.83	8.02	3.88	4.59	4.70
Total	64.82	82.01	89.82	16.33	19.09	20.28

** Data up to mid-January 2015*

4.11 The premium collections of insurance companies stood at Rs. 16.6 billions, registering a growth of 8.6 percent during first six-months of FY 2014/15. Out of the total premium collection, Life Insurance companies' premium accounted to 66.7 percent amounting Rs.11.1 billion whereas share of non-life insurance companies have 33.3 percent amounting Rs.5.5 billion.

4.12 The insurance coverage is very low in Nepal. As of mid-January, life insurance companies have a total of 3,953,172 effective policies. Similarly, non-life insurance companies have been able to sale 498,254 policies. Motor Insurance topped the chart among five major types of non-life insurance products, while Engineering and Contracts is at the bottom.

Figure 4.4: Pie-chart showing Non-life Insurance Collection



Employees Provident Fund

4.13 Employees Provident Fund (EPF) is one of the major contractual saving organizations of Nepalese financial system. According to unaudited figures till mid-March 2015, it has total provident fund of Rs. 179.4billion, while total assets/liabilities of EPF stood at Rs. 186.3 billion. The fund of the EPF grew by 9.58 percent compared to the fund collected till mid-July 2014. The savings in EPF equals around 9 percent of total deposits of NRB regulated BFIs while total assets of EPF weights equal to 7 percent of total assets held by NRB regulated BFIs. Reserves at EPF stood at Rs.4.9 billion.

4.14 With a portfolio of Rs.179 billion, EPF has been working as a major supplier of long term loans to hydel projects. Similarly, it has been providing loan support to government owned Nepal Oil Corporation. As of mid-March 2015, its loan and investment portfolio comprised of share investment, project loans, lending to contributors, fixed deposits at financial institutions and

government bonds and debentures. Within these, contributors lending accounts 56.7 percentage share and fixed deposits accounts second with 18.2 percentage share in the portfolio. The fund has been utilizing almost its total fund with loan and investment to total fund ratio at 96 percent and maintaining cash and bank balance of Rs. 5 billions.

Figure 4.5: Lending and Investments Portfolio of EPF

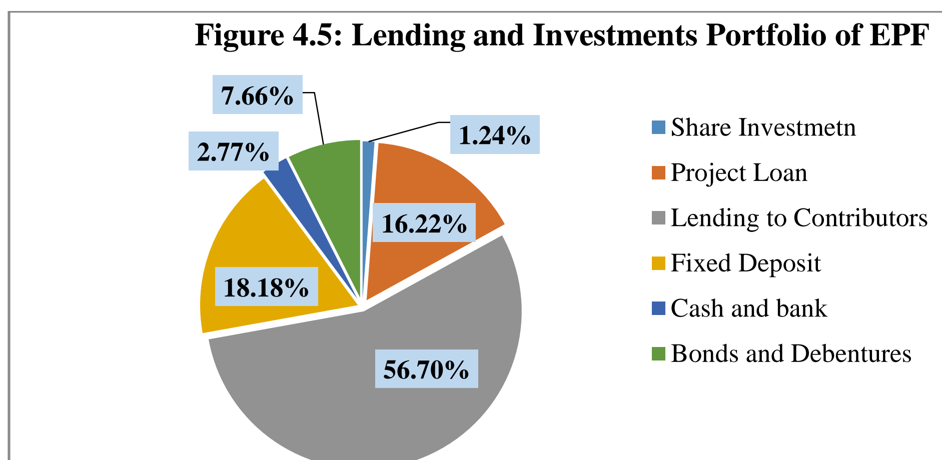


Table 4.3: Key Indicators of EPF

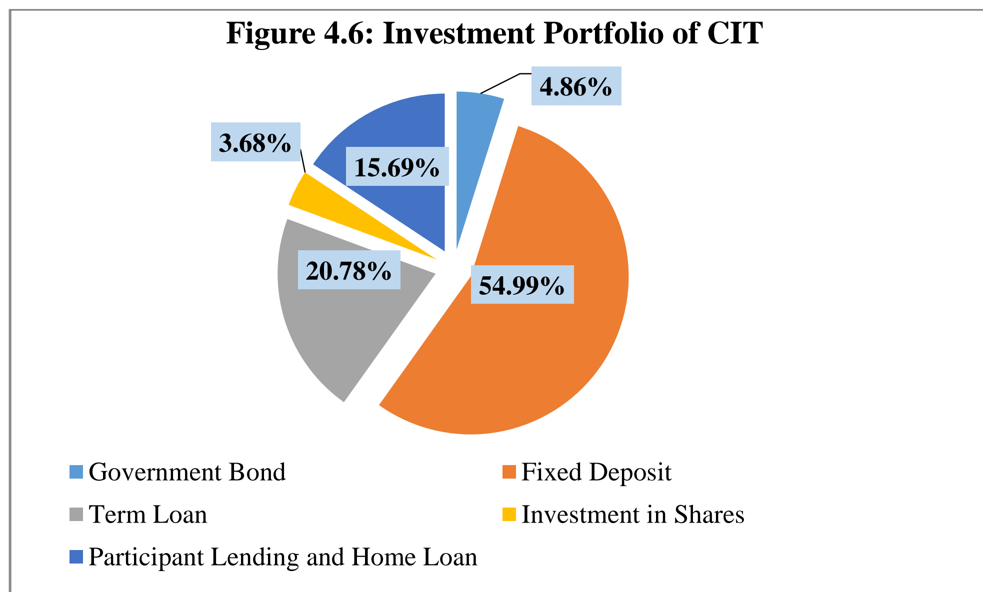
Indicators	Amount (Rs.)
Sources of Fund	**186,301,803,000**
Provident Fund	179,386,032,000
General Reserve and Funds	4,858,373,000
Liabilities	737,325,000
Provisions	1,320,073,000
Uses of Fund	**186,301,803,000**
Cash and bank	4,948,883,000
Bonds and Debentures	13,699,880,000
Fixed Deposits	32,490,000,000
Share Investments	2,220,531,000
Project Loan	28,988,000,000
Lending to Contributors	101,345,854,000
Investment in Fixed Assets	819,457,000
Fixed Assets	306,785,000
Assets under construction	2,168,000
Miscellaneous Assets	1,480,245,000
Loan and Investment to Total Fund Ratio	**95.9%**
Loan and Investment to Provident Fund Ratio	**92.5%**
Liquidity Ratio (Cash and bank to Total Fund)	**2.7%**

4.15 EPF holds significant chunk of fund available in the financial system through its contributors but lacks proper regulatory authority. Furthermore, fixed deposits in the BFI have been one of the major sectors for funds deployment. The figures of mid-March 2015 shows that it has fixed deposit worth Rs.32.5 billion, which gives it prowess to influence market interest rates.

Citizen Investment Trust

4.16 As of mid-January 2015, net fund collections at Citizen Investment Trust (CIT) stood at Rs.58.44 billion, recording a growth of 12.81 percent over the six month period from mid-July 2014. Fund collection of CIT equals to 2 percent of total deposits collected by NRB regulated BIFs. Apart from its capital of Rs.450 million, regular contributions from members are the only and major source of fund for CIT. Investments of the Trust, which are diversified in five broad categories, stood at Rs.50.80 billion.

Figure 4.6: Investment Portfolio of CIT



4.17 Figure 4.6 shows that the investment of CIT is highly concentrated on fixed deposits in BFIs making the earnings highly dependent on interest rates of BFIs. Being a contractual savings institution, it could have reduced its high dependency on fixed deposit. With fixed deposits of Rs.27.9 billion, it has some market power to influence the market interest rate which can pose threat to overall financial stability. Since the trust has huge fund that can be invested in long term projects, it could increase the investment in long-term projects such as hydel generation. It will not only help CIT to decrease over-

concentration but also substantially increase income by investing the fund in long term assets.

Table 4.4: Key Indicators of CIT

Indicators	Figures
Share Capital (Rs.)	**450,000,000**
Net Fund Balance (Rs.)	**58,435,300,000**
Investment (Rs.)	**50,797,400,000**
Government Bond (Rs.)	2,470,400,000
Fixed Deposit (Rs.)	27,935,000,000
Term Loan (Rs.)	10,553,300,000
Investment in Shares (Rs.)	1,870,200,000
Participant Lending and Home Loan (Rs.)	7,968,500,000
Fund to Investment Ratio	**86.93%**
Return on Investment	**8.03%**

CHAPTER - FIVE

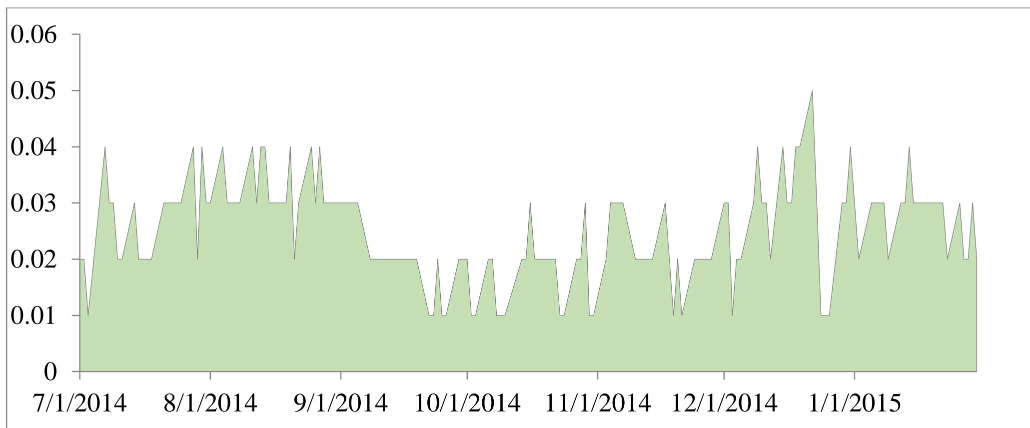
FINANCIAL MARKETS

Global Financial Market Perspectives

US Treasury Bills

5.1 While ECB entered into bond buying spree and Federal Reserve maintained its moratoriam in rate hike, low interest rates continued to help households and businesses finance new spending and help support the prices of many other assets, such as stocks and houses during the review period. Keeping with the momentum and to support continued progress toward maximum employment and price stability, the Federal Reserve Open Market Committee has remained reluctant for upward revision of federal funds rates from long standing 0 to 0.25 percent target range. As a result, 3-month Treasury bill secondary market rate on discount basis remained highly volatile within the band of 0.01 percent to 0.05 percent range during the review period.

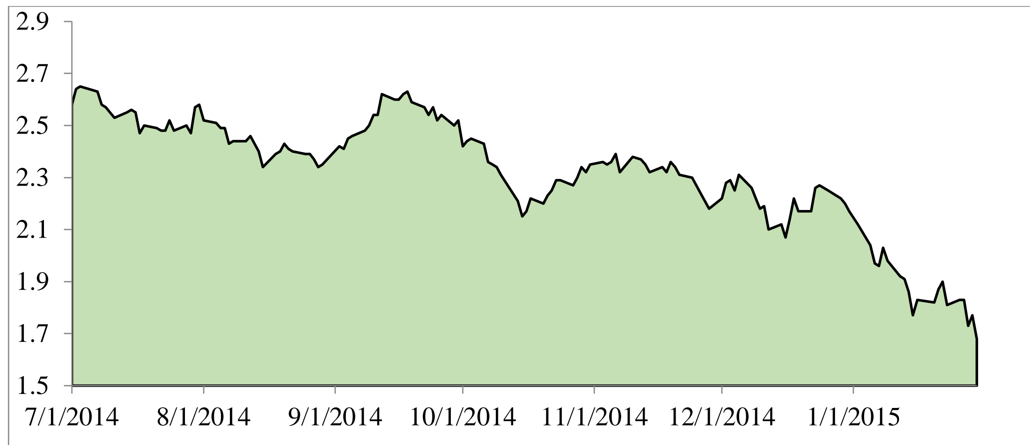
Figure 5.1: Three-Month US Treasury Bills Monthly Average Interest Rate (in percent)



Source: Federal Reserve

5.2 The interest rate on long term US Treasuries has been in decreasing trend albeit high volatile momentum during the review period. As of end of January 2015, long term government bonds were trading for interest rate of 1.68 percent, down from the reading of 2.65 on July 2014.

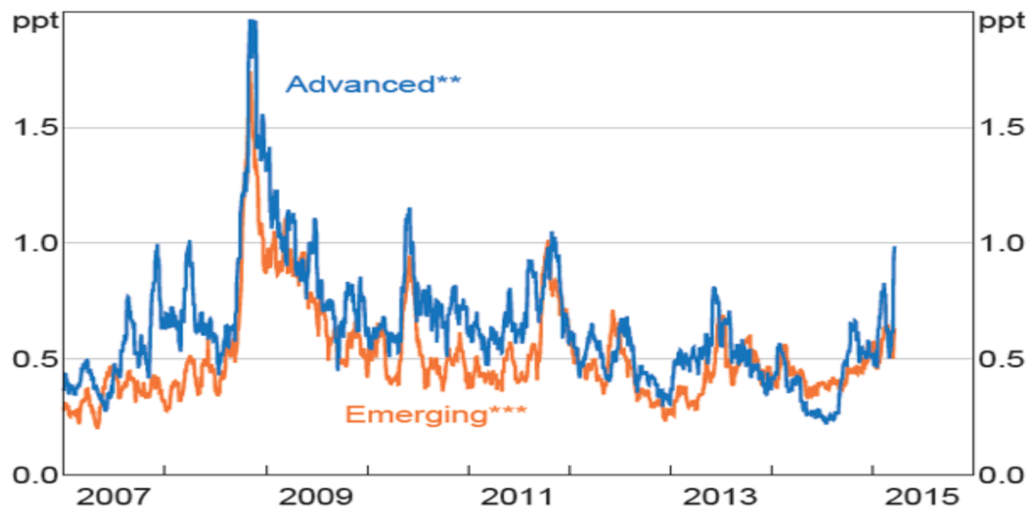
Figure 5.2: Ten-Year US Treasury Constant Maturities Monthly Average Interest Rates (in percent)



Exchange Rate Volatility

5.3 Exchange rate has remained volatile since the recovery in US economy while US dollar remaining strong against most of the major currencies. Much of the recent pick-up in currency market volatility from low levels (Graph 5.3) has been associated with divergent macroeconomic developments and hence diverging monetary policy outlooks in the major advanced economies. The ongoing economic recovery in the United States has contrasted with more modest economic growth and lower inflation expectations in the euro area and Japan. The Federal Reserve ended its bond purchasing program in October 2014 and financial markets assign a high probability to the Federal Reserve raising rates later this year, whereas during the past six months the ECB and the Bank of Japan have increased monetary policy stimulus through balance sheet expansion.

Figure 5.3: Exchange Rate Volatility
(Rolling 22-day standard deviations of daily percentage changes*)



* Median of Bilateral exchange rates against the US Dollar
** Australia, Canada, Euro area, Japan, New Zeeland, Switzerland and United Kingdom
***Brazil, Chile, Colombia, India, Indonesia, Malaysia, Mexico, Philippines, Russia, South Africa, South Africa, Taiwan, Thailand and Turkey
Source: Bloomberg

Dollar Index

5.4 Dollar Index consists of a geometric weighted average of a basket of six major foreign currencies – Euro 57.6 percent, Japanese yen 13.6 percent, Pound sterling 11.9 percent, Canadian dollar 9.1 percent, Swedish kroner 4.2 percent and Swiss franc 3.6 percent weight – against the dollar. The index is calculated by factoring in the exchange rates of these currencies.

5.5 The US dollar index appreciated from 79.8 in beginning of July 2014 to 94.8 at end of January 2015. The whopping surge in the value of index was result of combination of economic strengthening in the United States and relatively poor performance of Japan and Euro zone.

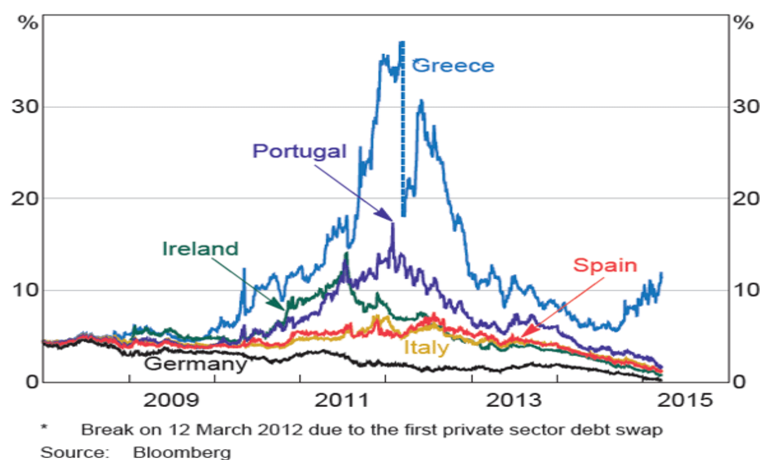
Figure 5.4: US Dollar Index Daily Movement

Source: barcharts.com

Euro Area Bond Yield

5.6 Bond yield for debt-ridden Euro Zone economies have been volatile. However, bond yields for Portugal, Ireland, Spain and Italy are mowing downwards in recent time. Contagion from Greece to other vulnerable euro area financial systems have so far been limited (Graph 1.4). In contrast to the situation in 2011, holdings of Greek sovereign debt are now more concentrated in the official sector, European banks have made progress with balance sheet repair and there have been further advances in the European framework for bank regulation. Bond prices in other periphery countries have also been supported by the announcement of additional policy stimulus by the ECB.

Figure 5.5: Euro area 10-year Bond Yields (in percentage)



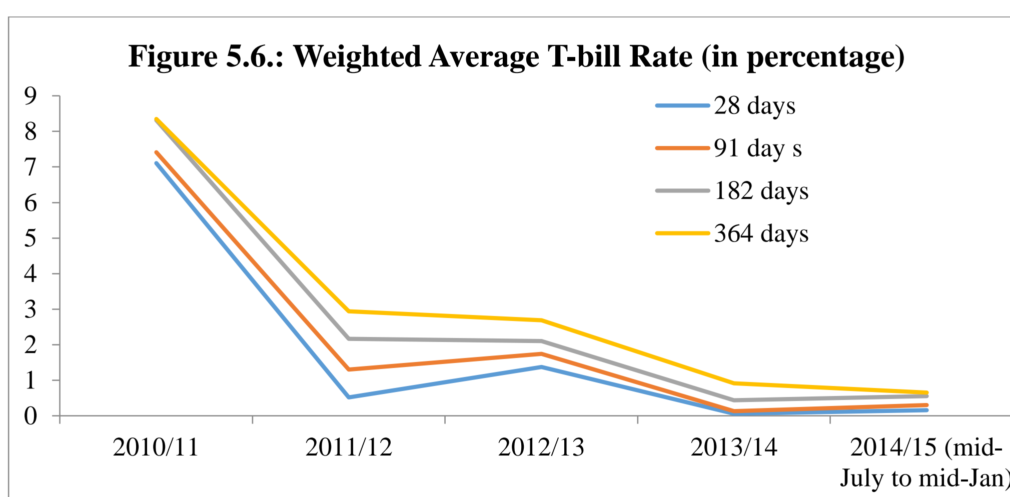
Domestic Financial Market

Money Market

Treasury Bills

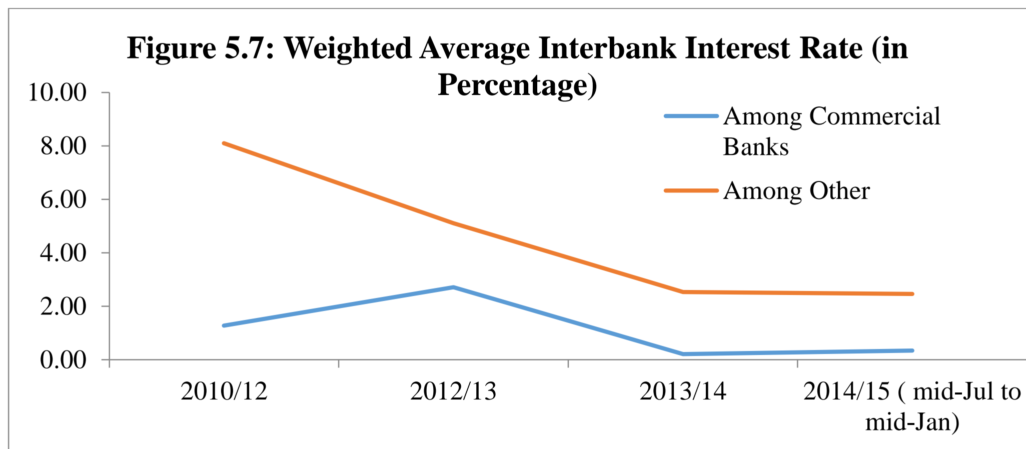
5.7 Weighted average of 91-days Treasury bill rates and inter-bank transaction rates have marginally decreased during the sixth month of 2014/15 compared to a year ago. The weighted average 91-day Treasury bill rate decreased to 0.15 percent in mid January 2015 from 0.47 percent a year ago. Other T-bills having different maturity also fared same in the money market adhering to the trend of 91-days bill.

Figure 5.6.: Weighted Average T-bill Rate (in percentage)



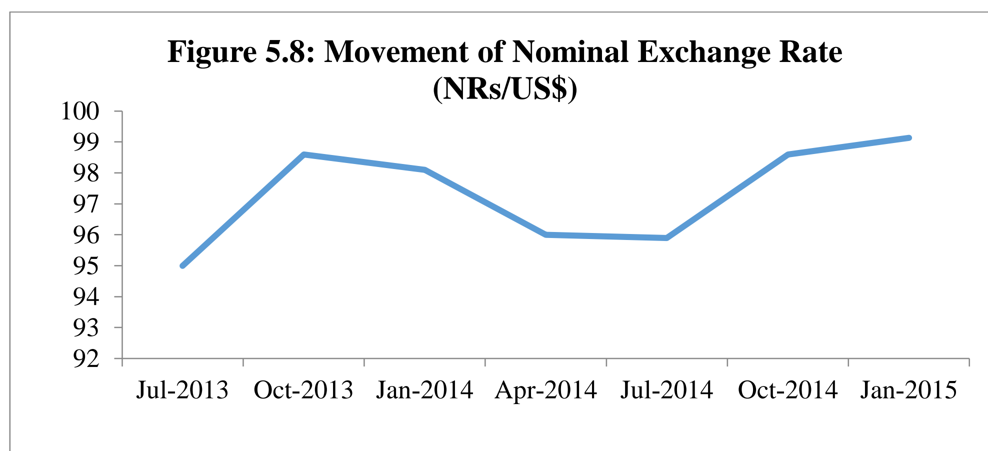
Interbank Rates

5.8 The interbank rates were seen almost stable during the last six-month period of current fiscal year. However, average inter-bank transaction rate among commercial banks remained at 0.15 percent in mid January 2015 down from 0.21 percent a year ago. Following the trend from past years, weighted average inter-bank rate among other financial institutions remained significantly higher than the rate among commercial banks. It was also stable during the first six months to the FY. However, it fell slightly to reach 2.51 percent in mid-January 2015 from 2.62 percent a year ago in mid-January 2014.



Exchange Rate

5.9 Nepalese currency depreciated by 3.3 percent against US dollar during the first six months of 2014/15 compared to depreciation by 3.2 percent in the same period of the previous year. The depreciation of Nepalese rupee against US dollar contributed to improve export competitiveness, stimulated remittance inflows. However, it increased net domestic assets and money supply, inflationary pressure and uncertainty in the external sector. It inflated the foreign debt liability of the government.



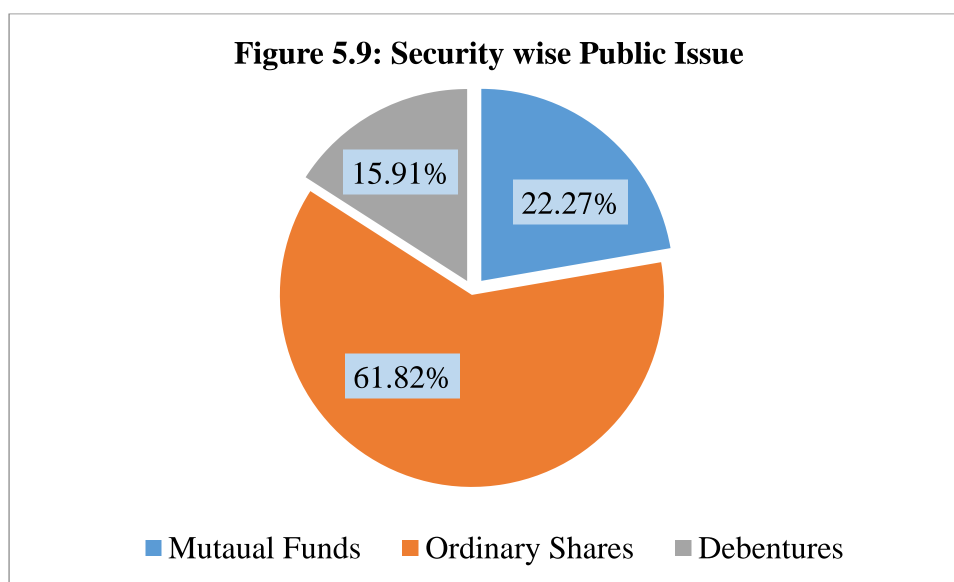
Securities Market

Public Offerings

5.10 During the first six-months of the fiscal year 2014-15, SEBON approved public offerings for nine companies amounting Rs. 6.3 billion. These offerings comprised of ordinary shares (5), debentures (2) and mutual funds

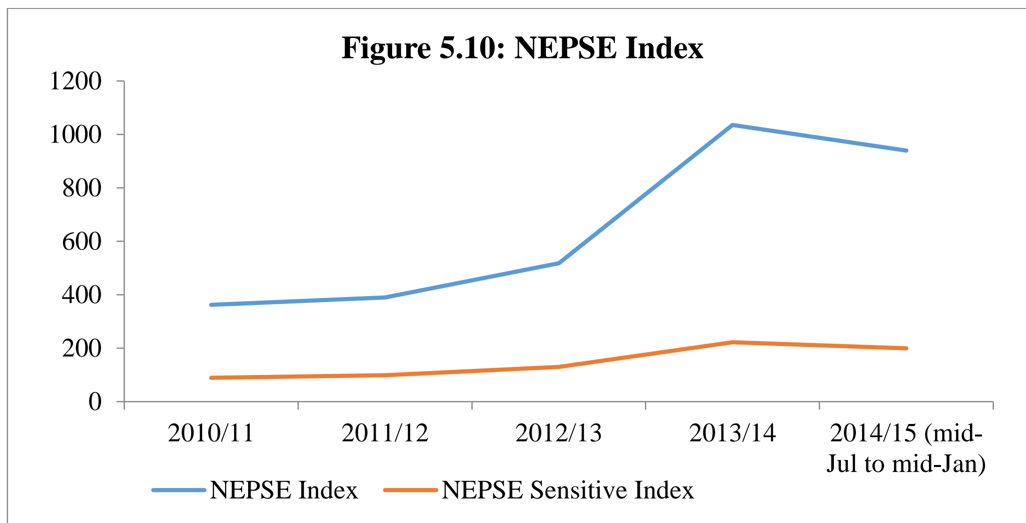
(2). Among those issues, Upper Tamakoshi Hydropower Company Limiter has the biggest one amounting Rs. 3.6 billion, more than half of total issue amount. The public issue of Upper Tamakoshi is biggest ever in the Nepalese capital market.

Figure 5.9: Security wise Public Issue



Secondary Market

5.11 NEPSE index rose by 19.4 percent to 939.5 points in mid-January 2015 on y-o-y basis. The index had increased by 48.6 percent in the corresponding period of the previous year and stood at 787.7 points in mid-January 2014. The y-o-y stock market capitalization increased by 20.5 percent to Rs. 963.4 billion in mid- January 2015. The ratio of market capitalization to GDP stood at 50.0 percent in mid-January 2015 compared to 47.2 percent a year ago. Of the total market capitalization as of mid-January 2015, the share of banks and financial institutions (including insurance companies) stood at 77.5 percent while that of manufacturing and processing companies, hotels, business entities, hydropower and other sectors stood at 2.5 percent, 2.8 percent, 0.1 percent, 7.3 percent and 9.7 percent respectively.



5.12 Total number of companies listed at the NEPSE decreased from 235 in mid-January 2014 to 232 in mid-January 2015. Of the total listed companies the number of banks and financial institutions (including insurance companies) stood at 198 followed by production and processing industries (18), hotels (4), business entities (4), hydropower (6) and other companies (2).Total paid-up capital of the listed companies stood at Rs. 159.2 billion in mid-January 2015, registering an increase of 16.4 percent over mid-January 2014. Additional securities worth Rs. 12.64 billion comprising ordinary share of Rs. 9.0 billion, right share of Rs. 0.87 billion and bonus share of Rs. 2.8 billion have been listed in NEPSE during the six months of 2014/15.

CHAPTER - SIX

FINANCIAL SECTOR POLICIES AND INFRASTRUCTURES

Regulatory Developments

Regulation to Promote Agriculture Sector

6.1 Nepal Rastra bank issued a circular to promote credit of BFIs in agriculture sector. The circular comprehends government strategy to promote agriculture as a business among youth. In order to attract rural youths towards agriculture, the government in its budget had announced a subsidy of four percent on interests charged by BFIs for agriculture credit. NRB issued working procedure for agricultural credits which was prepared of Ministry of Finance. According to the policy, youths aged between 21 to 45 years are eligible to get agricultural loans from Banks and Financial institutions.

6.2 According to the working procedure, an individual can avail the facility on loans up to Rs 10 million. The working procedure, which came into effect immediately, has identified 12 priority areas eligible for the facility. The areas include vegetable production, processing and storage; seed production, processing and storage; floriculture; livestock; fruits production, processing and storage; and dairy production, processing and sales. Fishery, production and sales; mushroom production, processing and storage; animal slaughter house and meat business; herbal production, processing and storage; sugarcane, cardamom and ginger farming, storage and processing and agriculture businesses.

6.3 The interest subsidy facility can be availed only in investment made in areas outside the Kathmandu metropolitan city and other sub-metropolitan cities. The procedure has restricted BFIs to charge more than 6 percent as interest from the borrowers. However, they can charge for insurance premium and credit information sans other services charges. The BFIs would receive subsidized interest payment from government while the remaining will be paid by borrower themselves. The repayment period for such loans will range from a minimum of three months to a maximum of five years. Maximum lending limit for any BFI has been set at one billion rupees for BFIs but that can be extended with NRB approval.

Provision of Watch List

6.4 In a bid to increase resilience in licensed financial institutions, NRB has added a layer to its prevailing credit classifications. It issued directive on maintaining "watch list" of loans. Furthermore, BFIs are required to make extra provisioning for loans under watch list. BFIs have to make provisioning of 1.5 percent in mid-April and 2 percent in mid-July 2015, and increase the provisioning by 50 basis points in every quarter until mid-January 2017 to increase the provisioning up to five percent for such loans after mid-January 2017.

6.5 The central bank added "watch list" as the new category of loan to discourage growing practice of borrowers not utilizing the loans in projects where they were supposed to go. According to this directive, any loan that has crossed the repayment deadline by a month will come under the "watch list". Also, short-term loans and operating loans whose deadline has been extended temporarily without renewal should be categorized under "watch list". Likewise, BFIS have to categorize the loans extended to a borrower whose loans from another bank have turned non-performing, and loans provided to a firm whose net worth and cash flow have remained negative for the past two years despite regular payment of principal and interest, under the "watch list".

BOX 6.1: New Provision Regarding Classification of Loans/Advances and Loan Losses

Entire loans and advances extended by a licensed institution have to be classified as follows based on expiry of the deadline of repayment of the principal and interest of such loans/advances:-

Classification of Loans/ Advances

Pass Loans: Loans/advances which have not overdue and which are overdue by a period up to three months. Such loans require provisioning of one per cent of the total loan amount.

Watch list Loans: If the borrower's cash flow cannot support both the payments, then the loan acquired by the firm should be classified as 'watch list'. Also, loans acquired by firms whose working capital, cash flow or net worth have remained negative for two consecutive years have to be classified as 'watch list', even if the firm is making timely principal and interest payments. In addition, Loans should also be categorized as 'watch list' if the credit obtained by the same borrower from another

financial institution turns into non-performing asset. Among others, credit obtained by borrowers, who have missed monthly, quarterly or half-yearly installment payment deadlines, should also be categorized as 'watch list', adds the directive. Five per cent of the total loan amount must be provisioned for such credit.

Sub-standard: Loans/advances which are overdue by a period from three months to a maximum period of six months. Such loans require provisioning of 25 per cent of the total loan amount.

Doubtful: Loans/advances which are overdue by a period from six-months to a maximum period of one year. Such loans require provisioning of 50 percent.

Loss: Loans/advances which are overdue by a period of more than one year. Such loans require provisioning of 100 percent.

Consumer Financial Protection and Financial Literacy

6.6 NRB has issued a circular regarding financial consumer protection guidelines to licensed institutions to make people aware about financial services and increase transparency in availing fees and charges from customers for services of financial institutions. Similarly, the circular aims to improve financial literacy and bolster consumer confidence in the financial institutions of the country. Major provisions stipulated in the circulars are presented below in the box.

BOX 6.2: Circular on Consumer Financial Protection and Financial Literacy

Transparency: the directive aims to enhance transparency by making compulsory arrangements to publicize all services and conditions including financial instruments and fees for obtaining these services and facilities. Similarly licensed BFIs are required to develop a booklet explaining about features of all deposit and loan services and associated fees and charges.

Licensed BFIs are required to inform the public about types of account, fees levied on services and theirs statement, procedures of banking transaction, process of closing accounts, method of interest calculations, pre-payment charges, actions taken by bank for loan defaults, penalties and late fees, information related to electronic cards and penalties and punishments in banking transactions.

Plain language: licensed BFIs are required to use plain language in notices and information to avoid ambiguity. Furthermore, use of Nepali language has been made mandatory for all communicative and official documents.

Notices: Notices and information of licensed institutions should be easily comprehendible to general public. BFIs are abstained from publishing notices that can create ambiguity in the public.

Easy banking services: BFIs must prioritize senior citizens and differently-able people and assist financially illiterate to avail the service.

Changes in fees and terns of conditions: BFIs should inform customers about changes in pre-agreed conditions and services through national, regional or district level newspapers accordingly with their coverage area.

Fees on operating and closing accounts: BFIs should abstain from charging any fees for operating or closing accounts, Any Branch Banking Services (ABBS), certification of deposit amount or account statements and should pre-inform customers about any fees apart from aforementioned. Furthermore, BFIs are abstained from levying annual fees for different electronic cards but renewal fees upon expiry.

Interest rate: Differential interest rate on different types of saving accounts should not be more than two percentage points. Any adjustments made on saving accounts should be made applicable to all types of saving accounts. Similarly, penal rates on credit (if any) should be accompanied with agreement paper while BFIs can charge interest on penal interests.

Service charge: BFIs should not charge customers in excessive of they have been charged for outsourced services like credit information, black-listing/delisting, electronic cards, mortgage valuation, insurance premium and others, if any. In addition, BFIs should not charge any fee for reactivating dormant account and must credit the interest on the dormant account regardless of cause for dormancy. Similarly, they cannot levy a fee from any account-holder for his inability to maintain minimum balance.

Pre-payment charge: BFIs are required to make clear provision about pre-payment charges in their credit policy and must pre-inform clients about such provision. However, if a client opts to pay the loan from his own income BFIs cannot charge pre-payment fee on such payment.

Grievance hearing: BFIs must open a desk for grievance hearing and inform about it publicly. Similarly, they must assign a hot line and an officer to hear customer grievances.

Financial literacy: BFIs must provide all information regarding any services in plain and understandable language. Similarly, they have to assist in enhancing financial literacy through providing information of financial services and develop advertisements and educational materials in this effect.

Privacy and data protection: BFIs must have sufficient arrangements for information privacy and unofficial access to records, account statements and other personal information of customers.

Financial Literacy, Financial Inclusion, Access to Finance

6.7 NRB has been involved in different activities to promote financial literacy in the country. Different financial literacy materials were disseminated in 2014/15. As NRB is affiliated with the different international organizations like Alliance for Financial Inclusion (AFI), Child and Youth Finance International (CYFI) etc., to promote financial inclusion and financial literacy in the country; various financial literacy-centric programs were organized in 2014/15. As a member of AFI, NRB has made some commitments regarding financial inclusion under the 'Maya Declaration 2013' and most of the commitments in this concern has been fulfilled.

6.8 With regard to financial literacy, NRB celebrated the global financial literacy week called 'Global Money Week' announced by the CYFI in March 2015. In this connection, NRB organized a grand financial literacy rally in Kathmandu on March 14th gathering some 4000 people comprising students, teachers, BFIs, Cooperatives, NGOs, donor agencies, etc. Intensive one-day interaction program on financial literacy focusing child and youths was also organized in Kathmandu on March 17th. During the program, a comprehensive presentation was presented on on-going financial literacy activities in Nepal. Ministry of Education also presented a presentation on its activities on financial literacy. Participants representing school students, teachers, school

organizations, BFIs, cooperatives, NGOs, donor agencies, journalists, etc., actively participated in the interaction.

6.9 Different financial literacy materials, like hand-book entitled 'NRB with Students', story-book called *'Paisako Bot',* musical CD comprising financial literacy songs, etc. were distributed during the rally and interaction program. Moreover, upon the request of NRB; BFIs, NGOs, Cooperatives, Bankers Training Institute, etc. also carried out different financial literacy activities during the week. Different Radio and TV programs on 'Global Money Week' were also broadcasted during the week. NRB have been regularly organizing such programs since 2013.

6.10 A special school-visit program, entitled 'NRB with Students' has been initiated by the NRB on financial literacy since 2013-14. During this on-going program, a team of NRB visits different schools to organize a brief presentation on financial literacy and distributes the reading literacy materials. Till date, NRB has organized such 9 programs in different schools of 4 districts. Most of these programs are chaired by the high-level authorities of NRB, even by the Governor on the occasion.

6.11 NRB has also been working closely with the Ministry of Education to incorporate the issue of financial literacy in formal educational curriculum. A separate window has been built within NRB web-site entitled 'financial literacy'. On the policy front, NRB is working for framing a new National Financial Literacy Policy. This policy is at the final stage of approval.

Foreign Exchange Related Regulations

6.12 NRB issued a circular regarding derivatives transaction to the ‘A’ class commercial banks according to which they can make Forward transaction up to 30 percent of its primary capital adding both buy and sale, except for any kind of speculative transaction.

6.13 In order to manage the foreign exchange risks the ‘A’ class commercial banks and ‘B’ class development banks can make investment in derivatives such as Forward, Futures, Option, and Swap in foreign agency banks. The investment is regulated to the limit of 35 percent of all the foreign exchange liability such as import L/C and other.

6.14 The exporters of specified goods that having at least 30 percent value addition can get export cash incentives based on exports value. The bank is

involved in providing reimbursement of export cash incentives to the commercial banks. As of mid-January 2015, the incentive of Rs. 830 million was provided to the eligible exporters starting from 6 December, 2011.

Regulatory Reform Initiatives

Liquidity Based PCA

6.15 Basel Core Principles No. 6 (Capital adequacy) focuses on capital requirement and enforcing Prompt Corrective Action (PCA). It states, "Supervisors must set prudent and appropriate 30 minimum capital adequacy requirement for banks that reflect the risks that the bank undertakes and must define the components of capital, bearing in mind its ability to absorb losses." It also emphasizes that supervisors should urge all banks to calculate and consistently maintain a minimum capital adequacy ratio. The supervisors should define the components of capital, ensuring that emphasis is given to those elements of capital available for absorbing losses. The supervisor should be equipped with the power to impose a specific capital charge and/or limits on all material risk exposures.

6.16 Similarly, BCP No. 23 (Corrective and remedial powers of supervisors) states that supervisors must have at their disposal an adequate range of supervisory tools to bring about timely corrective actions, if, for example, a bank is not complying with laws, regulations or supervisory decisions or engaged in unsafe or unsound practice or when the interests of depositors are otherwise threatened. These tools include the ability of the supervisor to take prompt remedial action and to impose penalties. The supervisors and regulators in least developed countries are being encouraged to adopt PCA. However, there are some preconditions needed for the adoption of an effective PCA and these include conceptual elements such as a prudential supervisory focus on minimizing public deposit losses, and mandating supervisory action as capital declines. The preconditions also include institutional aspects such as greater supervisory independence and authority, more effective problem bank resolution mechanisms, better methods of measuring capital, and enhancing supervisory capabilities. The PCA approach to supervision believes that early steps in preventing problems in banks are always better than caring for troubled banks.

6.17 NRB has been practicing PCA based on capital adequacy. In the PCA, immediate actions need to be taken to those banks whose capital adequacy

ratio falls short of the regulatory requirement. Such actions include restrictions on branch expansion, dividend payments, additional loan disbursement, deposit collection and increases in salary and allowances depending on the level of shortfall in the minimum regulatory capital adequacy ratio. Recently, NRB realized the need to add additional triggers for PCA that are based on liquidity and non performing assets (NPA). It has already drafted PCA bylaws incorporating such provisions and is under inter departmental consultation. After preliminary discussion within NRB, it will be further discussed with stakeholders and implemented accordingly.

Liquidity Monitoring Framework

6.18 As necessitated by contingency planning, Risk Management Process, and Basel core principles, NRB has issued a Liquidity Monitoring Framework to monitor the liquidity position of commercial banks. The Framework requires banks to submit their short-term liquidity position (liquid asset to short term liabilities position), deposit and credit concentration, interbank transaction, borrowing from NRB (SLF, Repo, refinance), and liquidity profile (short- and long-term asset liability position) within a given timeframe. This Framework helps in monitoring the liquidity positions and devise suitable actions. NRB will incorporate this framework in Unified directive issued for BFIs.

Risk Based Supervision

6.19 Risk Based Supervision (RBS) is a proactive and efficient supervisory process, which enables the supervisor to prioritize and focus efforts and resources on areas with significant risks and/or banks that have high-risk profiles. It entails a shift from a rigid rules/compliance-based supervisory approach to a more risk sensitive one which seeks to encourage a bank to develop and continuously update its internal risk management system to ensure that it is commensurate with the scope and complexity of its operations.

6.20 Adoption of RBS saves supervisory resources and helps to promote a safe and sound financial system. It saves resources by focusing supervisory efforts on areas of higher risk. It is a paradigm shift, which encourages institutions to manage risks themselves as opposed to correcting symptoms of problems in traditional supervision. Under, this approach, supervisors focus their actions on identifying and preventing the causes of problems requiring improvements in management practices and systems. RBS is not transaction based instead it

is a system-based inspection. In this approach, the regulator and supervisor enter into the depth and details of the system and procedures for managing and controlling risks. Risk based supervision is not fully implemented in Nepal. NRB has adopted both compliance based and risk based supervision for commercial banks. NRB aims to implement RBS in full phase by 2016.

Financial Safety Net or Deposit Guarantee

6.21 Developing a financial safety net for banks has been an important issue for sustainable development of financial system. NRB has the objective of promoting stability and credibility of the banking system among the general public. Strengthening regulatory and supervisory functions is important and developing a strong safety net is essential for attaining the objective. Deposit guarantee schemes for up to Rs. 200,000 have been introduced in Nepal. Besides, the establishment of Asset Management Company (AMC), strengthening the capacity of Debt Recovery Tribunal and establishment of Credit Rating Agencies are also equally important to maintain and promote a safe and sound financial system.

Strengthening of Microfinance Development Banks

6.22 Initiatives to promote financial discipline and corporate governance, increase financial soundness and magnification of financial inclusion process that ultimately contribute on the financial stability are underway focusing microfinance development banks.

6.23 Legal framework regarding the establishment of *National Microfinance Fund* is in the offing. A separate unified directive for 'D' class MFDBs has been already put in place. Revision of directives issued to cooperatives licensed by the NRB is under consideration. FINGOs have already been requested to transform themselves into Micro Finance Development Banks within mid-July 2015. Similarly, formulation of *National Financial Literacy Policy* is moving forward. Furthermore, establishment of a separate credit information agency for the MFIs is at the final stage.

Efforts of NRB after earthquakes

6.24 NRB took bold steps to run smooth banking services after the April Earthquake. It instructed all licensed institutions to keep providing services considering safety of theirs staff and assets. Similarly, supervisors from NRB visited banking offices of BFIs in Kathmandu valley to observe the damage

and panic created by the devastating earthquake. Similarly, it asked BFIs to assess damages caused by earthquake and report to NRB for final assessment.

6.25 In a bid to bolster recovery process and induce confidence among people, NRB has announced soft loan facilities to the individuals whose houses were demolished by the earthquake. As NRB does not directly lend to the public, it instructed licensed BFIs to provide loans to the affected people up to Rs.2.5 million in Kathmandu Valley and Rs.1.5 million outside valley as home loans with the condition of charging maximum of two percent interest on such loans. BFIs providing such loan are required to furnished necessary documents and avail the refinancing facility at zero percent. Similarly, it also eased current policy by allowing restructuring of home loans extended to affected people.

Potential Financial Sector Risk after earthquake in April/May 2015

6.26 The earthquake affected the overall economic activities including financial sector. The normal life of people and their economic activities were disturbed. Since economic activities were not conducted smoothly and people could not work normally, the loan and advances of BFIs was affected along with the postponement in loan repayment. If people do come back to normal life for longer period, it may increase the number of loan defaulter and non performing loans. The contraction of banking sector credit may increase banking sector liquidity and risks of substandard loans. Due to damage of collateral (building and projects), banks may face higher risks in loan payment for certain time period. It may affect financial stability adversely.

Mid-term Review of Monetary Policy

6.27 Considering the situation of long standing excess liquidity in the banking system and its likely adverse impact on inflation, external sector and financial stability, the stance of monetary policy has been made slightly tight. However, the provisions have been made to supply adequate credit from the banking system to achieve targeted economic growth for 2014/15.

6.28 There is a challenge for maintaining low level of inflation due to rise in aggregate demand supported by remittance inflows and expanding economic activities, higher inflation in India, increase in petroleum prices resulting from ongoing problems in Gulf countries and yet to improve domestic supply-side bottlenecks.

6.29 In the context of increasing disposable income by remittance inflows and the situation of not increasing supply accordingly, demand side needs to be managed in the short-run. Therefore, monetary policy will focus on containing monetary aggregates at a desired level to reduce additional inflationary pressure considering the sluggish growth of Nepalese economy, monetary policy has also focused on extending credit to the productive sector by encouraging BFIs and strengthening both demand as well as utilization of loans by promoting financial literacy programs. The monetary policy for 2014/15, formulated in this background, is directed towards restraining pressure on prices and external sector stability from demand side and supporting economic growth by promoting credit to the productive sector on supply side.

6.30 The mid-term review of the monetary policy estimated to achieve the targets of annual inflation within 8.0 percent to make conducive environment for growth rate to 6.0 percent and foreign exchange reserve sufficient to import goods and services for 8 months. On the basis of the six months data, the growth rate of credit to private sector has been increased to 20.0 percent from the previously projected 18.0 percent. CRR, SLR, bank rate, refinance rate and special refinance rate as mentioned in the Monetary Policy of the current fiscal year 2014/15 have been kept unchanged. To control excess liquidity in banking system, the reverse repo and deposit auctioning have been continued.

Annex - 1
Structure of the Nepalese Financial Sector (Assets/Liabilities)

(In million Rupees)

Financial Institutions	Mid-July 2011	Mid-July 2012	Mid-July 2013	Mid-July 2014	Mid-Jan 2015
Nepal Rastra Bank	319,692.6	455,826.5	534,897.9	655,280.6	682,351.5
Commercial Banks	853,490.7	1,052,450.7	1,242,881.4	1,467,151.9	1,599,298.9
Development Banks	129,617.4	160,360.2	199,954.8	255,373.4	261,272.5
MFFIs	20,862.9	29,815.5	35,774.9	49,395.8	58,433.6
Finance Companies	118,578.2	109,687.5	100,856.7	105,592.6	112,486.0
Financial Co-operatives	8,150.6	11,652.4	15,415.1	21,030.0	N/A
Financial NGOS	4,937.6	4,260.0	5,560.0	5,120.0	N/A
Contractual Saving Institutions					
Employees Provident Fund	106,584.5	125,752.8	145,283.4	170,638.6	180,796.8
Citizen Investment Trust	26,905.4	38,068.5	42,753.6	54,621.3	61,581.3
Insurance Companies	61,213.4	73,825.0	84,650.4	101,097.2	110,100.0
Postal Savings Bank	1,152.4	1,276.4	1,397.2	1,580.0	N/A
Total	**1,651,185.7**	**2,062,975.5**	**2,409,425.4**	**2,886,881.4**	**3,066,320.5**
Market capitalization	323,484.3	368,262.1	514,492.1	1,057,165.8	963,417.6
Total (incl. market	**1,974,670.0**	**2,431,237.6**	**2,923,917.5**	**3,944,047.2**	**4,029,738.1**
Percentage Share					
Financial Institutions					
Nepal Rastra Bank	19.4	22.1	22.2	22.7	22.3
Commercial Banks	51.7	51	51.6	50.8	52.2
Development Banks	7.8	7.8	8.3	8.9	8.5
Microfinance Development	1.3	1.4	1.5	1.7	1.9
Finance Companies	7.2	5.3	4.2	3.7	3.7
Financial Co-operatives	0.5	0.6	0.6	0.7	N/A
Financial NGOS	0.3	0.2	0.2	0.2	N/A
Contractual Saving Institutions					
Employees Provident Fund	6.5	6.1	6	5.9	5.9
Citizen Investment Trust	1.6	1.8	1.8	1.9	2.0
Insurance Companies	3.7	3.6	3.5	3.5	3.6
Postal Savings Bank	0.1	0.1	0.1	0.1	N/A
Total	**100**	**100**	**100**	**100**	100

Annex - 2
Aggregate Statement of Assets and Liabilities of BFIs (Aggregate)

(In million Rupees)

	Particulars	Mid-July 2012	Mid-July 2013	Mid-July 2014	Mid-Jan 2015
LIABILITIES					
1.	**CAPITAL FUND**	**115163**	**131724.3**	**145861.4**	**164674.5**
	a. Paid-up Capital	104303.8	119506.9	128985.3	137719.5
	b. Statutory Reserves	22068.1	26038.2	32722.1	36138.2
	c. Retained Earning	-24321.8	-22344.2	-27214.2	-21771.9
	d. Others Reserves	13112.8	8523.4	11368.3	12588.7
2.	**BORROWINGS**	**17805.9**	**26999.3**	**18202.8**	**28212.5**
	a. NRB	4286.7	2884.3	2010	2111.6
	b. "A" Class Licensed Institution	3297	10466.6	5182	13895.9
	c. Foreign Banks and Fin. Ins.	2507.9	2954.3	4.1	0
	d. Other Financial Ins.	781.1	2438.3	1306.5	1354.9
	e. Bonds and Securities	6933.2	8255.9	9700.1	10850.1
3.	**DEPOSITS**	**1071394.1**	**1250062**	**1477832.6**	**1569234**
	a. Current	95993.1	111686.5	129108.4	121366.8
	b. Savings	400723.1	471215.4	587593.5	641385.5
	c. Fixed	372137.6	423478.4	453408.6	484840.3
	d. Call Deposits	187998.5	225704.8	285024.3	298618.5
	e. Others	14541.8	17976.8	22697.8	23022.7
4.	**Bills Payable**	**1626.4**	**1561.6**	**1553.1**	**2119.4**
5.	**Other Liabilities**	**123660.2**	**140770.3**	**169227.4**	**184644.5**
	1. Loan Loss Provision	33874	42223.8	48932.5	51436.1
	2. Interest Suspense a/c	26056.2	27920.7	30453.8	33470
	3. Others	63730.1	70625.8	89841.2	99738.4
6.	**Reconciliation A/c**	**1537.8**	**7290**	**2869.5**	**4650**
7.	**Profit & Loss A/c**	**19776.5**	**26544.7**	**31566.8**	**19522.7**
TOTAL LIABILITIES		**1350963.9**	**1584952.3**	**1847113.7**	**1973057**
ASSETS					

	Particulars	Mid-July 2012	Mid-July 2013	Mid-July 2014	Mid-Jan 2015
1.	**LIQUID FUNDS**	**236056.9**	**259224.9**	**319196.6**	**277304.8**
	a. Cash Balance	31020.1	35728.2	41862.1	36552.6
	Nepalese Notes & Coins	30353.3	34876.1	41073.7	35172.4
	Foreign Currency	666.8	852.1	788.3	1380.2
	b. Bank Balance	164605.2	173856.7	220546.6	175483.8
	1. Nepal Rastra Bank	120457.3	130802.8	162286.9	104709.3
	2. "A" Class Licensed Institution	26284.3	23269.1	34656.5	34913.5
	3. Other Financial Ins.	7649.8	5673.4	5302.9	6365.6
	4. In Foreign banks	10213.8	14111.4	18300.4	29495.4
	c. Money at Call	40431.6	49640.1	56788	65268.4
2.	**INVESTMENTS**	**137304.4**	**151340**	**162544.9**	**176360.1**
	a. Govt. Securities	133251.1	149700.8	160867.1	164625.4
	b Others	4053.3	1639.2	1677.78	11734.7
3.	**SHARE & OTHER INVESTMENT**	**52851.1**	**66725.5**	**72656.2**	**79140.2**
4.	**LOANS & ADVANCES**	**779560.9**	**945698.4**	**1119260.8**	**1248089**
	a. Private Sector	741145	915010	1084965.3	1211852
	b. Financial Institutions	31389.3	21910.2	26247.7	26774.5
	c. Government Organizations	7026.6	8778.2	8047.8	9462.4
5.	**BILL PURCHED**	**9634.2**	**9007.9**	**9805.6**	**14642.6**
6.	**LOANS AGT. COLLECTED BILLS**	**645.9**	**1015.5**	**737.3**	**1001.3**
7.	**FIXED ASSETS**	**27146.4**	**28916.8**	**30477.7**	**31184.4**
8.	**OTHER ASSETS**	**93318.3**	**104448.2**	**123962.3**	**132060.7**
	a. Accrued Interests	27621.8	30638.6	32041.3	34611.2
	b. Others	65696.6	73809.6	91921	97449.4
9.	**Expenses not Written off**	**586.9**	**622**	**492**	**458.3**
10.	**Non-Banking Assets**	**2225.1**	**3731.3**	**4757**	**5595.82**
11.	**Reconciliation Account**	**8638.9**	**10394.1**	**-1032.5**	**5924.2**
12.	**Profit & Loss A/c**	**2994.9**	**3827.7**	**4255.8**	**1296.4**
TOTAL ASSETS		**1350963.9**	**1584952.3**	**1847113.7**	**1973057**

Annex - 3

Statement of Assets and Liabilities of BFIs

(Mid-January 2015)

(In million Rupees)

	Particulars	Class "A"	Class "B"	Class "C"	Total
LIABILITIES					
1.	**CAPITAL FUND**	**123981.8**	**29378.9**	**11313.7**	**164674.5**
	a. Paid-up Capital	95569.6	25909.9	16240.0	137719.5
	b. Calls in Advance	198.1	120.6	89.1	407.8
	c. Proposed Bonus Share	1069.1	201.8	88.4	1359.3
	d. General Reserves	30106.7	3432.2	2599.3	36138.2
	e. Share Premium	530.3	81.2	43.9	655.3
	f. Retained Earning	-12115.4	-1190.9	-8465.6	-21771.9
	g. Others Reserves Fund	8623.6	824.1	718.7	10166.4
2.	**BORROWINGS**	**22199.4**	**4319.4**	**1693.7**	**28212.5**
	a. NRB	2073.7	0.0	37.9	2111.6
	b. Interbank Borrowing	8230.1	4010.0	1655.8	13895.9
	c. Foreign Banks and FIs	0.0	0.0	0.0	0.0
	d. Other Financial Ins.	1045.4	309.4	0.0	1354.9
	e. Bonds and Securities	10850.1	0.0	0.0	10850.1
3.	**DEPOSITS**	**1291660.9**	**202680.1**	**74892.8**	**1569233.7**
	a. Current	117384.6	3871.7	110.4	121366.8
	Domestic	99729.5	3821.6	110.4	103661.5
	Foreign	17655.1	50.2	0.0	17705.3
	b. Savings	501407.0	106135.6	33842.9	641385.5
	Domestic	491846.1	104443.7	33769.9	630059.8
	Foreign	9560.8	1691.8	73.0	11325.7
	c. Fixed	395766.7	55341.8	33731.8	484840.3
	Domestic	367262.1	55312.4	33723.8	456298.3
	Foreign	28504.6	29.5	7.9	28542.0
	d. Call Deposits	260904.1	36574.0	1140.4	298618.5
	Domestic	225377.9	36357.8	1140.4	262876.2
	Foreign	35526.1	216.2	0.0	35742.3
	e. Others	16198.5	756.9	6067.3	23022.7

Particulars		Class "A"	Class "B"	Class "C"	Total
	Domestic	14299.2	751.6	6067.3	21118.1
	Foreign	1899.3	5.3	0.0	1904.7
4.	**Bills Payable**	**2087.0**	**20.0**	**12.3**	**2119.3**
5.	**Other Liabilities**	**144007.4**	**18922.7**	**21714.4**	**184644.5**
	1. Sundry Creditors	22890.7	605.6	689.2	24185.5
	2. Loan Loss Provision	34345.9	6867.2	10223.1	51436.1
	3. Interest Suspense a/c	23348.8	3635.6	6485.6	33470.0
	4. Others	63422.0	7814.3	4316.6	75552.8
6.	**Reconciliation A/c**	**-103.5**	**3069.5**	**1684.0**	**4650.0**
7.	**Profit & Loss A/c**	**15465.9**	**2881.8**	**1175.0**	**19522.7**
TOTAL LIABILITIES		**1599298.9**	**261272.5**	**112485.9**	**1973057.3**
ASSETS					
1.	**LIQUID FUNDS**	**183491.3**	**67552.3**	**26261.2**	**277304.8**
	a. Cash Balance	30215.5	5361.2	976.0	36552.6
	Nepalese Notes & Coins	28919.7	5276.9	975.9	35172.4
	Foreign Currency	1295.8	84.3	0.1	1380.2
	b. Bank Balance	128666.3	29200.3	17617.2	175483.8
	1. Nepal Rastra Bank	91430.0	10158.3	3121.0	104709.3
	Domestic Currency	90164.8	10086.8	3121.0	103372.6
	Foreign Currency	1265.2	71.5	0.0	1336.6
	2. "A" Class Licensed Institution	7770.3	15725.6	11417.6	34913.5
	Domestic Currency	7589.2	15705.9	11417.6	34712.7
	Foreign Currency	181.1	19.7	0.0	200.8
	3. Other Financial Ins.	131.8	3155.2	3078.6	6365.6
	4. In Foreign Banks	29334.2	161.2	0.0	29495.4
	c. Money at Call	24609.6	32990.8	7668.0	65268.4
	Domestic Currency	8649.8	32861.7	7668.0	49179.6
	Foreign Currency	15959.7	129.1	0.0	16088.8
2.	**INVESTMENT IN SECURITIES**	**170874.4**	**3048.1**	**2437.6**	**176360.1**
	a. Government Securities	159227.3	2998.0	2400.1	164625.4
	b. NRB Bond	11186.7	50.0	12.5	11249.2
	c. Government Non-FIs	27.8	0.0	0.0	27.8
	d. Other Non-FIs	0.0	0.1	24.7	24.8
	e Non Residents	432.6	0.0	0.3	432.8

	Particulars	Class "A"	Class "B"	Class "C"	Total
3.	**SHARE & OTHER INVESTMENT**	**75535.5**	**1988.5**	**1616.2**	**79140.2**
	a. Interbank Lending	5295.0	57.2	0.0	5352.1
	b. Non Residents	1.9	43.0	0.0	44.9
	c. Others	70238.6	1888.4	1616.2	73743.2
4.	**LOANS & ADVANCES**	**1013720.2**	**168675.8**	**65692.5**	**1248088.5**
	a. Private Sector	982281.9	164864.1	64705.7	1211851.6
	b. Financial Institutions	24222.5	1606.4	945.7	26774.5
	c. Government Organizations	7215.9	2205.3	41.2	9462.4
5.	**BILL PURCHASED**	**14625.4**	**10.7**	**6.4**	**14642.6**
	a. Domestic Bills Purchased	2016.0	10.7	6.4	2033.1
	b. Foreign Bills Purchased	5287.9	0.0	0.0	5287.9
	c. Import Bills & Imports	7321.5	0.0	0.0	7321.5
6.	**LOANS AGAINST COLLECTED**	**1001.3**	**0.0**	**0.0**	**1001.3**
	a. Against Domestic Bills	926.7	0.0	0.0	926.7
	b. Against Foreign Bills	74.6	0.0	0.0	74.6
7.	**FIXED ASSETS**	**23724.3**	**4936.0**	**2524.0**	**31184.4**
8.	**OTHER ASSETS**	**111997.6**	**9941.2**	**10121.9**	**132060.7**
	a. Accrued Interest:	24374.4	3764.9	6472.0	34611.2
	Financial Institutions	377.8	45.7	41.7	465.3
	Government Enterprises	1204.5	260.9	518.2	1983.6
	Private Sector	22792.1	3458.3	5912.0	32162.4
	b. Staff Loans / Adv.	18075.4	1123.5	286.4	19485.3
	c. Sundry Debtors	24386.1	994.6	1226.1	26606.8
	d. Cash In Transit	538.5	0.3	0.0	538.8
	e. Others	44623.2	4057.9	2137.4	50818.5
9.	**Expenses not Written off**	**378.6**	**32.9**	**46.8**	**458.3**
10.	**Non Banking Assets**	**2510.8**	**1542.2**	**1542.8**	**5595.9**
11.	**Reconciliation Account**	**1156.2**	**3088.9**	**1679.1**	**5924.2**
12.	**Profit & Loss A/c**	**283.3**	**455.7**	**557.4**	**1296.4**
TOTAL ASSETS		**1599298.9**	**261272.5**	**112485.9**	**1973057.3**

Annex - 4
Aggregate Balance Sheet of MFFIs ('D' Class Financial Institutions)

(In million Rupees)

	Particulars	Mid-July 2012	Mid-July 2013	Mid-July 2014	Mid-Jan 2015
LIABILITIES					
1.	**CAPITAL FUND**	**2174.7**	**2408.8**	**2816.6**	**5563.1**
	a. Paid-up Capital	1272.7	1546.3	1717.2	3451.3
	b. Statutory Reserves	162.9	245.6	288.3	695.5
	c. Retained Earning	125.2	-25.6	107.6	30.6
	d. Others Reserves	613.8	642.5	703.6	1385.6
2.	**BORROWINGS**	**10753.8**	**13037.6**	**16586.4**	**31586.5**
	a. NRB	210.4	200.9	198.4	432.4
	f. Others	10543.4	12836.7	16388.0	31154.1
3.	**DEPOSITS**	**2574.3**	**3537.4**	**5235.2**	**13093.3**
4.	**Other Liabilities**	**1415.5**	**1818.6**	**2502.9**	**4985.9**
	a. Loan Loss Provision	388.8	436.3	505.5	956.2
	b. Interest Suspense a/c	275.4	354.0	410.0	558.3
	c. Others	751.3	1028.4	1587.5	3471.4
5.	**Reconciliation A/c**	**1726.4**	**223.2**	**2236.6**	**2115.2**
6.	**Profit & Loss A/c**	**277.4**	**470.7**	**629.8**	**1089.5**
	Total	18922.1	21496.4	30007.5	58433.6
ASSETS					
1.	**LIQUID FUNDS**	**2172.8**	**3272.2**	**5843.5**	**6750.0**
	a. Cash Balance	24.9	31.8	44.2	66.0
	b. Bank Balance	1691.9	2632.4	3253.9	4158.5
	c. Money at Call	456.0	608.1	2545.4	2525.4
2.	**INVESTMENT IN SECURITIES**	**111.2**	**164.7**	**128.7**	**116.2**
3.	**SHARE & OTHER**	**2424.6**	**1560.5**	**2040.6**	**2092.7**
4.	**LOANS & ADVANCES**	**11117.0**	**14649.9**	**17738.3**	**39766.3**
	Institutional	11117.0	14649.9	6194.1	16426.6
	Individual			11544.2	27694.4
5.	**FIXED ASSETS**	**225.5**	**259.3**	**340.2**	**635.3**
6.	**OTHER ASSETS**	**907.8**	**1253.2**	**1594.9**	**1693.9**
7.	**Expenses not Written off**	**1.5**	**1.1**	**0.7**	**3.0**
8.	**Reconciliation Account**	**1712.1**	**253.0**	**2234.8**	**201.3**
9.	**Profit & Loss A/c**	**249.7**	**82.5**	**85.8**	**1576.7**
	Total	**18922.2**	**21496.4**	**30007.5**	**51786.5**

Annex 5

Sector wise, Product wise and Security wise Credit flow from BFIs

(Mid-January 2015)

(Rs. in million Rupees)

SECTOR WISE		Class "A"	Class "B"	Class "C"	Total
1.	Agricultural and Forest Related	42412.2	10018.5	1964.0	54394.8
2.	Fishery Related	2642.8	268.8	46.9	2958.6
3.	Mining Related	3196.7	240.5	106.9	3544.1
4.	Manufacturing (Producing) Related	241878.9	10920.6	3896.1	256695.5
5.	Construction	102747.9	21782.1	11120.4	135650.4
6.	Electricity, Gas and Water	25314.9	4130.1	218.9	29663.9
7.	Metal Products, Mach. & Ele. Eqp.	12223.3	2455.8	705.8	15384.9
8.	Tras., Com. and Public Utilities	25150.6	13266.5	6045.4	44462.5
9.	Wholesaler & Retailer	238940.3	29437.8	8291.4	276669.5
10.	Finance, Insurance and Real Estate	78331.6	11436.6	4565.0	94333.2
11.	Hotel or Restaurant	31627.8	5547.7	1706.9	38882.4
12.	Other Services	47511.0	7483.0	2225.3	57219.3
13.	Consumption Loans	75038.9	13583.9	5414.8	94037.6
14.	Local Government	1467.2	43.6	68.0	1578.7
15.	Others	100863.0	38071.0	19323.2	158257.1
	Total sector wise Loan	**1029347.0**	**168686.5**	**65698.9**	**1263732.4**
PRODUCT WISE		**Class "A"**	**Class "B"**	**Class "C"**	**Total**
1.	Term Loan	160884.9	23235.9	8615.0	192735.9
2.	Overdraft	194605.8	42742.2	25.4	237373.3
3.	Trust Receipt Loan / Import Loan	55754.4	0.0	0.0	55754.4
4.	Demand & Other Working Capital Loan	258797.2	18738.5	12996.3	290532.0
5.	Res. Per. H. Loan (Up to Rs. 10 mil.)	75804.0	18485.3	8790.1	103079.4
6.	Real Estate Loan	61978.5	11781.8	9043.0	82803.3
7.	Margin Nature Loan	13657.5	3360.4	3492.1	20510.0
8.	Hire Purchase Loan	48451.4	16901.2	7448.9	72801.5
9.	Deprived Sector Loan	44434.1	8763.0	2195.0	55392.0
10.	Bills Purchased	12664.1	10.7	6.4	12681.2
11.	Other Product	102315.2	24667.4	13086.8	140069.4
Total Product wise Loan		**1029347.0**	**168686.5**	**65698.9**	**1263732.4**

COLLATERAL WISE		Class "A"	Class "B"	Class "C"	Total
1.	Gold and Silver	26641.8	3899.8	395.5	30937.1
2.	Government Securities	921.7	5.4	15.7	942.8
3.	Non-Government Securities	11374.0	2790.2	1903.5	16067.6
4.	Fixed Deposit Receipts	7294.0	1695.5	1110.4	10100.0
	Own	6462.3	1665.3	1110.4	9238.0
	Other Licensed Institutions	831.8	30.2	0.0	862.0
5.	Collateral of Properties	838863.9	154170.2	55247.9	1048281.9
	Fixed Assets	667428.9	153782.2	55015.9	876227.0
	Current Assets	171435.0	388.0	232.0	172054.9
6.	Against security of Bill	15692.2	15.9	0.0	15708.1
	Domestic Bills	4938.4	15.9	0.0	4954.3
	Foreign Bills	10753.8	0.0	0.0	10753.8
7.	Against Guarantee	31581.8	4726.3	645.8	36953.8
	Government Guarantee	2115.1	117.6	68.4	2301.1
	Institutional Guarantee	22588.2	2180.5	300.5	25069.2
	Personal Guarantee	2235.4	117.7	116.9	2470.0
	Collective Guarantee	1161.5	2309.0	27.3	3497.8
	Int. Rtd. Foreign Bank's Guarantee	115.8	0.0	0.0	115.8
	Other Guarantee	3311.0	1.5	132.7	3445.2
8.	Credit Card	476.7	0.0	0.0	476.7
9.	Others	96500.9	1383.3	6380.3	104264.5
Total Collateral wise Loan		**1029347.0**	**168686.5**	**65698.9**	**1263732.4**

Annex - 6

Profit & Loss Account of BFIs

(As of Mid-January 2015)

(In million Rupees)

EXPENSES	Class "A"	Class "B"	Class "C"	Total
1 Interest Expenses	**23227.3**	**6234.3**	**2734.5**	**32196.1**
1.1 Deposit Liabilities	22543.1	6167.3	2716.4	31426.9
1.1.1 Saving A/c	6994.4	2810.7	1073.2	10878.3
1.1.2 Fixed A/c	11418.6	2486.8	1608.2	15513.6
1.1.2.1 Up to 3 Months Fixed A/c	484.8	24.7	15.3	524.8
1.1.2.2 3 to 6 Months fixed A/c	410.0	61.0	21.5	492.5
1.1.2.3 6 Months to 1 Year Fixed A/c	5119.2	1218.3	860.7	7198.1
1.1.2.4 Above 1 Year	5404.6	1182.8	710.8	7298.1
1.1.3 Call Deposit	4113.2	869.9	34.9	5018.1
1.1.4 Certificate of Deposits	16.9	0.0	0.0	16.9
1.2 Others	684.2	67.0	18.1	769.3
2. Commission/Fee Expense	**234.3**	**1.6**	**0.5**	**236.5**
3. Employees Expenses	**7510.7**	**1213.6**	**425.3**	**9149.6**
4. Office Operating Expenses	**5924.9**	**1295.5**	**425.3**	**7645.7**
5. Exchange Fluctuation Loss	**12.9**	**4.5**	**0.0**	**17.3**
5.1 Due to Change in Exchange Rates	12.9	4.4	0.0	17.3
5.2 Due to Foreign Currency Transactions	0.0	0.1	0.0	0.1
6. Non-Operating Expenses	**4.8**	**9.0**	**31.8**	**45.6**
7. Provision for Risk	**4736.7**	**1026.3**	**986.5**	**6749.6**
7.1 Loan loss Provision	4515.5	828.4	698.5	6042.4
7.1.1 General Loan loss Provision	1737.6	235.6	434.2	2407.4
7.1.2 Special Loan Loss Provision	2764.7	553.2	213.6	3531.5
7.1.3 Additional Loan Loss Provision	13.2	39.5	50.7	103.4
7.2. Provision for Non-Banking Assets	216.6	167.9	253.1	637.6
7.3. Provision for Loss on Investment	28.7	29.3	26.1	84.1
7.4. Provision for Loss of Other Assets	-24.1	0.7	8.8	-14.5
8. Loan Written Off	**16.6**	**19.3**	**120.5**	**156.3**

9. Provision for Staff Bonus	1431.9	268.8	76.2	1776.9
10. Provision for Income Tax	4463.5	782.5	204.8	5450.8
11. Others	1.4	21.8	15.5	38.7
12. Net Profit	15379.4	2473.4	1076.5	18929.4
TOTAL EXPENSES	**62944.5**	**13350.6**	**6097.4**	**82392.5**
INCOME				
1. Interest Income	**48010.7**	**11075.5**	**4205.2**	**63291.4**
1.1. On Loans and Advance	46269.3	10185.5	3814.7	60269.5
1.2. On Investment	1012.9	67.5	56.7	1137.0
1.2.1 Government Bonds	883.0	61.9	45.1	990.0
1.2.2 Foreign Bonds	14.8	0.0	0.0	14.8
1.2.3 NRB Bonds	67.7	4.5	8.5	80.8
1.2.4 Debenture & Bonds	47.3	1.1	3.0	51.4
1.3 Agency Balance	284.0	67.6	32.8	384.5
1.4 On Call Deposit	154.9	661.1	241.3	1057.3
1.5 Others	289.7	93.8	59.7	443.1
2. Commission & Discount	**4098.4**	**304.7**	**59.4**	**4462.5**
2.1 Bills Purchase & Discount	116.6	1.0	0.0	117.6
2.2 Commission	3445.5	220.0	33.7	3699.2
2.3 Others	536.3	83.7	25.7	645.7
3. Income From Exchange Fluctuation	**1906.3**	**22.9**	**0.0**	**1929.2**
3.1 Due to Change in Exchange Rate	508.7	1.4	0.0	510.1
3.2 Due to Foreign Currency Trans.	1397.6	21.5	0.0	1419.2
4. Other Operating Income	**2104.8**	**715.1**	**236.8**	**3056.7**
5. Non Operating Income	**3377.6**	**138.1**	**147.9**	**3663.6**
6. Provision Written Back	**2969.7**	**1016.9**	**906.9**	**4893.5**
7. Recovery from Written off Loan	**214.5**	**1.2**	**30.3**	**246.0**
8. Income from Extra Ordinary Expenses	**65.6**	**29.0**	**51.9**	**146.5**
9. Net Loss	**196.7**	**47.4**	**458.9**	**703.0**
TOTAL INCOME	**62944.5**	**13350.6**	**6097.4**	**82392.5**

** Cumulative figure adjusted for percentage calculation*

Annex - 7

Financial Soundness Indicators (Mid-January, 2015)

Indicators	A	B	C	Total
Capital Adequacy Ratios				
Regulatory capital to risk-weighted assets	11.30	15.40	13.96	11.98
Regulatory Tier - 1 capital to risk-weighted assets	9.69	14.57	13.24	10.52
Non-performing loan to total gross loan	2.80	4.01	14.90	3.59
Non-performing loan net of provisions to capital	4.89	4.96	1.65	4.70
Share of Sector Wise Loans in Total Loan (percentage)				
Agricultural and Forest Related	4.12	5.94	2.99	4.30
Fishery Related	0.26	0.16	0.07	0.23
Mining Related	0.31	0.14	0.16	0.28
Agricultural, Forestry and beverage Production	23.50	6.47	5.93	20.31
Non-food Production Related				
Construction	9.98	12.91	16.93	10.73
Electricity, Gas and Water	2.46	2.45	0.33	2.35
Metal Products, Machinery & Electronic Equipment	1.19	1.46	1.07	1.23
Transport, Communication and Public Utilities	2.44	7.86	9.20	3.53
Wholesaler & Retailer	23.21	17.45	12.62	21.89
Finance, Insurance and Real Estate	7.61	6.78	6.95	7.46
Hotel or Restaurant	3.07	3.29	2.60	3.08
Other Services	4.62	4.44	3.39	4.53
Consumption Loans	7.29	8.05	8.24	7.44
Local Government	0.14	0.03	0.11	0.12
Others	9.80	22.57	29.41	12.52
Total	**100.0**	**100.0**	**100.0**	**100.0**
Returns on Assets	0.95	0.93	0.55	0.92
Returns on Equity	10.27	7.35	5.28	9.47
Interest Margin to Gross Income (percent)	68.33	80.39	76.80	70.34
Non-interest Expenses to Gross Income (percent)	37.74	42.28	46.92	38.76
Liquid Assets to total Assets	22.13	27.02	25.49	22.97
Liquid Assets to total Deposits	27.40	34.83	38.29	28.88
Credit to Deposit Ratio	79.69	83.23	87.72	80.53

Annex - 8

Stress Testing Results for Commercial Banks

<table>
<tr><th rowspan="2">Criteria</th><th>Mid-Jan 2015</th><th>Mid-Jul 2014</th><th>Mid-Jan 2014</th><th>Mid-Jul 2013</th></tr>
<tr><th colspan="4">No. of banks with CAR < 10%</th></tr>
<tr><td colspan="5">Credit shocks</td></tr>
<tr><td>15 Percent of Performing loans deteriorated to substandard.</td><td>22</td><td>16</td><td>20</td><td rowspan="4">27</td></tr>
<tr><td>15 Percent of Substandard loans deteriorated to doubtful loans.</td><td>2</td><td>4</td><td>3</td></tr>
<tr><td>25 Percent of Doubtful loans deteriorated to loss loans.</td><td>2</td><td>4</td><td>3</td></tr>
<tr><td>5 Percent of Performing loans deteriorated to loss loans.</td><td>26</td><td>22</td><td>24</td></tr>
<tr><td>All NPLs under substandard category downgraded to doubtful.</td><td>2</td><td>4</td><td>3</td><td rowspan="2">2</td></tr>
<tr><td>All NPLs under doubtful category downgraded to loss.</td><td>3</td><td>4</td><td>3</td></tr>
<tr><td>25 Percent of performing loan of Real Estate loan directly downgraded to substandard category of NPLs.</td><td>3</td><td>4</td><td>3</td><td>2</td></tr>
<tr><td>25 Percent of performing loan of Real Estate loan directly downgraded to Loss category of NPLs.</td><td>14</td><td>9</td><td>9</td><td>5</td></tr>
<tr><td>Top 2 Large exposures downgraded: Performing to Substandard</td><td>6</td><td>6</td><td>3</td><td>2</td></tr>
<tr><td colspan="5">Liquidity shocks</td></tr>
<tr><td>Withdrawal of customer deposits by 2% 5% 10% 10% and 10% for five consecutive days respectively.</td><td>23</td><td>10</td><td>16</td><td>5</td></tr>
<tr><td>Withdrawal of deposits by 5%</td><td>10</td><td>0</td><td>2</td><td>1</td></tr>
<tr><td>Withdrawal of deposits by 10%</td><td>18</td><td>7</td><td>12</td><td>4</td></tr>
<tr><td>Withdrawal of deposits by 15%</td><td>26</td><td>17</td><td>22</td><td>16</td></tr>
<tr><td>Withdrawal of deposits by top 2 institutional depositors.</td><td>16</td><td>8</td><td>11</td><td>10</td></tr>
<tr><td>Withdrawal of deposits by top 3 institutional depositors.</td><td>20</td><td>11</td><td>15</td><td>14</td></tr>
<tr><td>Withdrawal of deposits by top 5 institutional depositors.</td><td>20</td><td>18</td><td>20</td><td>21</td></tr>
<tr><td>Withdrawal of deposits by top 2 individual depositors.</td><td>1</td><td>0</td><td>0</td><td>1</td></tr>
<tr><td>Withdrawal of deposits by top 3 individual depositors.</td><td>1</td><td>0</td><td>0</td><td>1</td></tr>
<tr><td>Withdrawal of deposits by top 5 individual depositors.</td><td>1</td><td>0</td><td>0</td><td>1</td></tr>
</table>

Annex - 9

Composition of Financial Stability Oversight Committee

Name and Designation	Status
Mr. Gopal Prasad Kaphle, Deputy Governor	Chairperson
Mr. Maha Prasad Adhikari, Deputy Governor	Member
Mr. Hari Prasad Kaphle, Executive Director, Development Bank Supervision Department	Member
Mr. Narayan Prasad Paudul, Executive Director, Bank Supervision Department	Member
Mr. Nara Bahadur Thapa, Executive Director Research Department	Member
Dr. Binod Atreya, Executive Director, Micro Finance Promotion and Supervision Department	Member
Mr. Janak Bahadur Adhikari, Executive Director, Finance Company Supervision Department	Member
Mr. Bhishma Dhungana, Executive Director, Foreign Exchange Management Department	Member
Mr. Shibanath Pandy, Executive Director, Bank and Financial Institutions Regulation Department	Member
Mr. Ramesh Kumar Pokharel, Director, Bank and Financial Institutions Regulation Department	Member Secretary
Registrar, Department of Cooperative	Invitee Member
Chief Executive, Insurance Board	Invitee Member
Chief Executive, Security Board of Nepal	Invitee Member
Administrator, Employee Provident Fund	Invitee Member
Chief Executive Officer, Citizen Investment Trust	Invitee Member
Related Sectors Experts (maximum 2)	Invitee Member

Annex - 10

Composition of Financial Stability Sub-Committee

Name and Designation	Status
Mr. Ramesh Pokharel, Director, Bank and Financial Institutions Regulation Department	Coordinator
Mr. Narendra Singh Bista, Deputy Director, Development Bank Supervision Department	Member
Mr. Devendra Gautam, Deputy Director	Member
Mr. Ram Hari Dahal, Deputy Director, Micro Finance Promotion and Supervision Department	Member
Mr. Bigyan Raj Subedi, Deputy Director, Research Department	Member
Mr. Nishchal Adhikari, Deputy Director, Finance Company Supervision Department	Member
Ms. Subash Aacharya, Deputy Director, Foreign Exchange Management Department	Member
Ms. Samjhana Dhakal, Deputy Director Bank and Financial Institutions Regulation Department	Member Secretary