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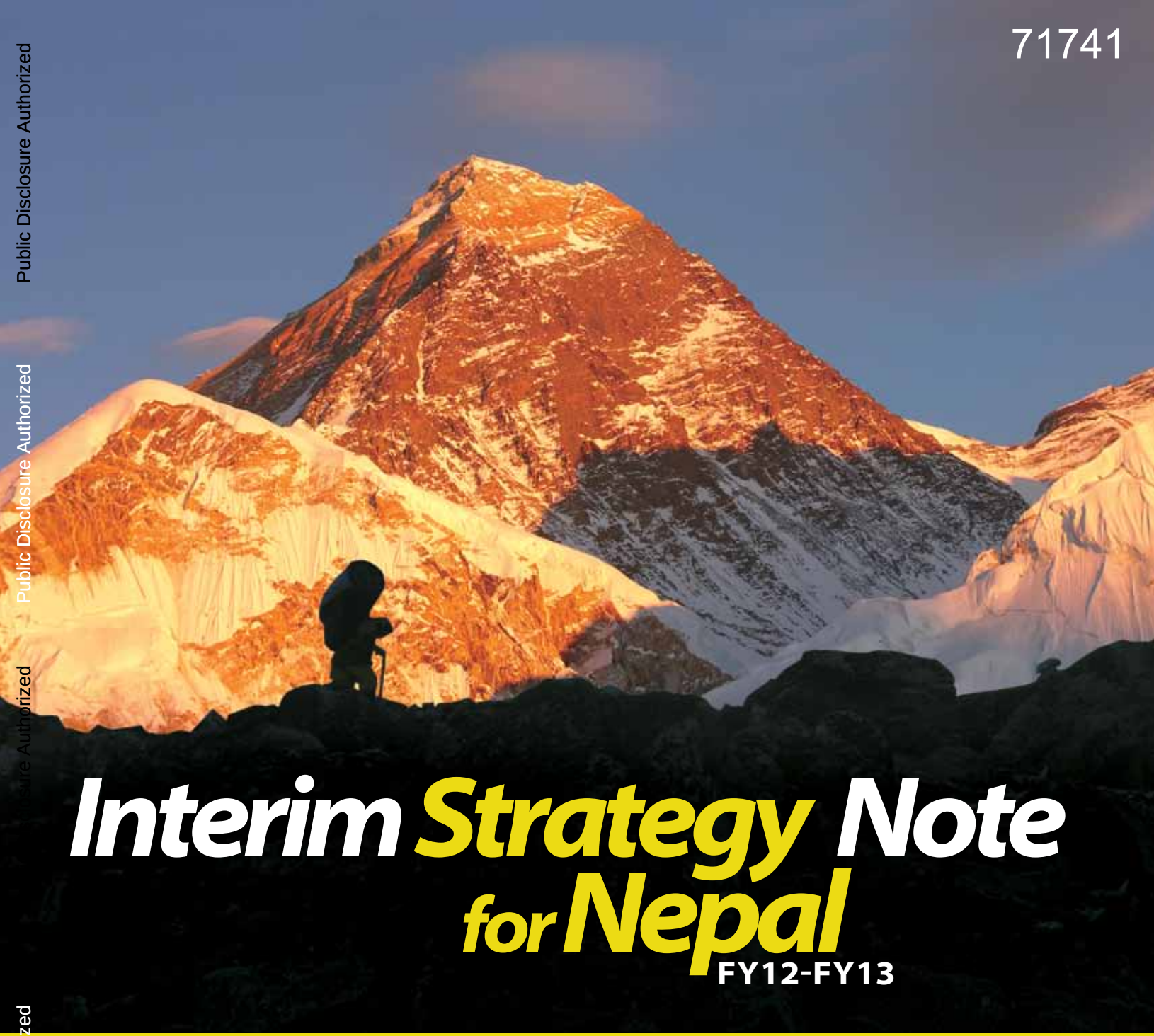

Interim Strategy Note for Nepal

FY12-FY13

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THE WORLD BANK GROUP

Interim Strategy Note for Nepal

FY12-FY13

THE WORLD BANK GROUP

This joint IDA-IFC Interim Strategy Note (ISN) was prepared under the guidance of Ellen Goldstein (IDA Country Director from July 1, 2011) and Susan Goldmark (IDA Country Director till June 30, 2011), and Kyle Kelhofer (IFC Country Manager), by a team led by Rajashree Paralkar, Task Team Leader (IDA) and Gunjan Gulati (IFC) and co-led by Hiramani Ghimire (IDA) and Rajeev Gopal (IFC).

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Interim Strategy Note for Nepal

FY12-FY13

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ABBREVIATIONS AND ACRONYMS

AAA	Analytical and Advisory Activities
ADB	Asian Development Bank
AF	Additional Financing
AGEI	Adolescent Girls' Employment Initiative
AMP	Aid Management Platform
A2F	Access to Finance
CA	Constituent Assembly
CSO	Civil Society Organization
CDD	Community Driven Development
CIF	Climate Investment Fund
CMD	Community Managed & Driven
DFID	UK Department for International Development
DRM	Disaster Risk Management
EVENT	Enhanced Vocational Education and Training
FDI	Foreign Direct investment
FPCR	Food Price Crisis Response
FY	Fiscal Year
GAAP	Governance Accountability Action Plan
GDP	Gross Domestic Product
GESI	Gender Equality and Social Inclusion
GFDRR	Global Facility for Disaster Reduction & Recovery
GON	Government of Nepal
GPF	Governance Partnership Facility
GSEA	Gender and Social Exclusion Assessment
ICA	Investment Climate Assessment
ICT	Information Communication Technology
IDA	International Development Association
IFC	International Finance Corporation
ISN	Interim Strategy Note
JICA	Japan International Cooperation Agency
MDG(s)	Millennium Development Goal(s)
MFIs	Microfinance Institutions
MDTF	Multi-Donor Trust Fund
MIGA	Multilateral Investment Guarantee Agency
MOF	Ministry of Finance
MTEF	Medium-Term Expenditure Framework
NBF	Nepal Business Forum
NRB	Nepal Rastra Bank
NICRP	Nepal Investment Climate Reform Program
NLTA	Non-Lending Technical Assistance
NOC	Nepal Oil Corporation
NPC	National Planning Commission
NPPR	Nepal Portfolio Performance Review
PAF	Poverty Alleviation Fund
PFM	Public Financial Management
PPCR	Pilot Program for Climate Resilience
PPP	Public Private Partnership
PRAN	Program for Accountability in Nepal
RSF	Risk-Sharing Facilities
RTI	Right to Information
SAFANSI	South Asia Food and Nutrition Security Initiative
SARTI	South Asia Regional Trade and Integration
SAWI	South Asia Water Initiative
SEZ	Special Economic Zone
SME	Small and Medium Enterprises
SREP	Scaling-Up Renewable Energy Program
SWAp(s)	Sector Wide Approach(es)
TEVT	Technical Education and Vocational Training
UNDP	United Nations Development Program
UNMIN	United Nations Mission in Nepal
WBG	World Bank Group
WDR	World Development Report

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EXECUTIVE SUMMARY

Country context

i. Nepal is passing through a momentous and prolonged political transition. This has two inter-related processes: the promulgation of a new Constitution and the completion of the ongoing peace process. The new Constitution is supposed to lead to a major restructuring of Nepal into a federal state. This process will involve challenges in terms of managing ethnic aspirations and maintaining political stability. The integration/rehabilitation of ex-Maoist combatants is one of the core issues of the peace process.

ii. Political transition and attainment of peace has overshadowed economic issues. Real GDP growth in FY10 was 4.6 percent, with agriculture, construction, financial and other services, and consumption being the major sources of growth. International migration is a major safety valve; remittances are estimated to be equivalent to 25-30 percent of GDP. But remittances have failed to offset the effects of a high trade deficit and capital flight. FY11 GDP growth is estimated to be 3.5 percent due to poor performance in non-agricultural sectors, delayed budget implementation and tight credit conditions. Nepal maintained a policy of prudent fiscal management during FY10 and through mid-FY11, but expenditure quality remains an issue.

iii. Notwithstanding the challenging political environment, the country has made significant progress in social development indicators. Many of the Millennium Development Goal (MDG) indicators have improved, and poverty levels are declining. Inclusion and representation have received increased policy attention, but capacity building of marginalized communities remains challenging.

National development strategy and the World Bank Group's response

iv. The Government's development strategy is outlined in an 'approach paper' for the Three Year Interim Plan (July 2010-June 2013). This plan has two major objectives - poverty alleviation and the establishment of sustainable peace through inclusive, employment-centric growth. The proposed Interim Strategy Note (ISN) focuses on agriculture, infrastructure, and social development which are basic priorities for Nepal and consistent with the Plan.

v. The ISN will continue to pursue the overarching goal of supporting the Government of Nepal (GON) to build a peaceful, prosperous and just Nepal. The ISN's three pillars include: (i) enhancing connectivity and productivity for growth;

(ii) reducing vulnerabilities and improving resilience; and (iii) promoting access to better quality services. Its cross-cutting themes which permeate all operations are: (i) governance and accountability, and (ii) gender equality and social inclusion.

vi. The 2011 World Development Report (WDR) on Conflict, Security and Development provides valuable insights for this ISN. Many of the principles of engagement proposed by the WDR are relevant for Nepal: enhancing political and economic inclusion, delivering early results to build public trust and confidence, focusing on social accountability tools, applying community managed/driven (CMD) approaches, and strengthening institutions in a phased approach. The ISN encompasses these principles.

Proposed program

vii. The ISN concept served as an input to IDA's 2011 South Asia regional strategy which emphasizes selectivity based on client demand, possibility to leverage results (particularly for MDGs), and opportunities for regional integration. In addition, criteria for Nepal operations include: (i) government and broad political support;

(ii) IDA's comparative advantage vis-à-vis other development partners; and (iii) evidence of effective implementation capacity. All proposed FY12/13 IDA Nepal operations build upon ongoing operations which are being implemented successfully.

viii. IDA will maintain its interventions in seven areas under the three ISN pillars: (i) power, roads, and, agriculture; (ii) food security/livelihood vulnerability; and (iii) education, health, and urban services. An eighth area of climate change and disaster management will continue to be supported exclusively through trust funds. These interventions should contribute to increased access to social and infrastructure services. The important area of private sector development will be taken up by the IFC leading on improving access to finance and investment climate.

ix. IFC's program in Nepal will seek to design and implement programs aligned with the three strategic pillars of IFC's regional South Asia Strategy which include: (i) promoting inclusive growth through emphasizing the base of the economic pyramid, rural areas, infrastructure building, and improving access to finance for MSMEs; (ii) addressing climate change through mitigation and adaptation, including renewable energy and energy efficiency investments and projects which focus on cleaner technology; and (iii) supporting regional and global integration through intra-regional trade facilitation, South-South investments, transport and logistics, investment climate and inclusive business models.

Instruments of engagement

x. The ISN incorporates a mix of sector investment loans and knowledge services. IDA's primary instrument will be the Sector Investment Loans, using Additional Financings and emergency operations where needed. The knowledge services will largely be delivered on a programmatic basis and "just-in-time" support will be continued.

Risk management

xi. Major risks to the proposed programs are associated with political uncertainties. Given the short time frame of the ISN, it does not propose large irreversible commitments. Attainment of results will be carefully monitored and corrective measures taken. If security risks increase in specific geographic areas, IDA will exit from those areas.

xii. IDA will engage with political leaders on a regular basis about development challenges so that all key parties are informed. Implementation of IDA's access to information policy and ongoing geo-mapping initiatives will improve information flows about IDA's interventions. Maintaining strong relationships with other development partners will help to collectively solve problems with the government. Closer links with civil society through new initiatives will help strengthen the accountability of IDA-supported interventions.

xiii. The community-managed and driven (CMD) project portfolio has shown robustness in the context of changing risks and an uncertain political situation. For the bulk of our program, the track record on CMD operations shows that they can withstand quite serious conflict situations. These operations will be maintained while the capacity of the state continues to be built. The ISN program will be flexible to respond to the new challenges of implementing the proposed federal structure once this has been formally adopted.

COUNTRY CONTEXT

1. Nepal is passing through a momentous and prolonged political transition. In the past five years, Nepalis have witnessed the signing of a peace agreement between the Maoists and the state, a new Interim Constitution, the election of a Constituent Assembly (which declared Nepal a federal republic), four governments (three during FY10-11 Interim Strategy Note period), and the rise of strong ethnic identity movements. The political compact around a new Constitution that endorses the devolution of power, social and political inclusion, democratic elections, and political accountability represents an opportunity in this transition. A new Prime Minister from the Unified Marxist Leninist (UML) party took office in February 2011 with the support of the Maoist party. However, inter and intra-party divisions make any government vulnerable. The major political parties are divided over core issues of the new Constitution including elections, systems of governance, and federalism. As a result, the Constituent Assembly (CA) could not meet its extended deadline of May 28, 2011 to pass the constitution. Now the deadline has been extended by three months to August 31, 2011[1]. If a draft framework for the Constitution is ready during this time and the political parties agree on the Maoist ex-combatants re-integration into the Nepal Army, then a final possible extension of three months is likely. However, the Supreme Court has ruled that this must be the final extension.

2. Given the extent of current transitions in Nepal, an interim strategy is being prepared, covering FY12 and FY13[2]. Major milestones of the peace process are yet to be met and progress in constitution-writing has been slow. The new Constitution is supposed to lead to a major restructuring of the state as Nepal will adopt federalism as a fundamental principle of governance. Managing ethnic aspirations, including those of the Madhesis and Janajatis[3] represents another challenge. In addition, elections both at national and local levels are supposed to be held after the Constitution is promulgated. The proposed interim strategy will set out some basic parameters of the World Bank Group (WBG) program but still retain the flexibility needed to deal with an uncertain and potentially volatile birth of this new republic. If the situation stabilizes over the next two years, it should be possible to prepare a Country Assistance Strategy (CAS) after this Interim Strategy Note (ISN). In the meantime, this ISN follows the previous two ISNs[4].

A. Political Context

3. Political instability has been the defining feature of the Nepali state during the last two decades. Nepal has had 20 governments since the introduction of democracy in 1990. Inter-party and intra-party tensions have increased among almost all parties because of growing factionalism. Given political uncertainties, actions of political parties and their leaders are often guided by short-term interests. Their willingness and ability to work towards longer-term benefits which might require sacrifices now or at the expense of short-term interests is limited.

4. Nepal is still emerging from a violent 10-year conflict with some aftershocks. This has contributed to a progressive erosion of the effectiveness of some state institutions. For instance, poor law and order is a growing concern, particularly in certain geographic areas. Also, the conflict raised awareness that the Nepali state had been associated with exclusionary political, social, and economic institutions that did not reflect the country's diversity. This has led to the rise of identity politics with an increasing demand for state recognition and greater accommodation of diverse social, cultural, and ethnic identities. The *Madhes Andolan* of early 2007 led to the incorporation of the principle of federalism in the Interim Constitution. One of the yet unresolved issues for the new constitution is the nature, form and degree of decentralization of the state. These challenges need to be addressed as part of the country's transition to peace and democracy. The CA provides an inclusive forum to negotiate these issues, but its potential has not yet been fully utilized. Informal political forums and 'street actions' are popular as approaches to resolving politically contested issues. Also, Nepal's local government officials elected in 1999 were dismissed in 2002; the lack of elected local officials increases the challenge of making the state downwardly accountable to its citizens.

5. Political transition and attainment of peace has overshadowed economic issues. As a result, inadequate attention has been given to issues of economic and other reforms that could improve the investment climate, stimulate growth and create more private sector jobs. Maintaining law and order has been a fundamental challenge for improving the investment climate; 90 percent of firms interviewed for WBG's

Investment Climate Assessment (ICA) cited poor law and order as their key concern. While the political space to introduce difficult reform measures is very limited, some actions to improve the current environment are underway. Economic growth and increased private investment is dependent upon a political settlement that promotes greater law and order.

B. Economic Update and Outlook

6. Nepal's economic growth has been adversely affected by the political uncertainty. Real GDP growth was 4.6 percent in FY10—following 4.9 percent in FY09 (see Table 1). Sources of growth include agriculture, construction, financial and other services, and consumption fueled by remittances. The remittance growth slowed to 11 percent (in NPR terms) from above 40 percent during the two previous years, and international reserves declined by about US$300 million to 6.5 months of imports. Official remittances, excluding informal flows and flows from India, remains about 20 percent of GDP. (When these flows are included, remittances are estimated to be equivalent to 25-30 percent of GDP). The trade deficit rose to 27 percent of GDP with surging imports and sluggish exports, and the overall BOP balance turned to deficit in FY10 as official remittances could not offset the high trade deficit. Capital flight added to the BOP deficit. To address this situation, the Nepal Rastra Bank (NRB) controlled gold imports (which was a major conduit for capital flight) and tightened the cap on real estate lending.

7. Despite political uncertainties, Nepal maintained a policy of prudent fiscal management during FY10 and through mid-FY11. The rapid expansion of expenditures (20 percent of GDP in FY10) has been supported by a strong revenue performance (15 percent of GDP) and the availability of foreign aid (2.5 percent) and domestic borrowing (2.5 percent). But expenditure quality remains an issue because of limited implementation capacity, emerging public financial management problems, and increasing transfers, some of which have limited transparency. The four-month delay in passage of the FY11 budget adversely affected the implementation speed of government projects.

8. Food prices in Nepal have risen rapidly, affecting the poor, especially in food-insecure areas. Food inflation remains at about 15-17 percent nationally[5]. An estimated 3.5 million people are currently food insecure; the impact of high food prices is most severe in economically-, geographically- and socially-marginalized communities. The country has also experienced a series of droughts and erratic monsoons in food-insecure areas which have reduced food availability and raised prices. The overall effect of rising or high food prices on the poor is therefore a function of location as well as prices. The urban poor are most affected by high prices for staples and vegetables in urban markets, while the rural poor – especially in remote, chronically food-insecure districts – are doubly impacted by high transport costs and grain prices. Recently improved production figures in both India and Nepal are likely to have a mitigating effect in the near term, but the government will have to continue its concerted effort to encourage a supply response and increase agricultural productivity to address chronic food insecurity in vulnerable regions.

9. The impact of international fuel price increases has largely been on government finances in Nepal. The government has not passed through all the increase of oil import prices, except gasoline[6], to consumers, and thus the impact appears as higher loss of Nepal Oil Corporation (NOC) and their monthly losses have increased. To the extent there have been modest adjustments in retail prices of various oil products, the poor have been affected--but modestly. This is in part because the real poor in rural areas consume few oil products (mostly kerosene for lighting). The urban poor, however, consume more LPG[7] for cooking and the impact on them would need to be monitored.

10. The joint Bank-Fund Debt Sustainability Analysis of 2011 concludes that Nepal remains at moderate risk of debt distress[8]. Nepal has successfully lowered its debt level from 43 to 35.4 percent of GDP from 2007 to 2011, and many indicators are well below the sustainability thresholds. Though debt dynamics are resilient to standard stress tests, debt indicators breach the thresholds under alternative scenarios analyzing debt risks arising due to financial sector vulnerabilities and to state-owned enterprises (SOEs) contingent liabilities. External public debt stands at US$3.5 billion (22 percent of GDP) in 2011. The largest share of this, 86 percent, is owed to the World Bank (WB) and the Asian Development Bank (ADB). The remainder is owed to bilateral

DEPARTURES

donors, among which Japan is the main creditor accounting for about 7 percent of total external public debt. The domestic public debt stock stands at 13.4 percent of GDP. In addition to the public debt, private external debt stands at 1.7 percent of GDP and is comprised of trade credits.

11. Since July 2010, NRB has been adopting some strong measures to reduce risks to the financial system. The financial sector's vulnerability rose during 2010 as many private banks continued to increase their exposure to the real estate sector at artificially inflated asset values associated with a real estate boom. NRB is strengthening its regulatory and supervision capacity - which is particularly important given the growing complexity of the sector. The officially announced level of non-performing assets of the banking system has now come down from 3.6 percent in 2009 to 2.5 percent in 2010. The current interbank rate is about 10 percent and the 91-day treasury rate is 8-9 percent, well above historical averages. Although NRB has taken some measures to minimize the risks, vulnerabilities remain. With the recent calming down of the boom, real estate transactions have largely halted and asset prices have started to come down. However, financial institutions that have high real estate exposure remain vulnerable due to possible deterioration of asset quality.

12. Economic outlook during the ISN period points to a weaker growth performance. The baseline projections take into account some financial sector weaknesses. GDP growth is expected to be sluggish during the ISN period. In FY11, growth is estimated to be 3.5 percent due to external shocks to oil and food prices, vulnerabilities in the banking sector and as last years' agricultural growth normalizes. Real GDP growth forecast for FY12 is around 3 percent in light of worsening structural economic weaknesses. Growth performance may strengthen slightly in FY13 to 3.4 percent as external price shocks fade, and if financial sector vulnerabilities are addressed, and prudent fiscal and macro policies are followed.

13. Inflation is around 9.5 percent in FY11, but is expected to gradually decline to around 9 percent in FY12 and 8.3 percent in FY13. Nepal's inflation rate is tightly linked to the inflation in India, and is marginally higher, due to lower productivity in Nepal. Over the ISN period, expected slowdown of inflation rate in India is likely to bring inflation down in Nepal. The exchange rate is assumed to remain pegged to the Indian rupee at the current level over the projection period[9]. The current account is expected to remain in a slight deficit in FY12 and FY13 at around 1.3-1.5 percent of GDP, from a deficit of 1.7 percent of GDP this fiscal year. Exports of goods and services are assumed to grow at an average of 7 percent over the ISN period. Remittances are expected to grow by around 12 percent annually. While import value growth is expected to be around 8.5 and 9.5 percent in FY12 and FY13; slower economic growth and slower remittances may slow down such growth. Foreign direct investment (FDI) is expected to finance only around 15 percent of the current account deficit. The overall fiscal deficit (after grants) is projected to rise to 3 percent of GDP in FY12 and FY13, with financing coming more from domestic than from foreign sources. Revenues are projected to be around 18 percent of GDP during the ISN period. Grants are estimated to be 2.6 percent of GDP in FY11 and are expected to hover around this rate. Expenditures are around 20 percent of GDP in FY11 and are expected to rise to 21 percent in FY12 as army integration costs, and interest rates on loans to cover NOC losses are expected to increase. In addition, about 1 percent of GDP is estimated to be NOC losses, which are financed domestically and recorded as contingent liabilities. The primary deficit is estimated to be 1.7 percent of GDP during the ISN period. Net domestic financing is likely to increase to 2.6 percent of GDP in FY12.

C. Poverty, Social Development and the Millennium Development Goals

14. Poverty has multi-dimensional manifestations in Nepal. Nepal is the seventeenth poorest country in the world with an annual per capita income of US$490[10]. The proportion of poor people has declined substantially in recent years from 42 percent in 1995-96 to 31 percent in 2003-04 (CBS 2005)[11]. More recent estimates show that since 2004, the national poverty rate may have declined further[12]. Income disparity has, however, increased during the same period which is reflected in the Gini co-efficient going up from 0.34 in 1996 to 0.41 in 2003. The Human Development Index ranks Nepal at 138 out of 169 countries in 2011, up from 136 out of 159 countries in 2003 (i.e. an increase from the 14th percentile to the 19th percentile).

15. Progress on several social indicators has been impressive (see Table 2). Many of the Millennium Development Goal (MDG) indicators have improved (primary education, education gender parity, under-5 mortality).

16. Notwithstanding the difficult and challenging political environment, the country has made commendable strides in primary education. The net primary enrollment rate is more than 90 percent. Gender and social parity have been achieved in primary education. The Gender Parity Index for secondary school net enrollment has also increased from 0.87 (2007) to 0.98 (2010). This improving trend is also true for different caste and ethnic groups. Nepal's completion rates, however, are unsatisfactory though improving[13].

17. Health sector indicators have also improved. The under-5 mortality rate has declined from 85 per 1000 in 2000 to 48 in 2009 and the infant mortality rate from 63 per 1000 live births to 39 during the same period. At least one-third of deliveries are now in the presence of trained health workers. Nepal won the MDG Millennium award in 2010 for reducing maternal mortality, but the rate is still high at 380 per 100,000 live births[14]. However, the nutritional status of women and children has not shown much improvement with chronic malnutrition affecting about half of the nation's children.

18. Despite the lower cultural and economic status traditionally accorded to women, gender relations in Nepal are undergoing significant changes. Women have been officially recognized (in the Comprehensive Peace Agreement, the Interim Constitution and the Three Year Interim Plan) as a social group similar to the Dalits, Madhesis, Muslims and Janajatis. The issue of gender discrimination is thus coming to be understood as not just a welfare issue or even a development issue but as a political issue that must be addressed as part of the process of state restructuring. The National Planning Commission (NPC) introduced the Gender Equality and Social Inclusion (GESI) framework into the preparation of the Three Year Interim Plan (2007-10) which systematically identifies the major barriers faced by these groups. It also incorporates special measures and processes into these programs to help overcome these barriers. The

TABLE 1 RECENT MACROECONOMIC DEVELOPMENTS

	FY08	FY09	FY10	FY11	FY12	FY13
		Actual		Est	Projected	
Real GDP Growth at market prices (%)	6.1	4.9	4.6	3.5	3	3.4
Inflation (%)	7.7	12.6	9.6	9.5	9.2	8.3
T-Bills (91 days)	4.2	5.8	6.5	7.7		
Real interest rate (%)	-3.48	-7.37	-4	-0.67		
Investment (% of GDP)	21.9	21.4	20.2	18	21	21
Public	4	4.5	4.5	3.8	6.8	6.9
Private	17.8	16.9	15.7	14.2	14.2	14.2
Government Revenues (% of GDP)	12.9	14.2	15.2	15.4	15.3	15.7
Foreign Grants (% of GDP)	2.6	2.7	2.6	2.5	3.1	3.6
Current Spending (% of GDP)	11.2	12.9	12.9	12.8	13.5	13.5
Capital Spending (% of GDP)	6.2	6.9	7.2	7.3	7.5	8.2
Deficit after Grants (% of GDP)	2.1	3	2.5	2.1	3	2.9
Net Domestic Financing (% of GDP)	2	3	2.4	2.2	2.6	2.4
CA/GDP (%)	2.9	4.2	-2.4	-1.3	-1.5	-1.3
Remittance/GDP (%)	16.5	21.5	20.1	21.3	22.2	22.9
Trade Balance/GDP (%)	-18	-21.5	-26.4	-25.5	-26.2	-26.9
Gross Off. Res. (In mnths of merchandise imports)	11.3	6	5.6	5.3	4.7	4.1
PEER (2000=100, +=appreciation)	105	104.7	109	113		
GDP at market prices (in billions of U.S. dollars)	12.6	12.9	15.7	16.9	18.5	20.2

Source: NRB, MOF Economic Survey, and WB Staff Estimates

TABLE 2 SELECTED INDICATORS IN SOCIAL SECTOR

Indicators	1995-1996	Latest available
Headcount Poverty Rate	42%	31% (2003-04)
Gini coefficient	34.2	41.4 (2003-04)
Net primary enrollment	67.5%	94.5% (2010)
Gender Parity ratio in primary education	0.66	0.99 (2010)
Under 5 mortality rate (per 1000)	118	48 (2009)
IMR (per 1000 live births)	79	39 (2009)
Full immunization coverage	43%	83% (2006)

government has enacted several laws and policies such as a system of reservations in the CA elections and the 2007 Amendment to the Civil Service Act that included a 45 percent reservation in state structures for those from excluded groups and backward regions. Gender disparities in political participation are decreasing both in elected and administrative government. Women now make up over 30 percent of the representatives in parliament[15]. Implementation of an inclusion policy of women in the civil service shows positive trends.[16]

D. GON's Development Strategy

19. The Government's development strategy is outlined in an 'approach paper' for the Three Year Interim Plan (July 2010-June 2013). This plan has two major objectives - poverty alleviation and the establishment of sustainable peace through inclusive, employment-centric growth.

20. Given the transitory nature of Nepal's government, Nepal's basic development priorities have been identified as those acceptable to all major political groups. Based on policies and programs under successive governments since the political change in 2006, poverty alleviation, employment-centric growth, agriculture, infrastructure building, and social development are basic priorities for Nepal. All of these priorities require good governance and social inclusion which have received policy emphasis (although still very weak in practice) under all recent governments. Their annual budgets reflect this. The proposed ISN is consistent with these broad priorities.

KEY HIGHLIGHTS OF THE LAST ISN

IMPLEMENTATION AND LESSONS LEARNED

Development Results

21. Overall, good progress has been made in the implementation of the FY10-11 ISN. Despite challenging and uncertain operating environment and the prolonged stalemate on the political front, there have been successes in many areas and most projects are on track to achieve their development objectives and ISN milestones at end-FY11 were largely met (see Box 1 and Annex A).

22. Innovative approaches have been developed in some projects to address fiduciary weaknesses impacting project implementation. With support from the International Development Association (IDA), some institutions have demonstrated good skills for efficient procurement management; for example, the Department of Roads (DOR) has been a pioneer in the introduction of e-bidding, with the consequence that competition for contracts has significantly improved. Preliminary analysis shows that between FY08-09 and FY09-10, DOR made a net saving of roughly US$10 million per year. In the health sector, implementation of the procurement improvement action plan resulted in better quality bid documents and bid evaluation reports, and in an increase in the number of bidders, increased competition and lower costs. For example, the procurement of contraceptives attracted twice the number of bidders and led to a cost saving of US$137,250 compared to the previous year.

23. Progress in some other areas has been slow. Agreements on the framework for a sector-wide approach in rural roads and water and sanitation have been deferred due to local insecurity, weak country systems and lack of clarity regarding local responsibilities. Key bills dealing with the financial sector, power, economic zones and investment are pending in the CA. There has been limited progress on strengthening core public sector institutions and systems, in particular on public procurement monitoring and financial management. Key positions in the Oversight Agencies and the Government (e.g., Auditor General, all five Commissioners of the Commission for Investigation of Abuse of Authority) remain unfilled because of the political stalemate. Efforts to reduce the 16 hour load shedding gap during the dry

BOX 1 DEVELOPMENT RESULTS OF THE RAIDP AND PAF

The Rural Access Improvement and Decentralization Project (RAIDP) has improved access to markets, schools and health clinics in remote and rural areas of the country. The project has rehabilitated and upgraded 540 kilometers of existing dry-season rural roads to all-season standard. It financed maintenance of about 3,500 kilometers of rural roads, constructed 102 trail bridges, and developed small community infrastructure. A survey of five completed roads found an increase of more than 20 percent in motorized and non-motorized trips during the first year of operations. Similarly, travel time for road users was cut from an average trip time of 2.6 hours to 32 minutes.

The recently completed rigorous impact evaluation studies in mid-FY11 for the **Poverty Alleviation Fund** (PAF) show that this program has resulted in enhancing income and consumption levels. The evaluations indicate that 66 percent of households covered under PAF have obtained a minimum income increase of 15 percent (in real terms) and have achieved an average increase in income of 82.5 percent in real terms and 182 percent in nominal terms. PAF has covered 40 poorest districts, supporting 14,831 Community Organizations and 405,000 poor households, and has benefitted more than 513,000 households. Of the total number of poor households supported currently, 57 percent are Dalit and Janajati. The estimated net program impact on per capita consumption has also been positive and in particular, growth has been higher for Dalit and Janajati and for the poorer segments of the population, implying program's ability to distribute growth towards targeted groups. The impact on other welfare indicators is also positive and significant: 10 percent points decrease in incidence of food insufficiency and 6 percent points increase in school enrolment rate for children aged 5-15. The program's positive effect is also seen in access to services (agriculture centers, community forest groups, farmers' groups) and women's empowerment.

season have been unsuccessful. Also, stand-alone technical assistance operations have had very limited success.

Tools to Promote Accountability and Conflict Sensitivity

24. During the last ISN, the Bank committed to improving accountability and conflict sensitivity in its operations through the introduction of a Peace Filter, Governance and Accountability Action Plan and social accountability mechanisms. Progress on designing each of these diagnostic tools has been good; but implementation needs to be strengthened.

25. The last ISN committed to the use of a Peace Filter to improve the peace and conflict sensitivity of IDA-supported operations in this difficult and unstable operating environment. More specifically, the peace filter was intended to help task teams better understand the operating environment at both national and local levels, as well as possible drivers of conflict through a deeper analysis on institutions, stakeholders and benefit-sharing. Peace filter analyses have been conducted for all new projects in the current ISN period, as well as at the sector level, for energy, irrigation, natural resources and education. The filter was revised during the ISN period to map it to the Operational Risk Assessment Framework (ORAF) and customize it to the different project stages (identification, preparation, and implementation). Peace and conflict sensitivity training was also organized for WBG staff, government staff and donor partners to enhance understanding and awareness of conflict-related issues and how they can be addressed in the operational space. Findings from the peace filter analysis were translated into the design of new operations. For instance, the Kabeli Transmission Project incorporated a new rural electrification component to provide electricity to communities in the footprint of the new line, and the phasing of the Rani Jamara Kulariya Irrigation project was designed with local Water User Associations to minimize conflict at the local level. Implementation modalities for the rural roads project were designed to increase job creation at the local level.

26. Similarly, the introduction of the Governance and Accountability Action Plan (GAAP) process has been a requirement for all new projects. On-going projects with a substantial implementation period remaining were retrofitted with GAAPs to ensure governance sensitivity. The GAAP process starts with a detailed review of governance and corruption vulnerability challenges. A variety of measures are then identified for each operation that aim to strengthen the governance framework for project interventions, identify entry points for social accountability mechanisms, and establish transparency and right-to-information (RTI) arrangements. An example of a good GAAP is "Governance, Peace and Security Assessment" developed by the roads project team, which received an internal WB global award for delivering the most innovative and more broadly applicable approach to addressing governance and anti-corruption issues. Both the peace filter and the GAAP have led to an increasing focus on communications strategy and stakeholder analysis for the program, including for advisory activities.

27. During the ISN period, IDA also put increasing emphasis on promoting social accountability efforts as a way of doing business. Social accountability mechanisms have been designed in all new projects and strengthened in some ongoing projects (and have been incorporated in the GAAPs). Given the lack of elected local government, local citizens' groups become even more important as partners in monitoring program implementation and as demanders of good governance. The scaling up of social accountability mechanisms in the lending program is being complemented by the Program for Accountability in Nepal (PRAN – See Annex B), which was launched in November 2010 with the goal of strengthening civil society organizations in the area of social accountability.

Process Improvements

28. The principles underlying the strategy have been to keep the program simple and flexible. In order to keep our program simple, the Additional Financing (AF) instrument has been used effectively, sometimes combined with emergency

operations (Social Safety Nets, Power Development). For some other projects, a phased approach has been adopted (Rani Jamaya Kulariya Irrigation, Kabeli Transmission and proposed Kabeli Generation). Maintaining flexibility in our program has encouraged the teams to restructure some projects (Emergency Peace Support and Second Higher Education) and quickly respond to government requests for new un-programmed projects that fit within the overall strategic framework (Enhanced Vocational Education and Training, PAF II AF). On the advisory side, a financial sector contingency exercise was undertaken to respond to the emerging vulnerabilities in the sector.

Donor Harmonization and Aid Effectiveness

29. Donor harmonization and coordination has improved over the ISN period and new partnerships have been forged (see Attachment D). Donor heads meet every two weeks to discuss priorities and share information. A country-wide public consultation to inform our development partner strategies was conducted jointly by the ADB, the UK Department for International Development (DFID) and IDA. Coordination among development partners has focused on leveraging the comparative advantages of each partner. Joint work on education and health sector-wide approaches (SWAps) intensified with a focus to improve development results. In addition to IDA and DFID, a Joint Financing Agreement was signed by other SWAp partners for the health SWAp, including AusAID, GAVI[17], UNFPA, USAID, and WHO. This will reduce transactions costs to all parties due to the single fiduciary framework (including a single audit) that is being used. In the roads sector, programmatic analytical work is underway using a joint peer review process, with donors active in the sector, each taking the lead on an agreed priority theme for analysis. During 2010, the local donor community in Nepal, coordinated by the United Nations (UN), collectively drafted a "Peace and Development Strategy" with the goal of assessing the current status of the peace process, identifying peace and development linkages, and offering development community support in identified priority areas. IDA works closely with the UN and bilateral contributors to the Nepal Peace Trust Fund, to ensure coordinated support for conflict-affected groups and capacity building efforts. In a parallel initiative, the ADB and IDA have partnered to jointly address the challenge of public procurement reform. Similarly, nine development partners have formed a Public Financial Management (PFM) Donor Group to coordinate donor support for strengthening PFM systems and the accountability role of civil society and a PFM Multi-Donor Trust Fund (MDTF) was activated in December 2010. IDA has also worked closely with a variety of development partners over the ISN period to support the government of Nepal in its efforts to secure global funding for climate change resilience (PPCR), scaling up renewable energy sources (SREP), and food security and agriculture (GAFSP). The International Finance Corporation (IFC) works with various donors on its advisory projects such as climate resilience/mitigation, access to finance, investment climate reform and with lending agencies such as IDA, KfW, DEG and ADB for infrastructure and the financial sector projects.

Regional Integration and Global Initiatives

30. WBG is actively supporting Nepal's participation in regional and multilateral global initiatives. The Regional Wildlife Program[18], *Strengthening Regional Cooperation for Wildlife Protection in Asia*, is assisting participating governments to build capacity, institutions and incentives to collaborate in tackling illegal wildlife trade and other conservation threats to habitats in border areas. The *Nepal-India Electricity Transmission and Trade Project* will enable power trade through imports into Nepal as needed, and eventually, export of surplus power to India. In the non-lending areas, IDA is channeling support to Nepal from the regional programs like the South Asia Water Initiative (SAWI) and the South Asia Food and Nutrition Security Initiative (SAFANSI). IFC is enhancing regional integration through investment activities, such as trade finance facilities for local banks and advisory activities, such as investment climate strengthening and trade facilitation. Nepal is also part of IFC's SME Venture Fund global initiative which focuses on eight high-risk IDA countries. In addition, IDA and IFC plan to collaborate on two new tentative programs, IDA's North Eastern Region Trade and Transport Facilitation Program

(NER T&T) and IFCs planned South Asia Regional Trade and Integration (SARTI) program. Trade facilitation work by IFC includes assisting governments to build efficient trade logistics systems and services through targeted reforms aimed at reducing the time and cost for the private sector to import and export. IFC's trade logistics reform work relies on a strong private sector partnership approach to identify issues and validate results.

31. At the global level, Nepal is the only country in the world that has been selected to participate in two Climate Investment Fund (CIF) Pilot Programs – the Scaling Up Renewable Energy Program (SREP) and the Pilot Program for Climate Resilience (PPCR). Both these CIF programs involve joint design and implementation by the ADB, IDA, and IFC, as well as collaboration with other donors (such as DFID, Denmark, the United States) to ensure complementarity with local programs.

IDA-IFC collaboration

32. Nepal has been selected as a pilot country to implement an enhanced joint strategy to leverage IDA and IFC resources and realize synergies. Building upon co-located offices and staff, IFC and IDA work together closely, particularly in the areas of financial sector, i.e., e-payments, infrastructure, hydropower, climate change, and business enabling environment (see Annex C). In hydropower, IFC and IDA are working together to support the Kabeli hydropower project (37MW). The IDA-IFC joint work on climate change ensures an approach that reinforces both public sector and private sector involvement through the PPCR and SREP. IDA's assistance on macroeconomics, financial sector, and governance fronts facilitates IFC's investments and advisory work, especially the support for investment climate reform. IFC's investment climate work, in turn, reinforces better public service delivery for businesses by creating stronger institutional mechanisms to support private sector development through the Nepal Business Forum (NBF). IFC would also continue to complement other ongoing donor support on Public Private Partnerships (PPP) and to provide the WBG a unique capability to focus on Nepal's private sector development.

IDA Portfolio

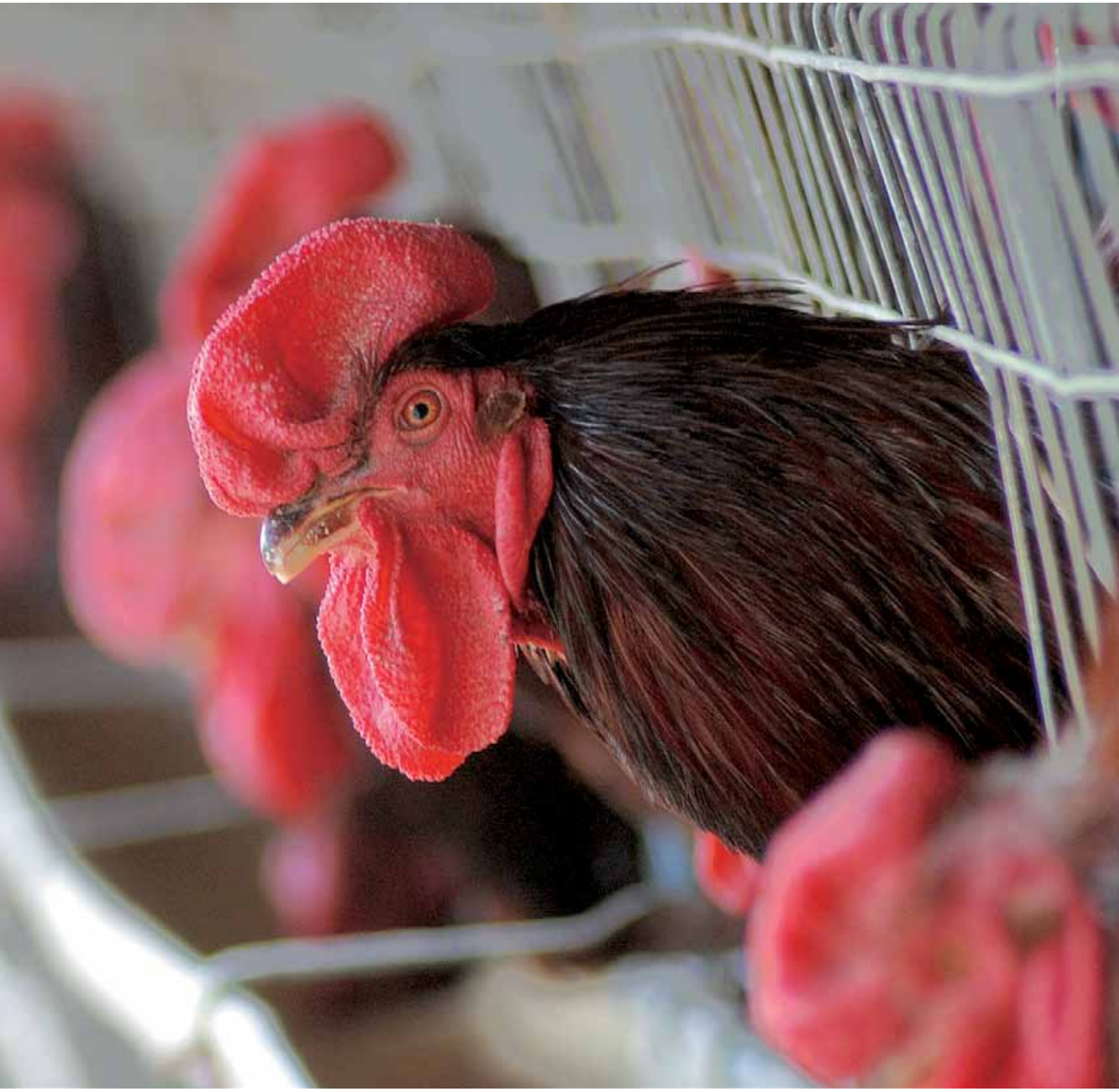
33. As of end-June 2011, Nepal's portfolio includes 19 IDA operations (two of which are regional projects) and 9 active trust funds, with a net commitment value of US$1.3 billion[19] and US$142.1 million, respectively. US$238 million was disbursed in FY11 out of Nepal's opening undisbursed balance of US$711.76 million, representing a disbursement ratio of 33.4 percent. Three projects (18 percent) found themselves in problem project status, representing about 16 percent of net IDA commitments. Overall, the uncertainties of the transition, combined with generally low institutional capacity, weak systems of governance and accountability, rugged topography, and a diverse socio-cultural mosaic, all make implementation challenging. Physical security remains a concern in some areas. Continuous implementation support from the country office has facilitated the acceleration of implementation rates in the second half of the FY, which has made possible the strong disbursement performance in FY11.

34. To address project implementation problems, targeted restructurings and partial cancellations are being undertaken and have contributed to improved performance. Intensive implementation support through continuous dialogue by field-based teams has moved projects out of problem status in the past. Such pro-activity has contributed to improve project quality in this difficult operating environment. During the past years, the Nepal Country Office has strengthened its technical capacity to implement analytical activities and operations (64 percent of Nepal task team leaders are field-based). In addition to the annual Nepal Portfolio Performance Review (NPPR), semi-annual portfolio review meetings chaired by the line ministry are also conducted. Joint portfolio reviews with the ADB are under discussion at the sector level to enhance coordination, reduce transaction costs for the Government, and promote cross-agency learning.

IFC Portfolio

35. IFC's committed investment portfolio in Nepal stood at US$28 million as of June 30, 2011, consisting of power, transport, banking, microfinance, tourism, and trade finance lines. IFC invested in 11 projects (for US$29 million

KEY HIGHLIGHTS OF THE LAST ISN IMPLEMENTATION AND LESSONS LEARNED



in total) in FY09 and FY10 and six projects (for around US$12.6 million in total) in FY11. IFC activity after being low during FY2002-07, picked up after the peace agreement was signed in November 2006 and IFC re-opened its office in January 2008. This led to IFC's investment of US$10 million in a local airline in August 2008.

36. On the investment side, IFC has prioritized on financial sector and infrastructure in Nepal. IFC's investments include shares in two hydropower projects and, most recently, expansion of a hydropower project, an airline expansion, and investment in a Nepali microfinance institution which were IFC's first support to the sectors in ten years. In addition, IFC has supported technology companies and trade finance in a number of commercial banks. However, investments in Nepal, including for IFC, are constrained by a challenging regulatory and legal framework for foreign investment, poor governance and accounting practices, weakness in the domestic banking sector together with lack of a swap market for the Nepali Rupee, poor implementation of property rights, and heightened political uncertainty. In addition, country's logistical limitations, absence of supporting infrastructure and the relatively smaller size of projects constrain investments, especially in the manufacturing sector. Domestic supply side constraints, especially the lack of reliable power supply and high cost of credit, have also accentuated the sluggishness in private investment. Indeed, in the five years to 2009, net FDI in Nepal averaged only 0.1 percent of GDP as compared to an average of 1.9 percent for low-income developing countries. Regulatory constraints such as inadequacy or absence of competitive bidding to award infrastructure projects and the lack of an adequate framework and limited capacity to conceive, implement and monitor PPPs have limited IFC's PPP transaction advisory work in Nepal.

37. On the advisory services side, IFC is engaged broadly in four areas, including investment climate, access to finance, sustainable business advisory and PPP advisory services. On the investment climate, IFC is working towards creating new jobs, attracting investment and improving the overall growth environment, despite the difficulties. IFC sees this post-conflict period as a strategic time to assist the country and is working with the Government, development partners and the private sector to leverage opportunities for private sector-led growth. Through its Nepal Investment Climate Reform Program (NICRP), it has embarked on a three-pronged approach of reforming the regulatory environment, creating and supporting the NBF and assisting with the establishment of Special Economic Zones (SEZs). The three year NICRP is funded through contribution by DFID-Nepal (US$7.25 million) and South Asia Enterprise Development Facility2 (SEDF2) core budget (US$750,000). IFC's financial markets advisory work – Access to Finance (A2F) – focuses on financial infrastructure, sustainable energy financing (SEF), SME lending, microfinance, credit information bureaus, secured transaction registries, e-payment and support to long-term lending institutions. Under its Sustainable Business Advisory (SBA), IFC is providing support to enhance the ability of SMEs and farmers to increase revenues and expand access to markets by strengthening their management capacity (financial literacy, business acumen) and technical skills (farmer productivity). Currently, IFC is executing the Poultry Supply Chain Strengthening project which works with SME farms and two lead firms in the poultry sector. IFC is also a partner in the two climate change projects, PPCR and SREP in partnership with IDA and ADB. IFC is working with local financial institutions to set up a new locally managed fund by end FY12 to support the SMEs in Nepal. This would be part of SME Ventures, a new IFC Fund that provides a combination of investment products and advisory services to entrepreneurs. Due to constraints noted above, IFC's PPP transactions advisory work in Nepal has been limited.

MIGA Portfolio

38. MIGA's gross exposure in Nepal is US$29.4 million, all in the hydro-power sector. MIGA has not underwritten any new investments since 2001, but is seeking new investments to support. MIGA financially supports FIAS with their investment climate work in Nepal.

Interim Strategy Note for Nepal
FY12-FY13

PROPOSED WORLD BANK GROUP **STRATEGIC PRIORITIES AND PROGRAM** FY2012-2013

39. The World Bank Group will continue to be more selective in terms of its interventions in the context of the underlying political climate, IDA's comparative advantage vis-à-vis other development partners, constraints on administrative budget and resource (IDA) availability. Additionally, the ISN proposes to maintain other principles underlying the previous ISN: aligning the strategy with broad country priorities, harmonizing with donors, building on IDA and IFC's comparative advantage, designing community based interventions where possible, and keeping the program simple and flexible. Regarding selectivity, IDA will disengage from lending in some sectors (see Table 3). The ADB, IDA and DFID have agreed on those subsectors where all are active, one takes the lead or some of us withdraw. This process is being extended to the UN and other bilateral agencies as well. At this stage, the ISN does not foresee development policy credits. IDA will also not be engaged in peace operations involving security sector reform or any financial packages for ex-combatants. The important area of private sector development will be taken up by the IFC leading on improving access to finance and investment climate. The Bank and IFC expect to work together on power development and agriculture. And, the IMF is likely to play a larger role in the financial sector and macro-economic management. This strategy would maintain IDA's interventions in the following 7 areas, down from 13 areas during the last ISN: power, roads, agriculture, education, health, urban, and food and livelihood vulnerability. An eighth area of climate change and disaster management will be supported through trust funds that have already been mobilized under the CIF and Global Facility for Disaster Risk Reduction (GFDRR).

40. Based on the country needs and the underlying economic situation, IFC proposes to be selective in its engagements. IFC will continue to place emphasis on infrastructure, financial and transportation sector. Within infrastructure, the focus will remain on hydropower and renewable energy. In hydropower, IFC will initially continue to consider medium sized (10-50 MW) projects for the domestic market while large export oriented projects will be supported over the long run once the transmission line networks are available and can support export of power. Sectors like telecommunication are likely to be engaged in after evaluating individual opportunity. In the financial sector, IFC aims to focus on improving access to trade finance and explore possibility of extending credit lines to local banks. Supporting commercial banks with equity investments can also be considered thereafter. On PPP, IFC will look forward to initially supporting project implementation through transaction advisory services and subsequently providing funding if required. However, it would be important to leverage this with core strengths of the donor partners to develop a framework for undertaking PPPs. On the non-lending activities, IFC's Sustainable Business Advisory (SBA) will continue to adopt the lead firm approach. In addition, IFC's advisory work will continue to be based on cost sharing mechanism which further adds to IFC's selectivity in the country.

41. The 2011 World Development Report (WDR) on Conflict, Security and Development provides valuable insights and lessons for working in fragile states. As a country still emerging out of a violent conflict, Nepal could

TABLE 3 IDA SELECTIVITY CHOICES

FY10-11 ISN Activity	Projects/AAA	Comments	Proposed Strategy
GON Economic reform TA operation	Closed	Not continued	No stand-alone TA operation; ongoing WB analytical support
Financial Sector TA operation	Closed/to be closed	Not to be continued	IMF/IFC + WB monitoring + contingency support option
Telecommunication	Closed	Not continued	ADB
Judicial Reform IDF	Closed	Not continued	DFID
Private Sector Dev.	ICA	No project anticipated	IFC leading with WB analytical support
Avian Influenza	To be closed	Not to be continued	UNICEF
Peace Support	To be closed in FY12	Not to be continued	Bilateral donors, UN, EU, WB EVENT Project (training)
Rural Water & Sanitation	To be closed in FY13		Agreed exit strategy needed

PROPOSED WORLD BANK GROUP **STRATEGIC PRIORITIES AND PROGRAM** FY2012-2013

adopt much of the WDR framework. Having said this, it is important to note upfront that although Nepal went through a decade-long conflict, it is not a standard post-conflict/ fragile country that experienced a substantial breakdown in institutions. Even as the conflict was ongoing, the basic Nepali public sector apparatus continued to function, the macro-situation never spun out of control, and social indicators and poverty conditions actually improved.

42. Nevertheless, many of the principles of engagement proposed by the WDR are relevant for Nepal: enhancing political and economic inclusion, delivering early results to build public trust and confidence, focusing on social accountability tools, applying community-driven approaches, and strengthening institutions in a phased approach. The ISN encompasses all these principles with governance and accountability and gender equality and social inclusion being cross-cutting themes. The three-year capacity building program, PRAN, aims to enable practitioners from both civil society and government to promote improved governance and public service delivery through the application of social accountability approaches and tools. PRAN is initially focusing on promoting social accountability in three priority areas: public financial management, municipal governance, and public service delivery where some early gains can be achieved.

43. Community-managed/driven (CMD) development will continue to be an effective mechanism for IDA to deliver services in this fragile context. Nearly half of IDA's investment program in Nepal is delivered through various forms of CMD programs. These mechanisms have been resilient despite weak governance in the central and local state institutions, a contentious political transition, a history of prolonged insurgency in the rural areas, and the challenges of remoteness arising from Nepal's difficult terrain. The CMD mechanisms have been found to be robust, well-targeted and are successfully delivering services to communities. This ISN continues to build on the success of CMD programs (see Box 1), both in terms of delivering quick results and for contributing towards peace-building activities. In this context, the ongoing multi-sectoral PAF will be the key instrument of engagement and will continue to support community level institutions and strengthen its outreach to vulnerable communities for delivering basic services and livelihood support.

44. At the portfolio level, IDA will explore opportunities to build specific linkages with other sector-specific CMD projects to help meet the development objectives of the overall program. During the last ISN period, the country team adopted a portfolio-wide approach to manage the CMD portfolio by using AFs and SWAps, which allowed the program to concentrate on developing a relatively narrow range of higher quality programs and then ensuring sustained support. Nevertheless, in communities with multiple interventions, there is insufficient coordination across projects. This calls for a more integrated approach to community engagement across multiple projects to encourage synergies. In a way, this collaboration has already started with the ongoing Power Development Project which supports micro-hydropower and is working with the PAF at the field level to explore ways to increase the daytime use of electricity for income-generating activities. We see similar opportunities to increase linkages with other CMD projects which are delivering roads, irrigation, health, education, and social protection. The ongoing geo-coding of projects will further strengthen these linkages.

45. Nepal's transition from conflict to peace has program implications for all development partners. On the program side, the WDR's top three priorities include citizen security, justice, and jobs. The WDR notes that *"electricity, literally the most "visible" of all results, can be critical for progress in security and job creation"* [20]. Improving the power situation is one of the key focus areas of the ISN as discussed under pillar 1. In Nepal, delivery of basic services and infrastructure has been repeatedly cited as the key "peace dividend" that citizens want. WBG will continue to engage in the delivery of education, health, roads, power, etc. which are so important to the poor communities. Migration is one of the key conduits for job creation in Nepal – about one-third of the male workforce works outside the country and about 300,000 people migrate per year. The *Enhanced Vocational and Training Project (EVENT)* will focus on training youth, with

a focus on disadvantaged communities and women. Support to the agriculture sector will help create jobs and improve incomes in the rural areas. With IDA's increasing focus on selectivity and comparative disadvantage in the areas of security and justice, these are being supported by other donors as outlined in Table 4. The ongoing IDA-supported *Peace Support Project* will close in FY12. Once the constitution has been enacted and greater clarity is achieved, other development partners might increase their support in these two areas, at the local as well as at the national level. Given that social exclusion was one of the root causes of conflict in Nepal, IDA's engagement to promote social inclusion across its entire program can be seen as a contributing factor towards promoting social justice.

46. Implementation of the peace filter and the GAAP will continue. While recognized as a useful tool, the peace filter is being revised to reduce overlap with the GAAP tool and to enhance conflict sensitivity. The GAAP experience over the previous ISN period has improved awareness of governance risks, mitigation possibilities and the definition of actions to be taken when these risks materialize. The broad interests and various initiatives among development partners on conflict and governance analysis for operations will be shared and coordinated wherever possible.

TABLE 4 DONOR SUPPORT FOR PEACE BUILDING, JUSTICE, AND SECURITY

Donors	Peace-building[1/] (US$ million)	Justice, Security, and Human Rights (US$ million)
Asian Development Bank	4.5	-
Canada	6.7	4.4
Denmark	0.3	10.7
European Union	12.2	1.7
Finland	7.3	-
Germany	9.0	-
Norway	9.6	-
Switzerland	-	-
United Kingdom	4.0	9.3
USAID	-	41.0
United Nations	-	0.8
World Bank Group	28.5	-
Total	**82.1**	**67.9**

1/ Including army re-integration, rehabilitation of the conflict-affected, elections, etc.

47. The ISN concept served as an input to IDA's 2011 South Asia regional strategy. The strategy focuses on selectivity based on client demand, possibility to leverage results (especially in terms of MDGs), and opportunities for regional integration. Cross-cutting issues such as governance, inclusion, and gender equality will be emphasized in all IDA operations. For Nepal, this means that IDA will engage in areas for delivering transformative projects in power, trade and transport, advisory services support on climate change adaptation programs, nutrition, and roads. Results-based operations such as bridge repair and skills development will also be supported.

48. IFC's program in Nepal will seek to design and implement programs aligned with the three strategic pillars of IFC's regional South Asia Strategy which include: (i) promoting inclusive growth through emphasizing the base of the economic pyramid, rural areas, infrastructure building, and improving access to finance for MSMEs; (ii) addressing climate change through mitigation and adaptation, including renewable energy and energy efficiency investments and projects which focus on cleaner technology; and (iii) supporting regional and global integration through intra-regional trade facilitation, South-South investments, transport and logistics, investment climate and inclusive business models. These strategic pillars are inter-related and consistent with those proposed in the ISN.

49. Together with its advisory business, IFC aims to create positive impact on private sector development through: (i) financial sector and infrastructure development; (ii) improved access to finance, including for MSMEs; (iii) reduction of the private sector's carbon and environmental footprint; and (iv) regional and global integration. In the financial sector, IFC aims to focus on facilitating improved access to trade finance and explore the possibility of extending credit lines for hydropower sector to local banks to meet both short-term and long-term commitments. IFC will also explore supporting commercial banks with equity investments. Within infrastructure, IFC is focusing on renewable energy and hydropower. IFC will continue to look at medium-sized power projects (10-50MW) for the domestic market and

large export-oriented projects over the long run and will seek to complement IDA's support for transmission wherever there is role for the private sector. IFC will also work towards improving access to climate-resilient technologies and reducing market barriers that prevent the private sector from playing a key role in building climate-resilient communities. On the advisory side, the ongoing projects (noted in the portfolio section) are expected to continue.

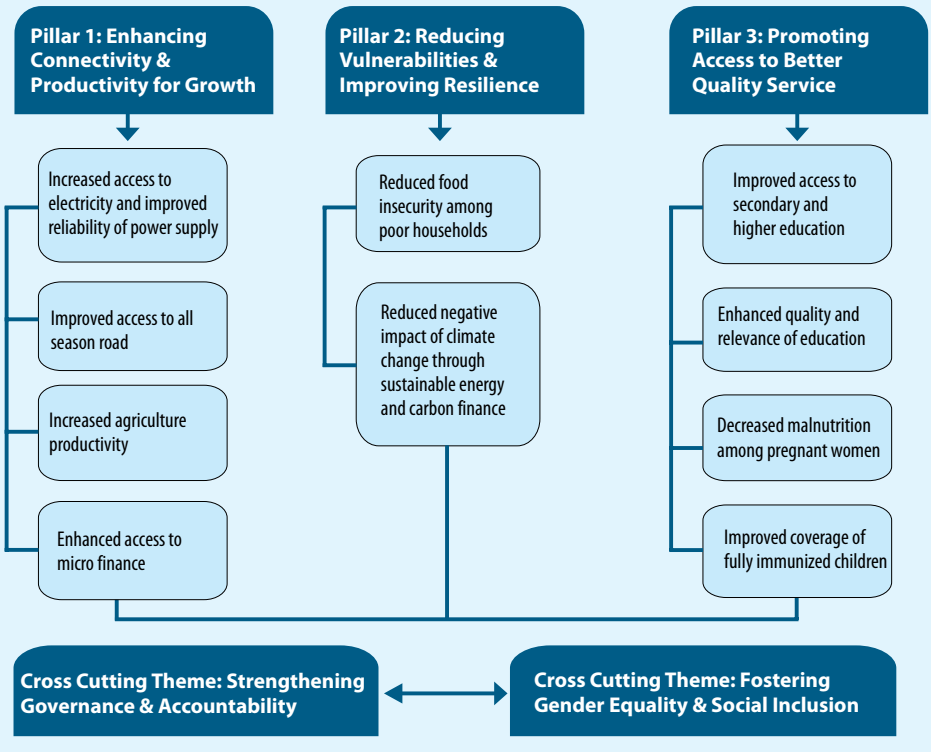
A. Proposed Pillars and Cross-Cutting Themes

50. The ISN will continue to pursue the overarching goal of supporting the GON to build a peaceful, prosperous and just Nepal. This ISN proposes two cross-cutting themes: (i) governance and accountability, and (ii) gender equality and social inclusion. The three pillars include: (i) enhancing connectivity and productivity for growth; (ii) reducing vulnerabilities and improving resilience and (iii) promoting access to better quality services. This marks a small change from the previous ISN. Governance used to be a separate pillar but now is a cross-cutting theme to reflect that it is being mainstreamed in all our projects. Gender equality and social inclusion considerations also permeate all of our operations. Enhancing connectivity and productivity reflects our commitment to address some key bottlenecks to growth. Nepal's vulnerability to food insecurity, climate change and disasters is increasing, requiring some immediate action and access to better quality services such as education and health remain key needs (see Figure 1).

Cross Cutting Theme 1: Strengthening Governance and Accountability

51. Nepal's current transition to peace and democracy has been marked by political instability. Coalition governments of the recent past have had to struggle to show 'unity of purpose' in the functioning of key state institutions. This has contributed to weakening of the legislative branch, with

FIGURE 1 NEPAL ISN STRATEGIC AREAS AND OUTCOMES



implications for the timely passage of laws and the budget, as well as its ability to perform key oversight functions. Frequent changes of government with concomitant rotations at lower levels have weakened certain ministries' financial management and procurement capacity. In addition, key institutions of accountability (i.e. Auditor General, CIAA) are under-resourced with vacant leadership positions.

52. Governance in Nepal has grown weaker. Three priorities for governance reform include: (i) a political settlement to promulgate the Constitution and ensure peace, (ii) the strengthening of state and non-state institutions at all levels, and (iii) assurance of the effective delivery of public services. But this is a long-term agenda and will take time. It is only after the passage of the new Constitution that the restructuring of state institutions could start in earnest. The strategy to support these changes would involve creating internal demand for institutional change, identifying opportunities to work with particular organizations offering potential for positive change, and promoting inclusive public policies. The ISN will support some immediate activities in the shorter term to show quick results and create momentum. For example, state-society relations need more attention, and the provision of basic services should improve. Checks against corruption and dissipation of public resources for vain and unproductive activities are long overdue.

53. The long road to promoting a sustainable peace lies in strengthening the overarching governance framework in Nepal—facilitating citizen voice, eliminating centuries of discrimination and bias among groups in society, building political and administrative institutions and processes, and promoting transparency. Necessary elements include effective institutions of accountability, sound systems of public sector financial management, procurement, and auditing, systematic performance monitoring and impact evaluation, and fair and accessible dispute resolution and legal services. These are long term changes, and it is unlikely that there will be substantial improvements in the above areas within the time frame of the proposed ISN. But maintaining the momentum and engagement and realizing incremental improvements in areas where IDA has already had a presence, such as public financial management, procurement, and social accountability, will be actively pursued.

54. Depending on progress in the new constitution, Nepal will face a significant challenge of restructuring the state within a federal set-up. The restructuring will have to be accomplished gradually within a well-conceived transition management plan. IDA will engage in this area, but the specific form of engagement will be based on the needs identified by the Government as it proceeds with the restructuring agenda.

55. Governance and accountability cut across all three ISN pillars and will be mainstreamed throughout IDA's program. In addition, IDA and IFC will support specific interventions to improve the overall governance in Nepal. In this regard, the key areas of focus for IDA will be: (i) strengthening institutional capacity in public financial management and procurement within the government agencies, and (ii) promoting social accountability. A PFM MDTF has been launched to improve program effectiveness and accountability. It aims to support strengthening (i) public financial management systems; (ii) demand-side initiatives from citizens to monitor government; and (iii) third-party results monitoring. Strengthened government systems are a prerequisite for some bilateral development partners to put more of their funds through the government. This will be complemented by the PRAN initiative.

56. IDA will also work with the Government to improve the quality of governance in all of its projects and programs. Major tools for this will include the GAAP, political economy analysis of change and reform, institutional assessments of selected programs, and the peace filter. Effective M&E systems and results management will also be supported. In view of Nepal's poor performance in implementing public policies, IDA will work with the government to put some standards of good governance into practice. These include non-lending technical assistance (NLTA) for RTI, anti-corruption, social accountability, and inclusion.

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57. These efforts will be complemented by IFC's Regulatory Reform project (NICRP) and access to finance initiatives which aim to encourage good corporate governance; improve productivity, competitiveness and enhance investment and trade activity along with a broader set of regulatory issues. IFC continues to work to raise awareness and encourage improved practices by bringing together listed companies, banks and stock exchanges. Better corporate governance in the private sector, followed by IFC investments has a powerful demonstration effect.

58. IDA will provide support to improve municipal governance, including municipal services, through its Emerging Towns Project. In addition, IDA-funded activities at the local level will be better linked to local government plans and programs. Our local government strategy will be defined after government actions are taken (see Box 2).

59. IDA is continuing to help strengthen governance and accountability in the financial sector. NRB's liberal bank licensing policy and limited supervision capacity encouraged banks' lending to the real estate and risk taking behaviors. Due to the NRB's past actions to curb speculative lending and to the banks' own liquidity shortages (as credits rose faster than deposits), lending into the real estate has slowed, lowering asset prices as well. Financial institutions that have taken risks and have high real estate exposure may now face deteriorating portfolio quality. IDA will continue to assist NRB by maintaining a close policy dialogue to enhance forward-looking supervision and to establish a framework for bank resolution, as needed. IFC complements this by promoting corporate governance among banks.

60. Finally, it is important that public investment programs are appropriately prioritized and efficiently implemented. Effective use of the Medium-Term Expenditure Framework (MTEF) is essential, for which continued NLTA support will be provided. And, strengthening the oversight of these projects by independent, professional government agencies is critical.

BOX 2 THE WORLD BANK AND LOCAL GOVERNANCE IN NEPAL

While broad agreement to move Nepal to a federal system exists, tremendous uncertainty about timelines, the shape of federalism, the number of states and boundaries, intergovernmental structures, and how "transition" will be rolled out institutionally and politically remains. This transition is still underway and is a source of potential unrest and instability.

Once key decisions have been finalized, implementation needs will be substantial. This will include restructuring intergovernmental relations, establishing new institutions at different levels of government, reforming the ways in which services are managed by the local public sector, and establishing modalities to absorb citizen voices in the planning, management and oversight of public resources at the local level. This change will be incremental, perhaps in fits and starts, and subject to episodic reversals. Postponing action for that perfect order to emerge is not an option. In the interim, the government and its development partners need to work with the shifting political and socio-economic trends to outline a working strategy on decentralization and localization, while not losing sight of the longer-term vision of federalism and state restructuring.

The move to federalism and a new system of local governance provides both a challenge as well as an opportunity for IDA's operations in Nepal. Our operations will be affected in the medium to long term. While our current program interfaces with the local state in numerous ways – through our support to community development programs and support currently being designed for a few small urban local governments, given the uncertainty of how transition to a federal structure will take place, we will continue to focus attention on developing linkages between our projects and local government wherever possible.

At the same time, IDA will take a proactive role in providing strategic support to policy and institutional reforms on federalism through "just-in-time" support to policy makers on the transition agenda including sharing experiences on intergovernmental transfer systems and technical and capacity building support to ministries and sectors to enable them to plan and manage this institutional transition. Modeling institutional scenarios for the new state and supporting sectors to design strategies and approaches to decentralization that will lead to more effective service delivery will be critical aspects of IDA support to Nepal during the ISN period.

Cross Cutting Theme 2: Fostering Gender Equality and Social Inclusion.

61. The government has placed gender and social inclusion as a priority area on its development agenda. Since the promulgation of the Interim Constitution in 2007, a number of laws and policies have been enacted to promote social inclusion in the country. Despite these positive developments, there is still a significant gap between policies and their actual implementation on the ground. High-caste hill Hindu males continue to dominate Nepal's political and administrative apparatus despite the diversity that the CA embodies. Similarly, the hitherto-marginalized groups continue to experience discriminatory practices in terms of access to resources and services like in health and education as a result of which the prevalence of poverty is higher among these groups. Furthermore, women across the board are more underprivileged than their male counterparts. Women migrant workers joining overseas jobs has doubled (in the last three years) to an estimated 70 per day in the fiscal year 2009-10. 147,000 Nepali migrant women have been documented as working overseas; unfortunately harassment and abuse of these women is common.

62. The recently completed "Peace and Development Strategy" by a group of development partners in Nepal also notes the importance of gender equality and social inclusion in programs and projects. Over the last few years, donors have provided targeted support for poor and socially excluded groups and made efforts to promote greater diversity in their own programs. Many innovative programs, such as the PAF (supported by GON, IDA and IFAD), have reached out particularly to women and dalits. The report, "Unequal Citizens: Gender, Caste, and Ethnic Exclusion in Nepal", prepared by IDA in partnership with the NPC, DFID, and the ADB, has been key in influencing government and donor agencies' policies and strategies on social inclusion. This is consistent with IDA's commitment to gender equality at the corporate level.

63. The post-conflict environment offers an opportunity for Nepal to actively promote social inclusion and equitable access to all its citizens irrespective of their income level, gender, location, caste and ethnicity. In the backdrop of these developments and the gaps that currently exist, there is substantial scope for IDA's engagement to actively promote gender and social equality as well as inclusive development in Nepal through its operations and advisory activities. Inclusive development will not only help sustain poverty reduction, but also help address one of the root causes of the conflict in Nepal. Fostering trust between Nepal's diverse[21] and excluded groups will be a critical building block to restore the legitimacy of the state.

64. IFC plans to work with both microfinance banks and wholesale microfinance institutions (MFI) and on e-payments to improve access to credit and to scale-up operations to hilly regions and to increase the outreach to under-banked and underserved populations. Support to MFIs will also help improve access to finance for women as majority of their clients are women. Advisory service projects will involve new product development, strengthening risk management capacity and launching mobile banking as a delivery channel. In addition, IFC plans to help increase investment and create jobs though economic zones to be set up across the country by the Ministry of Industry. International evidence suggests that more than half of the new jobs created in SEZs generally go to women.

65. Preliminary results from an ongoing internal IDA review of the gender portfolio indicate that while gender considerations are an important component of community development and human development projects, they are not so in others. Even then, in most projects, women are viewed only as project beneficiaries and little effort is made to address the structural barriers that prevent them from accessing services and/or exercising effective participation and decision-making roles. In addition, the initial findings also suggest significant gaps between government policies, awareness of those policies within both IDA and the government, and the capacity of the government to implement those policies.

66. IDA will help the government implement its commitments as well as enhance its capacity to address

the social development challenges in Nepal. More specifically, IDA in collaboration with other development partners and civil society organizations, will engage with government counterparts to develop the capacity of key sectoral ministries and implementing agencies by raising awareness of *Gender Equality and Social Inclusion (GESI)* policies. This will be largely through information dissemination, and encouraging compliance with existing laws through its policy advisory role and specific operations. The simultaneous support to the government and incorporation of GESI framework into IDA's own operations may help to ensure that GESI strategies become embedded as part of Nepal's national systems in the future. IDA will incorporate gender and social inclusion agenda in future lending and monitor gender impact during project implementation. On the analytical side, the ongoing Poverty Assessment will pay particular attention to gender issues.

Pillar 1: Enhancing Connectivity and Productivity for Growth.

67. The first pillar of the strategy aims at supporting GON's efforts to improve connectivity and productivity for growth in some key sectors. Creating an enabling environment for inclusive growth can create jobs and reduce poverty, thus alleviating one of the root causes of conflict. This is important but very difficult to achieve under current circumstances. Since the most important impediments to increased investment and growth – political instability, delayed conclusion of the peace process and poor law and order conditions – depend on the political leadership's actions, we have focused on those areas where the WBG can make a difference even under such conditions. These include: (i) alleviating infrastructure bottlenecks in energy and roads; (ii) improving agricultural productivity through better irrigation schemes and (iii) establishing a better enabling environment through advisory activities, public-private dialogue, and direct investments to support private sector activities and access to finance. Underlying these activities is the need to maintain fiscal and financial sector stability. IDA will continue an active monitoring program and provide advice as requested on key macroeconomic and financial sector issues.

68. IDA will continue to provide its support to improve energy access and reliability of power supply during the ISN period. Poor reliability and access to power are the most serious infrastructure bottlenecks to growth. The power sector was cited by the ICA survey business respondents as their most critical constraint after law and order concerns. Increasing access to electricity in a timely and cost-effective manner is one of the most significant development challenges facing Nepal today. The total grid-connected generation capacity amounts to a meager 683MW as compared with the annual peak demand of 900 MW which is reached in the winter; this is why Nepalis face load-shedding up to 16 hours a day in the dry season. IDA will continue to provide financing through the components of the three ongoing projects – *Power Development, Kabeli Transmission,* and *Second Poverty Alleviation Fund* – directly aligned with this energy outcome measure. It will focus on increasing electricity service coverage in rural areas through micro-hydro schemes through a community-based program which has proven to be effective. In addition, IDA will continue to support rehabilitation of existing generation capacity through the ongoing *Power Development Project*.

69. Ironically, Nepal has one of the largest untapped hydropower resources in the world – an estimated 83,000 MW of hydropower potential and is surrounded by two of the fastest growing, energy-hungry countries in the world. And yet, no large hydropower projects have been constructed to date. Significant private sector participation in generation could be mobilized, but given the current political uncertainties, private investors would need high risk premia and so sizeable investments may not be expected in the near future without guarantees or government support. In the immediate term, IDA, along with IFC, will provide support to the proposed 37MW *Kabeli 'A' Hydroelectric Project*. IDA is also supporting cross-border domestic transmission linkages through the *Nepal-India Electricity Transmission and Trade Project*. Being a land-linked country, Nepal will benefit from increased transmission interconnections with India as these lines will enable power trade through imports into Nepal and, eventually, when sufficient generation capacity is built in Nepal, through export of surplus power to India.

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IFC has existing investments in private hydropower projects – representing 16 percent of installed capacity – and plans to expand its hydropower portfolio in Nepal. IFC will also invest in the 30MW *Nyadi Hydropower Project* during the ISN period. The WBG is working closely with the ADB and other development partners active in the power sector. In the foreseeable future, however, power shortages will continue to hamper economic development in Nepal. So IDA is also promoting alternative energy activities such as micro-hydropower and biogas through scaling-up of on-going renewable energy initiatives. In the context of SREP, IFC expects to support small hydropower projects through credit lines to local banks. In addition, IDA will continue to implement various non-lending activities funded by ESMAP and other trust funds, and IFC plans to explore the regulatory impediments to increased private sector investments in hydropower in Nepal.

70. IDA will support selected interventions that will have long lasting effect on increasing access to road network in Nepal. Poor physical connectivity has been another major challenge to Nepal's development efforts. Its road density is one of the lowest in South Asia[22]. There also exist geographical disparities in the availability of roads[23]. Over one-third (36 percent) of the people in the hills are more than four hours away from an all-weather road. In addition, 15 out of 75 district headquarters are yet to be connected by a road. The quality of the road network is also poor – 60 percent of the road network, including most rural roads, cannot provide all-weather connectivity, and roads to the nation's production/consumption centers are grossly inadequate and unable to support even the current level of economic activities. Maintenance is a seriously neglected issue. The existence of many gaps on completed roads, coupled with the poor quality of existing bridges on them, further limits the prospect of providing universal physical access.

71. The Government has formulated a priority investment plan with an objective to improve investment efficiency in the roads sector. Two ongoing IDA-supported projects, *Road Sector Development and Rural Access Improvement and Decentralization*, will contribute towards improving all season road networks to increase access and reduce travel time. The projects focus on rehabilitation and upgrade of existing roads and construction of new roads and small bridges both in the targeted rural and non-rural areas. In addition, further support will be provided for bridge repair and maintenance through the proposed *Results-Based Bridges Project*. Also, IDA plans a regional investment operation to complement the ADB's efforts to improve Northeast trade and transportation linkages through Bangladesh. On the analytical front, the ongoing multi-donor *Road Sector Assessment study* will be completed.

72. Improving irrigation schemes is crucial to increasing agricultural productivity. Nepal is a predominantly agrarian economy characterized by low productivity with inefficient irrigation systems. Given that productive agriculture is a crucial element of inclusive growth, enhancing the efficiency of irrigation systems will continue to be critical to increase agricultural productivity, incomes, and rural livelihoods. Studies have shown that poverty incidence is much lower in irrigated than rain-fed areas and that access to irrigation reduces the severity of poverty. IDA will continue to support development of traditional farmer irrigation systems owned and managed by the communities (e.g. water users' associations) through its ongoing *Agriculture Commercialization and Trade* and *Irrigation and Water Resource Management projects*. In addition, IDA will also focus on agricultural commercialization that should help the country move into new growth areas such as commercially viable agriculture commodities, value addition and export-oriented agriculture. More concretely, it should help farmers take advantage of the rapidly growing demands of neighboring countries—and export what consumers demand[24]. IDA-supported *Rani Jamaya Kulariya (RJK) Irrigation* project will help improve the performance of the irrigation systems and strengthen community-based irrigation management in targeted areas. IFC's *advisory services* will complement the work done by IDA and other donors via the SME Venture Fund and investment climate work.

73. The WBG will work to promote increased access to financial services--particularly important in this country

with so many remote and relatively inaccessible areas. Financial sector connectivity is important for promoting growth. IFC, with IDA, is supporting the development of financial infrastructure critical to enhancing creditors' rights, reducing risks, and improving access to credit services. IFC expects to extend advisory services to help improve financial infrastructure, expand and improve SME portfolios, and help expand financing for sustainable energy. IFC plans to strengthen the capacity of commercial banks to scale-up their SME portfolio. In addition, based on demand, IFC seeks to continue to provide advisory and technical assistance to build a payment framework including electronic banking guidelines, enhance capacity of the Credit Information Center Ltd (CICL) to cover MFIs, and assist in strengthening the legal and regulatory framework for a functional movable collateral registry. These activities will directly contribute to the overall outcome of improving access to finance. This will be done through support to financial institutions which is expected to create and expand business opportunities. IFC plans to expand micro-finance services through technical assistance and will explore opportunities to offer lines of credit. The WBG is working together to assist NRB with an improved payments system and regulatory framework that includes the introduction of mobile banking and other delivery mechanisms to increase the access of more remote communities to more efficient, safer and cheaper payment systems. In addition, an IDA/FIRST *Financial Sector Monitoring Report* will be prepared.

74. The WBG is working to improve the enabling environment for private sector growth. IFC is taking the leadership role in: (i) advisory activities related to private sector development and (ii) catalytic investments in the private sector. IDA is leading on public sector investments and regulatory framework issues needed to leverage opportunities for private sector-led growth. In response to government's interest and request for support, IFC could provide PPP transaction advisory support. In this context, it would also be important to leverage the core strengths of other donor partners in developing the framework and strengthening GON's capacity for undertaking PPPs. Successfully structured PPP projects may further benefit from IFC's funding.

75. IFC-facilitated NBF is promoting dialogue between the private sector and key government actors to promote sustainable reforms in critical sectors. This initiative has shown long-lasting results in other countries and is particularly appropriate given Nepal's fractious transitional status. Through the NBF, private participants identify business impediments, and public sector representatives commit to taking necessary actions to alleviate them. Already, a number of sensitive issues including VAT administration and industrial relationships are being analyzed. Discussions are ongoing regarding easing the entry of new firms and enabling the exit of old, obsolete firms while encouraging labor mobility so that workers can move easily to more productive jobs. Going forward, some of the NBF recommendations might be supported by IFC/IDA, depending on government's request.

76. The activities under the first pillar of this ISN are expected to contribute to four key outcomes to support GON's connectivity and productivity agenda: (i) increased access to electricity and improved reliability of power supply; (ii) improved access to all-season roads; (iii) increased agriculture productivity; and (iv) enhanced access to microfinance.

Pillar 2: Reducing Vulnerabilities and Improving Resilience

77. The second pillar of the strategy is targeted towards reducing food insecurity and improving resilience from exogenous shocks like climate change effects and natural disasters. Three and a half million people are considered moderately to severely food insecure in Nepal. Moreover, Nepal is highly susceptible to climate change risks and ranks 11th in the world in terms of vulnerability to earthquakes. The countries most vulnerable to climate change are characterized by high levels of poverty, exposure to climate-related events, weak capacity for risk management, and reliance on flood and drought prone agricultural land. Climate change is expected to intensify Nepal's already pronounced climate variability and increase the frequency of climate extremes such as droughts and floods.

78. IDA will remain committed to reducing food insecurity among poor households. The prevalence of hunger varies substantially across the fifteen sub-regions of Nepal. The highest prevalence of hunger can be found in the Far and Mid-Western Hill and Mountain regions. The hunger indices in these parts of the country point to an extremely alarming situation. IDA will continue its activities related to improving nutritional impact through increasing agriculture production in food insecure areas, promoting various CMD activities, including small-scale irrigation, to reduce vulnerabilities, implementing cash transfer systems, and strengthening safety net programs that help to improve the livelihood options among rural households. IDA through its ongoing *Social Safety Nets Project,* and *Poverty Alleviation Fund II Project*, will support these activities. This also includes co-financing support from the *Food Price Crisis Response Trust Fund (FPCR TF)* and the *Global Agriculture and Food Security Program (GAFSP)*. Specific interventions under the program include provision of a short-term program for vulnerable districts through the food/cash for work program which would improve food consumption amongst vulnerable groups, including women. In addition, IDA's proposed *Poverty Alleviation Fund III* project will further continue the focus on these issues. Under *PPCR*, IFC aims to enhance agricultural productivity through capacity building of 'seed' supply chain members and providing better access to finance – this is expected to be completed by FY16.

79. IDA will be actively engaged in disaster risk management activities. A combination of rough topography, steep slopes, active seismic zone and intense impact of monsoon rains makes Nepal extremely vulnerable to disaster impacts. IDA has been actively engaged in Disaster Risk Management (DRM) through the GFDRR. Through grant funding from GFDRR, IDA is engaged in assessing the risks of GLOFs[25], co-financing an earthquake school safety program, and developing a detailed hazard risk and vulnerability assessment. The GFDRR also identified Nepal as one of the 21 priority countries globally and is funding the preparation of a Country Disaster Risk Management proposal. The proposal focuses on immediate priorities for Nepal: floods management, institutional strengthening, emergency response and earthquake safety. During FY12-14, the GFDRR will provide training to government counterparts and other stakeholders on seismic resistant building designs and other disaster risk reduction initiatives.

80. Nepal ranks 4th in the world in terms of vulnerability to climate change[26]. The poor who are generally most exposed to natural hazards and most dependent on subsistence agriculture will be the most vulnerable to climate change impacts. At the regional level, the Bank through its ongoing multi-donor funded *SAWI* will focus on strengthening water resources management within and between the countries of South Asia, with an emphasis on regional cooperation and adaptation to climate change. In addition, as implementing agencies of the *CIF,* ADB, IDA, and IFC will jointly support programs for climate resilience, such as the *PPCR*, focusing on climate proofing vulnerable infrastructure, mainly hydropower stations. In addition, IFC is planning to promote sustainable energy finance with a few financial institutions which are primarily focusing on energy efficiency products. This is expected to help participating companies improve operational efficiency, reduce cost and lower their carbon footprint.

81. The activities under the second pillar are expected to contribute to the following outcomes: (i) reduced food insecurity among poor households; and (ii) reduced negative impact of climate change through sustainable energy and carbon finance.

Pillar 3: Promoting access to better quality services

82. The third pillar of the ISN aims to improve the quality of and access to services, especially to the poorest and excluded sections of the society. Although Nepal has made great strides to improve human development indicators, much more needs to be done to improve the quality of and access to services, especially to the poorest and excluded sections of the society and in remote areas.

83. Nepal continues its commitment to education sector reforms which have been instrumental in helping it

achieve significant positive outcomes in education. The country has invested significant amounts of resources into the system and has had tremendous success in enhancing access to basic education, and improving overall governance structures with a strong emphasis on the roles of critical stakeholders. The country is progressing well towards closing the gap in the net enrolment ratio at the primary education level. The disparities across gender, regions, poverty quintiles and ethnic groups have also been narrowed. However, increasing access to secondary school education (grades 9-12) remains a major challenge as evidenced by the disturbingly low net enrollment rate of 24 percent at this level. More than half of primary level students do not enter secondary schools, and only one-half of them complete secondary schooling. In addition, fewer girls than boys join secondary schools and, among those who do join, fewer complete the 10th grade[27]. Experience in Nepal indicates that girls who do not go to school are more at risk of trafficking, early marriages and sexual violence. Research has shown the positive impact that girls' school continuation into secondary level can have on their status in the family, maternal and newborn health, nutrition, early marriage, and on the general economic, health and nutritional status of the family. Scholarships and incentives have long been used internationally as a means to provide girls education and retaining them in school. Although the government is committed to expanding the scholarship schemes to girls at secondary education level, the coverage of these schemes is very limited. The Government is planning on additional expansion of the scholarship program to provide universal scholarships to girls in grades 1-8 and is seeking IDA's assistance to expand the scholarships programs to all girls in grades 9-10 in districts with lowest enrollment. IDA will support this through the proposed *School Sector Reform Project Additional Financing*.

84. While student enrolment numbers have increased, there is a pressing need to improve the quality of basic education. As a first step, the government has initiated a National Assessment of Student Achievements (NASA) according to international standards. This will establish an important baseline on learning outcomes in the country. The first NASA is expected to be fielded by December 2011. IDA-financed *School Sector Reform Project* along with the *Education For All Fast Track Initiative* is supporting quality enhancement of basic education.

85. At the higher education level, Nepal has not been as successful and improving quality and relevance of higher education remains challenging. Implementation of many higher education initiatives have been stalled due to poor internal efficiencies, high level of dropout and repeaters. In addition, there are weak linkages to the higher secondary education systems, thus imposing enormous burdens between higher secondary and higher education. The government has begun to consider some far-reaching policy reforms to improve the functioning of the Technical Education and Vocational Training (TEVT) system and reduce fragmentation in provision, quality assurance, and certification. Another challenge is to make TEVT access more inclusive. A draft new government policy on TEVT is currently being formulated and aims to strengthen coordination, not only within and across government and private institutions, but also help harmonize donor support to the subsector. IDA through its ongoing *Second Higher Education* and recently approved *Enhanced Vocational Education and Training* (EVENT) projects is focusing on improving quality and relevance of higher education through systemic reforms, incentives to selected institutions and providing technical and vocational training that will enhance the skilled labor market in Nepal. In this regard, IDA will monitor students' pass rates at bachelor's level, enrollment in relevant subjects (for instance, science and technology) and the employment rate of vocational training graduates to measure the progress. IDA, through the *EVENT* project is working closely with other development partners to support the implementation of the new TEVT policy. In addition, the Bank-supported *Adolescent Girls Employment Initiative (AGEI)* supports occupational skill training, life skills training and business skills training for adolescent girls aged 16-24 years to assist them to enter into gainful employment.

86. Nepal continues to do very well in the implementation of its micronutrient programs but the progress in addressing chronic malnutrition has been less impressive. Progress in the area of nutrition indicates that Nepal is not on track to achieve the related MDG targets by 2015[28]. In spite of the less than successful attempts in

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the past, there is currently significant momentum to re-introduce a multi-sectoral approach to promote Food and Nutrition Security in Nepal. Significant investments will be needed to reduce the prevalence of underweight children aged 6-59 months from the 2010 level of 38.6 and to reduce the proportion of stunted children aged 6-59 months from 49 percent in 2010. During the ISN period, IDA's key interventions to address the issue of chronic malnutrition are through the ongoing health sector SWAp *Second Health Nutrition and Population* and *HIV/AIDS and Social Safety Net Projects*. The SWAp focuses on improving the nutritional status of children and pregnant women. The government has recently announced new nutrition program for the first 1,000 days of life (including pregnancy) and IDA will support this initiative through the proposed *First 1000 Days Project*. On the advisory side, the Bank will continue its dialogue on *Nutrition Policy*.

87. The activities under the third pillar are expected to contribute to the following outcomes: (i) improved access to secondary and higher education; (ii) enhanced quality and relevance of education; (iii) decreased malnutrition among pregnant women and; (iv) improved coverage of fully immunized children within the poorest quintile.

B. World Bank Group Instruments of Engagement

88. The ISN proposes to use a mix of lending and advisory services instruments to support the program. IDA's primary instrument will be the Sector Investment Loans (SILs), using AFs and emergency operations where needed. If a results-based instrument is approved by the Board, we will also explore using this instrument in Nepal. Responding to the government's demand for more targeted and timely advisory support, the non-lending program will be delivered on a more programmatic basis with intermediate short outputs. "Just-in-time" support to the client will be continued. As in the last ISN, GAAPs will be developed for all projects; however more attention will be paid to strengthening the monitoring arrangements of GAAP implementation.

89. IDA proposes to continue to assess all new projects from a peace perspective to maximize the potential pro-peace impact of the portfolio. A stock-taking of the peace filter in 2011 found that there was substantial duplication with the GAAP tool, and that there was not substantial team input into the conflict analysis process. As a result, the peace filter approach is being revisited to enhance its effectiveness as a conflict analysis and peace building tool. Under the revised approach, joint GON-IDA project team members will work together at key milestones (post concept note, appraisal, periodically during implementation) to jointly identify drivers of conflict, potential connectors, and opportunities for modifying project activities and/or implementation arrangements to build social cohesion at the local level. Joint findings could then be explored in depth as part of the preparation process, and then regularly monitored during implementation, in order to continually make adjustments during the life of a project as the local environment evolves. In this process, teams will keep in mind that development operations have the potential to both create and exacerbate conflict, as well as to promote the peace and build social capital. This approach is being discussed with the government and development partners, with the goal of better coordinating conflict analysis in development operations. The possibility of developing conflict sensitivity training for civil servants through the Administrative Staff College is also under discussion.

90. Fostering gender equity and social inclusion will be actively pursued and monitored. The Bank is currently reviewing its existing portfolio from a gender perspective to draw lessons, identify gaps, and highlight good practices and the most effective entry points for addressing gender considerations in its operations. Moreover, the Bank will coordinate among different sectors and integrate gender and social inclusion considerations into existing analytical work undertaken by the Bank such as the poverty assessment. Similarly, the Bank will actively seek funding for additional analytical work especially on gender and migration, and improving justice for the poor, preferably with other development partners active in these fields.

91. IDA resources under the FY12-13 ISN are estimated at SDR 268.3 million (US$403 million equivalent). The ISN

covers the first two years of IDA16. The estimates for FY12-13 are indicative only and can change depending on: (i) total IDA resources available, (ii) the country's performance rating, (iii) the number of IDA eligible countries, (iv) the performance and assistance terms of other IDA-eligible countries, and (v) the terms of IDA's assistance to Nepal (grants or credits), which are determined annually and based on the risk of debt distress. IDA allocations are made in SDRs, and the US dollar equivalent is dependent upon the prevailing exchange rate.

92. An indicative IDA pipeline has been agreed with the government. Activities were selected based on the following criteria: consistency with the government priorities, broad political support, IDA's comparative advantage, and evidence of implementation capacity. All proposed projects build on or scale-up ongoing projects which have been effective in the past (see Annex B3).

93. Consultations with GON and development partners have confirmed the value added of the WBG's analytical work in Nepal. Although the Conflict WDR does not explicitly refer to analytical work in fragile states, it provides some useful principles to think about analytical work in a politically uncertain environment, as well as offers some valuable thoughts on how to do it in practice. It implies that stand-alone big reports are unlikely to be very useful in the context of a fragile state. These reports typically take a couple of years to be produced, which feels even longer in an uncertain environment. This is consistent with GON requests that the Bank prepares fewer large multi-year reports and instead tailors the non-lending program to their country-specific priorities and just-in-time requests. Another insight offered by the WDR is that credibility needs to be built with all the relevant counterparts and there is a need to reach out to a broad spectrum of stakeholders, so as to understand their concerns, and come up with practical ways to address them. A strong field-based presence is required to be responsive and to reach out to non-traditional counterparts. Keeping these principles in mind, an indicative analytical and advisory program (AAA) is presented in Annex B4. It is clustered under five main programmatic themes consistent with the ISN's proposed strategic thrusts: (i) economic and financial sector key issues and results monitoring, (ii) strengthening governance and accountability, (iii) enhancing connectivity and productivity for growth, (iv) poverty, gender, and social inclusion, and (v) reducing vulnerabilities and improving resilience. Each of the clusters is expected to include a combination of just-in-time policy notes, core diagnostic work and NLTA support led by field-based staff and international staff. A key deliverable during the ISN period will be the completion of the Poverty Assessment (one of the key pieces of core diagnostic work) based on NLSS III data. Several thematic notes will also be prepared building on NLSS III. Majority of the other proposed AAA is currently ongoing - largely funded by trust funds - and will continue over the ISN period (e.g., PFM reform, governance reform NLTA, water resource and climate change, forest sector governance, nutrition policy issues, disaster risk management, etc.). In many of these areas, the WBG is already working with other development partners – for example SAWI, PFM reform, roads sector assessment, GSEA, GESI, ICRP and SARTI. Finally, several of the products that have been completed recently or will be completed in the next few months will be disseminated appropriately through a combination of workshops, publications (including in Nepali) and press releases.

94. IFC seeks to effectively leverage its investment and advisory services to support the country program. IFC's investment instruments currently include senior and subordinated loans, long and short-term credit lines, trade finance lines and guarantees, and minority equity stake in companies – all in hard currencies. IFC aims to continue to provide long-term and counter-cyclical financing for companies that are unable to access financing at appropriate terms, with special attention to providing risk capital to small businesses under the SME Ventures program. IFC's additionality in Nepal comes through providing longer tenor financing than is available in the market, patient equity capital, crisis response products such as liquidity facilities, global and regional expertise and experience, and technical assistance to enhance areas such as corporate governance and management of environmental and social risks. IFC aims to continue to respond to client needs through facilities

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such as SME Venture Fund, Infraventures, transaction advice for PPPs, and risk-sharing facilities (RSF), as well as to crisis situations through special initiatives such as bank recapitalization fund and Global Trade Liquidity Program. As local currency financing is essential for companies and sectors that generate local currency revenues, including large scale infrastructure hydropower-projects, IFC plans to continue its effort in partnership with IDA, with the GON to create such instruments. IFC's advisory services engagement areas are expected to remain largely intact. MIGA will continue to support the proposed pillars of the ISN through the provision of long term political risk insurance to investors, with a focus on infrastructure projects and south-south investments.

95. The World Bank Institute (WBI) is also exploring areas of collaboration in Nepal. Their overall approach is to prioritize, be selective, and share global and regional experiences that may be of relevance to Nepal. The primary focus is expected to be on supporting the governance and accountability theme of the ISN. This would include collaboration with the PRAN and project teams to promote regional learning and capacity development related to social accountability and RTI. In addition, building on the Nepal Country Team effort to geo-code project interventions supported by IDA, WBI is also exploring the possibility of providing support to development partners to geo-code their project interventions as well, with the goal of facilitating division of labor discussions and promoting synergies within and across sectors. A pilot in Nepal to facilitate the use of ICT and crowd-sourcing for improved governance and service delivery is also under discussion. The WBI regional and global teams will support South-South knowledge exchange as per demand from Nepal, and connect Nepal to regional and cross-regional experiences.

C. Partnerships: Donor Harmonization and Aid Effectiveness

96. The WBG will further improve coordination of its interventions with other development partners and contribute to discussions around division of labor, sector selectivity and aid effectiveness. The MOF began rolling out its Aid Management Platform (AMP) to all local development partners, including India and China in February 2011. Plans are also underway to engage non-resident donors in this exercise, and to enable the AMP to accept geo-spatial data codes that could be used to generate maps showing locations of development programs. A complete overview of donor-supported projects, both on and off budget, is expected by end August, with partial data available as of this writing. In advance of completion of the AMP data, WBG, ADB and DFID have held informal consultations to discuss how the respective country programs can be adjusted to be complementary and to build on each institution's comparative advantages. Recent consultations with the UN Country Team also focused on comparative advantages and where the UN could usefully focus, given its strong local field presence. These consultations have resulted in shifts in sector support on the part of IDA, DFID, the ADB, and the UN, based on better information and better appreciation of respective mandates/competences. IDA will continue to participate in the annual NPPR process, and support the government's efforts to transform this mechanism into a broader aid effectiveness tool for all donors. The 2010 NPPR Action Plan (focused on actions to improve country systems performance) was approved by the Cabinet, and a tracking mechanism reporting to the Prime Minister has been put in place. In 2011, the MOF is seeking to expand the NPPR focus beyond country systems to incorporate elements of mutual accountability for both government and development partners.

MANAGING RISKS

97. Overall country risks depend on what happens on the political front -- sustained peace/consolidation versus political disintegration or stalemate. There are wide variations in possible outcomes as reflected in Table 5. Scenario B assumes continued stalemate and slow movement forward regarded by many analysts as the most likely scenario. Given the short time frame of the ISN, and the continued uncertainties of this prolonged transition/ new constitution/new government, we are not proposing large irreversible commitments from which we might have difficulty exiting if the political/policy context became untenable for the Bank. We also do not anticipate the ability to do fast-disbursing policy reform-based Development Policy Credits. The investment climate is unlikely to improve in the short term and while IFC continues to undertake small steps towards improving the investment climate, its contribution may be limited by the political environment. Finally, engaging in decentralization/fiscal federalism discussions will no doubt be particularly challenging.

98. Increasing vulnerabilities in the financial sector have prompted NRB to take measures to prevent further escalation, including preparation of a contingency plan[29]. Because the real estate prices have started to come down, financial institutions that have high real estate exposure are increasingly vulnerable due to possible deterioration of asset quality. The IDA team, in coordination with the IMF, is continuing to discuss measures that are needed to be taken to reduce future risks. If the financial sector deteriorates, IFC could scale up its advisory services program and also provide financing to deserving clients. Its SME Venture Fund, designed for quick disbursement, could provide credit and advice to SMEs. IFC could also provide trade facilitation support via the Global Trade Finance Program, and short term liquidity support to commercial banks and the corporate sector. Finally, IFC could explore equity support for banks.

99. Good revenue performance experienced over the last four years might be at risk. Revenue growth was substantially aided by high and increasing remittance flows. A significant portion of incremental revenue has been due to tariff and VAT revenues levied on remittance-induced imports. However, the slowing down of remittance growth in recent months is likely to put downward pressure on revenue mobilization and, as planned expenditures are rising rapidly, could potentially make fiscal management difficult. Other fiscal risks are associated with financial losses of the two state-owned enterprises (NOC and Nepal Electricity Authority), army integration, and the potential costs of addressing financial sector weaknesses. While IDA will not directly support the government to enhance revenue mobilization during the ISN period, it will continue to support improvements in expenditure planning, prioritization and efficiency through the NLTA on MTEF.

100. The country's transitional issues and political instability have sidelined the drive against corruption. Despite strong anti-corruption legislation, the high-powered CIAA has not been able to function effectively. However, some opportunities are emerging. The RTI Act and the recently ratified United Nations Convention Against Corruption are two examples. The Judiciary has also started playing an active role in dealing with corruption cases, especially those involving high-profile politicians. To address corruption issues at the national level, IDA is providing support (together with other development partners) towards strengthening the government's PFM systems. Civil society organizations are also being strengthened as part of IDA's program to promote social accountability. Effective implementation of the monitoring tools, including GAAPs, will continue to address corruption risks in IDA-supported projects.

101. In the past, new governments have rotated some high and mid-level staff. IDA's response to these risks is to engage with political leaders on a regular basis about development challenges, the need for political leadership on policy questions, and our proposed development projects, so that all key parties are informed, whether they participate in future coalition governments or not. IDA program has received the endorsement of major political leaders as well as key development partners. By improving information flows, this dialogue helps to reduce mistrust and facilitate support for ISN initiatives. IDA also has strong relationships with other development partners so that when problems are identified, a unified approach is presented. Finally, IDA is strengthening links with civil society through new initiatives such as the PRAN. Greater political instability however, might

affect implementation of more sensitive operations – such as the Cross-Border Transmission line to India. The Nepal program will continue to make use of COSO[30] workshops as a risk reduction/quality enhancing tool for identifying risks, formulating actions, and achieving results.

102. The CMD project portfolio has shown robustness in the context of changing risks and an uncertain political situation. These projects were resilient during the earlier conflict and are at the heart of IDA program today. For the bulk of the program, the track record on CMD operations shows that these operations can withstand quite serious conflict situations. Community-based mechanisms are now well established in Nepal and are likely to remain an important part of development strategy in the country. So that part of the program has a reasonable chance of successful outcomes even under a worst case scenario. The community portfolio includes a good framework for mitigating governance and fiduciary risk at the community level. There is significant community participation in decision-making and good knowledge of the project investments. Most of the investments show evidence of significant community contributions, either in terms of co-financing or donated labor. And most of the communities demonstrate high awareness of financial entitlements and detailed record-keeping of financial intakes and expenditures.

TABLE 5 NEPAL – COUNTRY SCENARIOS FOR FY12-13

SCENARIOS	DRIVERS	OUTCOMES	WBG RESPONSE
A. Resolution: Promulgation of the new constitution; Agreement on federalism model; Conclusion of the peace process; Integration of armies; Resolution of property issues; Free and fair local and national elections	• Pressure from below (people's pressure) • Civil society engagement • Mass protests against poor governance	• High level of political understanding on the new political order • Increased certainty and stability of government • Measures to promote healing from wounds of war underway	• Engagement on longer-term development issues, including programs to support implementation of constitutional provisions • Support to a decentralized approach to governance
B. Stalemate: Further extension of the CA by 3 months; no party or coalition strong enough to impose resolution	• CA members unable to pass constitution • Political understanding on army integration still discussed • Agreement on rotational government leadership through coalition reached for the short-term horizon	• 'Business as usual-muddling through' • Some protest actions, limited violence • Unstable coalition governments	• Continued engagement in community driven and selected ring-fenced programs • Strong external monitoring of results, strengthening social accountability • Private sector engagement by IFC at the current low, but steady level
C. Breakdown and violence: Failed democracy	• Political deadlock • No agreement on most CA theme papers • No progress in army integration • Rise in activities of various increasingly violent ethnic groups, armed political groups, thugs and paramilitary groups • Continued capital flight out of Nepal	• CA dissolved; Cabinet dissolved • Power vacuum (with no constitutional measures available to tackle the situation) • Extra-constitutional rule imposed • Mass protests and riots • Re-emergence of violent conflict	• Stop programs where there is high risk of physical harm to occur • Rethink WBG engagement and adjust portfolio and staffing levels to changing conditions

End Notes

1 Based on Nepali calendar.
2 This is consistent with OP 2.30, along with BP 2.11 and OP 2.30 and the Guidelines to Staff for CAS Products dated October 2010.
3 Indigenous people of Nepal. The law defines the term "Janajati" as a community having its own language, traditional rites and customs, distinct cultural identity, distinct social structure, and written or unwritten history.
4 The last CAS had covered the period FY04-06 and the most recent ISN expired on June 30, 2011.
5 Food inflation in the first nine months of the GON fiscal year is 20 percent and is expected to stay in that range until the harvest season (September 2011).
6 Gasoline share is 15-17 percent in total import volume of petroleum products.
7 Liquefied Petroleum Gas.
8 Draft Joint Bank-Fund Debt Sustainability Analysis, July 2011
9 However, the depreciation of the Indian rupee relative the US dollar will affect the exchange rate between the Nepali rupee and the US dollar.
10 Based on World Bank's Atlas methodology. World Development Indicators Database, July 1, 2011.
11 These estimates are based on the national poverty line.
12 The third Nepal Living Standards Survey (NLSS) is underway and will provide updated poverty figures.
13 Of every 100 students who enter grade 1, only 78 reach grade 5, and only 62 reach grade 8.
14 World Development Indicators, World Bank.
15 Elected from diverse caste, ethnic and regional groups.
16 14 of the 28 new civil servants appointed to Foreign Affairs Services this year are women, compared to a total of 6 women in its history thus far.
17 The Global Alliance for Vaccines and Immunization.
18 Includes Nepal, Bangladesh and Bhutan in South Asia (approved) and Laos and Vietnam in East Asia (under preparation).
19 Includes only the country IDA share for the two regional projects.
20 2011 World Development Report, Chapter 4, page 128.
21 The 2001 Nepal Census recorded 103 different caste/ethnic groups.
22 121km/1,000 sq km against Bangladesh's 2,080km/1,000 sq km.
23 For example, the southern Tarai area contains more than three-fifths of all roads.
24 E.g., coffee, tea, ginger, and cardamom.
25 Glacial lake outburst floods.
26 According to the 2011 Climate Change Vulnerability Index released by global risks advisory firm Maplecroft.
27 34 percent compared to 38 percent for boys.
28 MDG targets are to lower the prevalence of underweight children aged 6-59 months to 29 and to reduce the proportion of stunted children aged 6-59 months to 30 by 2015.
29 The contingency plan was prepared by NRB in 2010 with IDA's assistance.
30 Committee of Sponsoring Organizations.

Interim Strategy Note for Nepal
FY12-FY13

ATTACHMENTS

THE WORLD BANK GROUP

Attachment A

Results of FY10-11 ISN

Sectors	ISN Results Indicators	Progress as of June 2011
Pillar 1: Promoting Capable State Structures and Systems and Fostering Accountable Institutions		
Public Financial Management	> Production of financial statements for FY11 according to internationally accepted accounting principles (IPSAS-based) for public sector > Completed piloting of a single treasury account in two districts	> The implementation has been delayed. The government is aiming to have the financial statement for FY12 (on a pilot basis) prepared according to IPSAS. > The piloting has been completed in both the districts (Bhaktapur and Lalitpur) during FY09-FY10. The roll out has now been made in 22 districts. This will be supported through PFM MDTF for full roll out.
Procurement	> Implementation of OECD/DAC indicators for public procurement monitoring > Issuance of standard bidding documents (works and goods) for NCP by PPMO	> Implementation has now begun. PPMO has started interacting with stakeholders. Draft report is expected by end-July 2011. It is expected to be finalized before the closing date of the IDF Grant that is, by September 30, 2011. > Completed and the standard bidding documents are available in PPMO website.
Governance	> Endorsement by Cabinet of a set of regulations to implement the Right to Information (RTI) Act, 2007 > Inclusion of Governance and Accountability Action Plans (GAAPs) in all new IDA operations plus five of ongoing projects > Introduction of Social Accountability (demand-side) in new operations and five ongoing projects > Social Audits increase from 68 percent to 80 percent non-private grade 1 to 8 schools > Preparation of a framework to govern Private Participation in Public Services (PPP) for GON consideration	> Redrafted the regulations, new regulations endorsed. > GAAP prepared for 15 new projects. > Social Accountability (SA) mechanisms introduced in all new projects. > Social audits 83.2% in FY 2009; target exceeded. A new status report will be available in Nov 2011. > IFC and MoF organized a PPP workshop on Dec 9th, 2010. The workshop was supported by WB, PPIF, DEVCO and WBI.
Pillar 2 : Laying the Foundation for Sustainable Economic Growth		
Macro/Public Expenditure Management	> Medium-term expenditure framework agreed for FY11 > Improved SEZ Law submitted to the Constituent Assembly	> MTEF agreed and delivered. > The SEZ act has been further improved and nine chapters of regulation drafted.
Private Sector Development	> Public-Private Policy Dialogue initiated through IFC's ICRP > 50 hotels participating in local hotel booking portal (IFC)	> The 1st round of meetings of NBF working group has been completed with 35 recommendations out of which 9 has already been implemented and 4 others have been addressed in the current budget. Eastern Regional Business forum has been established to set up task forces on SEZ, Power and Security. The forum made 15 recommendations out of which 5 has been implemented and 1 has been addressed by the current budget. > 65 hotels registered in the website. The project is successfully closed.

Sectors	ISN Results Indicators	Progress as of June 2011
Pillar 2 : Laying the Foundation for Sustainable Economic Growth		
Financial Sector	> At least one bank offers energy efficiency credits to private sector	> IFC signed MoU with Clean Energy Development Bank (CEDBL) on May 2010. Strategy and portfolio assessment completed for CEDBL in Sep 2010. Market Potential Study on EE/RE for Industries and FIs completed in June 2011. First phase of training on SEF for bankers completed with CEDBL and remaining portfolio development activities underway. > IFC conducted Energy Auditor training for energy service companies to develop pipeline of EE investments and a market scoping study to identify business cases for EE/RE in the Nepali market in Feb 2011, pilot audits for FI pipeline development underway.
Irrigation	> Rehabilitation of 8,000 hectares of small-scale irrigation	> The rehabilitation of 58 farmer-managed irrigation schemes has commenced, with a total command area of about 11,700 ha. Out of these, the works at ten schemes, commanding 1,900 ha, have already been completed.
Energy	> Increased availability of power generation capacity by 100 MW	> IFC has committed US$6.5mn for 4.3MW refurbishment and upgradation of an existing plant from 5.1MW to 9 MW. IFC is working on disbursing the committed US$6.5mn loan, which is expected to be partially disbursed in FY12. In addition, IFC is working on financing additional 30-50MW of hydropower capacity for FY12.
Roads	> 250 km of strategic roads upgraded with an increase of 5 percent of the population within 20 mins walking distance to core strategic roads in the RSDP project area. > 270 km of rural roads improved to all weather standard equivalent, representing an increase of 5 percent of the rural population within 4 hours walking in the hills and 2 percent within 2 hours of walking in the low lands in the RAIDP project districts > Funding in budget sufficient for 500 km of road maintenance per year (FY10/11) > Agreement on the framework for sector wide approach in rural roads	> 265.5 km of strategic roads completed as of December 2010. The DOR survey also shows that where road upgrading works have been substantially completed there had been a 35% decrease in travel time to economic centers for residents of the project area. This will be verified by an ongoing survey. > Upgrading of 598 km of rural roads completed. Increase in population served will be verified through an ongoing survey (Results of the survey expected in September 2011) > Maintenance budget for FY 2010/2011 has increased from last year and consolidation of SRN maintenance funds to be fully channeled through Roads Board Nepal has taken place. > Agreement to move to SWAp has been deferred due to capacity constraints and high country risks. A pooled funding arrangement for trail bridges is in operation.

Attachment A

Results of FY10-11 ISN

Sectors	ISN Results Indicators	Progress as of June 2011
Pillar 2 : Laying the Foundation for Sustainable Economic Growth		
SME	> Credit Bureau equipped with the necessary hardware and software to carry out its functions (IFC) > SME lending strategy approved by three commercial banks (IFC)	> Credit Information Bureau: Financial bids opened in May 2011 under an IDA project exceeded NRB project budget. Alternative options being explored by IFC to support credit bureau. Secured Transactions Registry (STR)- MOU signed between MoF and CICL in Oct 2010; Stakeholders workshop conducted in Mar 2011 by IFC/WB experts to finalize amendments to the Regulations and Act; REO and RFP documents finalized in Apr 2011 and pending with MoF and NRB for the next steps. IFC may consider exploring alternative options to support STR. > BOK adopted SME strategy in 2009; Cooperation Agreement with NIC Bank signed in May 2011; Discussion with additional bank to be carried out in FY 2012.
Climate Change	> Completion of hydro-economic model of the Ganges River > Clarification of Nepal's climate change priorities in context of regional climate change conference in FY10 > GON Action Plan available on protecting tigers habitat	> The final draft report completed. > Done. Priorities clarified. A new department in the Ministry of Environment called Climate Change Division has been established. Its focus is to build Global Mountain Alliance to highlight the effect of climate change on mountain communities. > Action Plan completed.
Pillar 3: Enhancing Equitable Access to Services & Social Inclusion		
Education	> NLSS completed > Increase in community managed schools from 8,000 to 12,000 > Completion of training of 1000 girls in vocational skills and life skills > Net enrollment increases from 92 percent to 94 percent (grades 1-5) and from 73 percent to 86 percent (grades 1-8) as verified through EMIS > Establishment of an accreditation system for higher education > 4000 students from 1st and 2nd income quintile benefit from financial aid to attend higher secondary and post-secondary education	> Survey fieldwork completed in Feb, 2011. Data analysis ongoing. Poverty assessment report to be completed in FY12. > Current Number is 11,400 > As of March 2011, training has been completed for 810 girls in vocational and life skills. > Net enrollment (grade 1-5) is 94.5%. Net enrollment (grade 1-8) is 86%. A new report on the update will be out by Aug 2011. > Accreditation system established, 1 institution accredited (Bal Kumari College in Chitwan). Three (3) institutions completed quality assurance cycle. Four other institutions completed self study report (SSR) and ready for peer review. > 2000 students from 1st and 2nd income quintile have benefitted from financial aid to attend higher secondary and post secondary education. Data entry of new (3rd) cohort complete for selection of 2,346 students in academic year 2010/2011. * 3000 beneficiary-students were selected and their names were published in national dailies.
Health	> 35 percent of pregnant women receive at least four antenatal visits (29 percent in 2006) > Share of deliveries by trained health workers increased from 31.7 percent in 2009 to 42 percent > Share of women with knowledge of at least one method of HIV infection in women increases from 56 percent in 2006 to 72 percent	> 35.2% of pregnant women received at least four antenatal visits > Share of deliveries by trained health workers increased to 36%. > Share of women with knowledge of at least one method of HIV infection in women increased to 88%

Sectors	ISN Results Indicators	Progress as of June 2011
Pillar 3: Enhancing Equitable Access to Services & Social Inclusion		
	> Share of under-five malnourished children decreases from 49 percent in 2006 to 35 percent > Contraceptive Prevalence rate for modern methods increases from 44 percent in 2006 to 48 percent in 2011 > 6000 surgeries for uterine pro-lapse per year > Share of children under 12 months immunized with DPT3 increases from 79 percent in 2008 to 90 percent	> Share of under-five malnourished children decreases to 45%. > Contraceptive Prevalence rate for modern methods increased to 65.35% (As of May 2011). > 4600 surgeries for uterine pro-lapse last yr. > Share of children under 12 months immunized with DPT3 increased to 89%.
Social Protection	> Endorsement by Cabinet of a Social Protection Strategy, including the framework for a set of principles and information base on targeting social programs for poor and vulnerable groups > 20,000 more rural households benefiting from modern electricity through sustainable community based micro-hydro schemes: (Baseline: 20,586 HH) > 21,000 more rural families using biogas	> The NPC led inter-ministerial team submitted a draft social protection framework for 10 years to the NPC in 2011. > As of June 2011, 23,965 additional HHs have gained access to electricity. > By the end of Mar 2011, 20,503 families will have benefited from biogas plants. 7036 more families will benefit from such plants in 2011.
Water and Sanitation	> 69,000 more rural households benefiting from community managed rural water systems and 65,000 more from sanitation systems	> As of May 31 2011, about 69,859 more households have benefitted from water supply within 15 minutes walking distance (Baseline: 101,658) and 73,572 more households have household latrines (Baseline: 55,504).

Attachment B

Program for Accountability in Nepal (PRAN)

PRAN is a three year US$3 million project funded by the State and Peace Building Fund (Oct 2009 – Sept 2010), supplemented by US$1m in funds from a Multi-Donor Trust Fund in Nepal. Its objective is to develop the capacity of civil society and government actors to promote social accountability in Nepal through provision of practical training, action learning, and networking opportunities. Its three focal areas are Public Financial Management, Urban Governance, and Public Service Delivery.

The background is IDA's commitment to the two themes of Demand for Good Governance and Social Accountability which together recognize that a special effort has to be made to listen to the poor and marginalized groups affected by IDA projects; to empower people to demand accountability from the government and other power holders; and to underline governments' obligation not only to listen to its citizens, but also report on and account for their activities to the citizens. The background in Nepal is that while there is considerable institutional (government and legislative) attention to issues of social exclusion and citizen participation, in reality these fine and far sighted policies are often sidelined or not fully implemented.

PRAN seeks to promote and encourage IDA and GoN to use their own funds to advance demand for good governance programming with CSOs, as is being done in, for example, the Poverty Alleviation Fund, and the Rural Water Supply and sanitation project. While its main work is with Nepali CSOs and government actors to promote and support work on social accountability, it also offers WB projects opportunities for coordination and collaboration with PRAN in incorporating social accountability mechanisms in their project design. Its main components are:

Component 1: to build up and work through a National Capacity Building Institute. This will provide training and capacity building to both CSO and GoN actors, mentoring and coaching visits and scholarships, and special programs for targeted audiences (e.g. journalists). A project working with CSPO and GoN actors might value using such services.

Component 2: to make grants to CSOs to practice what they have learnt in Component 1, or to deepen and further pilot their own work in social accountability. PRAN has helped to set up a completely independent Grant making Committee which will decide on grants under this component. Again an IDA project working with CSOs may see value in encouraging them to apply to this Committee for funds.

Component 3: to build a National Centre for Social Accountability to be the knowledge centre for this topic and have information about the relevant mechanisms, trainers, and experiences, in Nepal. It is also untended to encourage and develop networks and coalitions among Nepali CSOs who are interested in the same topic. An IDA project may see ways in which its partners can benefit from such ideas.

Component 4: for monitoring, impact evaluation, and learning, and also to be the source of funding for special studies, such as, for example, the research on the Political Economy of Social Accountability in Nepal. The findings of this and any future studies may be of relevance and use to Task Team Leaders, and the PRAN will ensure that they are circulated to all staff.

The Nepal Country Office has recruited a team to manage the PRAN program, including a social accountability Adviser to coordinate the program. Apart from coordinating the PRAN activities, the team is also supporting World Bank task teams in Nepal in better understanding and incorporating social accountability mechanisms in their operations.

Attachment C

IDA-IFC Areas of Collaboration

Sectors	Activity
Joint ISN exercise	Implementing a joint IDA-IFC ISN for FY10-11; preparing a new joint ISN for FY12-13.
Hydropower	IDA and IFC are jointly preparing the Kabeli 'A' Hydroelectric Project – a first in Nepal. IDA and IFC teams are also working in close coordination to provide financing support through IFC's sub-national finance group for the Nepal-India Electricity Transmission and Trade project.
Coordinated approach on water resources	IFC infrastructure team and IDA water resources/energy team are adopting a coordinated approach for the sectors' development in Nepal.
Financial sector	IDA and IFC are collaborating on financial infrastructure reform and access to finance (such as e-payments that include mobile banking/ microfinance) in Nepal.
Climate Change	IDA and IFC (along with ADB), are implementing two Climate Investment Fund (CIF) pilot programs-SREP and PPCR. Once approved, IFC plans to help manage the US$30 million funds expected to be provided to Nepal's private sector.
Private Sector Development	IDA and IFC are collaborating to execute IFC led Investment Climate Reform Program in Nepal. A Memorandum of Understanding has been signed in October 2010 between the two country office staff in Nepal.
Trade and Transport	IDA and IFC plan to collaborate on two new tentative programs: IDA's North Eastern Regional Trade and Transport Facilitation Program (NERTTP) and IFC's planned new South Asia Regional Trade and Integration (SARTI) program. This would complement IDA's work on trade and transport facilitation through IFC's work on trade facilitation.
Agribusiness	IFC's agribusiness advisory services will complement the work done by IDA and other donors via the SME Venture Fund.

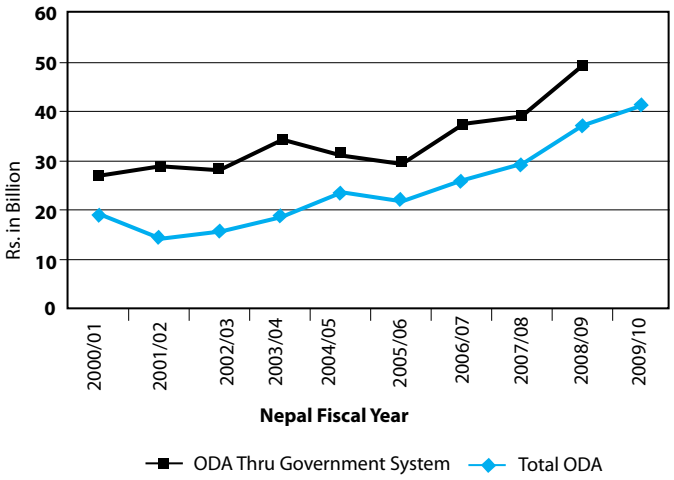
Attachment D

Official Development Assistance and Development Partner Coordination

As noted in the Nepal Country Evaluation carried out for the Joint Evaluation of the Paris Declaration (Phase II 2010), a history of aid dependence and fragmented external support has characterized the DP relationship with Nepal. The mixed record of aid effectiveness was a focus of discussion at early NDFs (Nepal Development Forum), and the Foreign Aid Policy (2002) was an effort to provide a structure for aid management. Since 2007, the Three Year Interim Plans (TYIP) have set aid management policy in the context of Paris Declaration Principles.

Nepal has been receiving foreign aid as a source of financing for socio-economic development since the mid-fifties. Up through the 1990's, foreign assistance remained around 5-6% of GDP, financing about 25-30% of total government expenditure and about 60% of the development budget. The past 10 years have seen a reduction in dependency (from 24% in 2000 to 17% in 2009), reflecting strong domestic revenue collection efforts. However, external assistance as a share of the development budget continues to be significant. The past decade has seen a doubling of total official development assistance (ODA), with a slight increase in the proportion of ODA channelled through GoN systems. At moments of political crisis (e.g., intensification of the armed conflict in 2001/02 and the king taking power in 2005), ODA channelled through government dipped, while total ODA increased, suggesting that DPs shifted more aid through non state modalities. Since the peace settlement in 2006, ODA through government has steadily increased, although other modalities have been retained, reflecting concerns over GoN capacity and a growing concern over corruption. The increase in ODA through government systems appears to be largely due to the increase in multilateral support and support from DPs participating in pooled sector programmes.

Total ODA and ODA through Government System



Source: OECD Website and MOF, 2010

Nepal Fiscal Year (NPR bn)	2000/01	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09
Total Government Revenue	48.89	50.45	56.23	62.33	70.12	72.28	87.71	107.62	143.47
	61%	*63%*	*67%*	*70%*	*68%*	*65%*	*66%*	*67%*	*65%*
Total Foreign Aid	18.80	14.38	15.89	18.91	23.66	22.04	25.85	29.30	36.35
	24%	*18%*	*19%*	*21%*	*23%*	*20%*	*19%*	*18%*	*17%*
Internal Loan & Cash Balances	12.14	15.24	11.89	8.20	8.78	16.56	20.04	24.43	39.84
	15%	*19%*	*14%*	*9%*	*9%*	*15%*	*15%*	*15%*	*18%*
Total Public Expenditure	**79.84**	**80.07**	**84.01**	**89.44**	**102.56**	**110.90**	**133.60**	**161.35**	**219.66**
	100%	*100%*	*100%*	*100%*	*100%*	*100%*	*100%*	*100%*	*100%*

Source: Economic Survey, 2009/10, MoF

Looking at ODA trends from the perspective of the contributing DPs, the two development banks have dominated aid throughout the decade. Amongst the bilaterals, DFID and India have grown in significance, whilst Japan has reduced its level of aid (in particular aid channeled through government systems). On-budget ODA disbursements by the 10 largest DPs is shown in the following table:

Development Partners (NPR bn)	2000/01	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10
World Bank	4.16	3.20	1.67	3.80	5.29	4.51	4.16	5.34	8.74	8.33
ADB	7.30	4.06	1.63	3.36	2.88	3.32	5.32	6.00	6.91	6.96
Japan	3.28	3.03	3.75	4.23	3.50	3.59	2.63	2.55	2.79	1.57
UK	0.05	0.13	0.22	0.52	0.57	0.43	1.10	1.75	1.18	1.45
India	0.03	0.00	0.82	0.07	0.49	0.12	2.60	1.21	1.82	1.12
Korea	0.02	0.04	0.00	0.00	0.00	0.00	0.00	0.00	0.28	0.96
Germany	1.43	0.70	2.93	2.84	4.10	2.76	0.59	2.11	0.80	0.74
UNDP	0.01	0.00	0.00	0.01	0.72	0.56	0.55	0.45	0.26	0.72
Denmark	0.28	0.81	1.24	1.16	0.80	0.49	0.43	1.33	0.61	0.66
IFAD	0.14	0.11	0.14	0.11	0.14	0.11	0.14	0.24	0.36	0.46
Others	2.41	2.40	3.48	2.80	5.14	6.30	8.44	8.56	13.34	18.20
Total	**19.13**	**14.49**	**15.88**	**18.90**	**23.66**	**22.20**	**25.97**	**29.54**	**37.09**	**41.17**

Source: MOF, 2010a and FCGO

Changes in the relative DP rank over the past decade, based on share of on-budget disbursements, are presented below:

2000/01			2004/05			2009/10		
DP (NPR bn)	**Amount**	**%**	**DP**	**Amount**	**%**	**DP**	**Amount**	**%**
ADB	7.30	44.3%	World Bank	5.29	31.9%	World Bank	8.33	42.9%
World Bank	4.16	25.3%	Germany	4.10	24.7%	ADB	6.96	35.8%
Japan	3.28	19.9%	Japan	3.50	21.1%	Japan	1.57	8.1%
Germany	1.43	8.7%	ADB	2.88	17.4%	UK	1.45	7.5%
Denmark	0.28	1.7%	Denmark	0.80	4.8%	India	1.12	5.8%
Total for Top 5	**16.46**	**100%**		**16.58**	**100%**		**19.43**	**100%**

Source: MOF, 2010a

A review of sectoral trends in ODA over the past decade reveals a steady increase in DP support to health, education and overall social services (68% of disbursements combined), coinciding with a decline in funding of the economic sectors - agriculture, irrigation, forestry, transport, power and communications (23% of disbursements combined). This indicates a major investment by DPs in human development, notably through the two sector programs in health and education, and relative neglect of productive infrastructure.

Attachment D

Official Development Assistance and Development Partner Coordination

Year	2000/01	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	
Sectors (NPR bn)	**Amt.**	**Amt.**	**Amt.**	**Amt.**	**Amt.**	**Amt.**	**Amt.**	**Amt.**	**Amt.**	**%**
Agriculture, Irrigation and Forestry	3.77	3.29	2.18	2.43	2.60	2.40	3.72	3.86	2.29	6%
Transport, Power and Communication	9.24	5.91	7.77	7.57	9.86	7.14	6.66	6.71	6.30	17%
Industry and Commerce	0.02	0.37	0.40	0.15	0.12	0.11	0.12	0.08	0.16	0%
All Social Services	5.76	4.69	5.32	8.73	10.75	11.16	15.18	18.19	24.70	68%
Of which: Education	1.93	1.88	2.03	2.43	4.66	4.62	5.05	6.89	8.75	24%
and: Heath	0.64	0.38	0.65	0.52	1.10	1.95	3.28	4.34	5.36	15%
Others	0.01	0.14	0.21	0.04	0.33	1.30	0.17	0.46	2.91	8%
Total	**18.80**	**14.38**	**15.89**	**18.91**	**23.66**	**22.10**	**25.85**	**29.30**	**36.35**	**100%**

Source: MOF, 2010a

Currently, there are some 50 bilateral and multilateral Development Partners (DPs) and over 100 international non-governmental organizations (INGOs) operating in Nepal. The MoF is designated by the GoN to lead aid coordination and management, with the Foreign Aid Coordination Division (FACD) of the MoF entrusted to look after all matters relating to DP-provided external resources. FACD is in the process of rolling out a web-based Aid Management Platform (AMP) to capture data on external assistance to Nepal. The initial focus is on collecting information related to DP-supported programs, both on and off budget, with the intent to expand coverage to INGO spending in the next phase. This database is expected to contribute to better transparency and predictability through: (i) rolling three-year projections on disbursements for all projects, updated on an annual basis; (ii) regular reporting on actual disbursements both for on and off-budget projects; and (iii) geo-referencing of project activities to enable mapping across donors and across sectors.

As this is the first year of data entry in the AMP and the process is not yet complete, analysis of stocks and flows can only be considered indicative at this stage. Overall, about US$3.3 billion in ODA is available for disbursement in the future, of which US$2.6 billion (78%) will be channeled through the budget. The largest donors, in terms of approved funds ready for disbursement, include the Asian Development Bank, the World Bank, USAID, United Kingdom, United Nations, and the European Union (in descending order of importance). These 6 DPs account for about 78% of funding available to Nepal (see Table 1 below). At the sector level, the proportion of approved (undisbursed) funding for agriculture, energy, and health remains largely unchanged from previous years (7%, 15%, and 14%, respectively), while undisbursed funds available for education have declined (from 24% to 14%). Additional analysis of on and off-budget projects will be carried out in the final month of the FY (15 June – 15 July) to enable a more refined understanding of funding composition and availability (see Table 2 below).

The Paris Country Evaluation Report (2010) concluded that, while aid effectiveness has taken center stage as the conventional wisdom, adoption of Paris Declaration Principles remains low. The authors find that the political context has been the most significant factor influencing DP behavior. During the conflict, it was not feasible to increase the level of alignment, and what harmonization existed was focused on humanitarian and peace related responses. Since the peace agreement, some DPs have reinforced their support to GoN whilst others have continued to follow more unilateral approaches. A comparison of the findings of the two Paris Declaration surveys undertaken in 2008 and 2011 (2007 and 2010 data, respectively) is presented below, showing overall performance against the PD indicators by DPs in Nepal.

Indicators	2008 Results	2010 Results	OECD Target 2010
Aid on Budget (average per donor)	46%	58%	85%
Coordinated Technical Assistance	15%	48%	50%
Using Country Public Financial Management System	68%	63%	76%
Using Country Procurement System	56%	35%	N/A
Parallel Project Implementation Units (number)	106	68	64
In-year predictability	47%	55%	65%
Programme-based approaches	23%	31%	66%
Joint missions	23%	33%	40%
Joint country analytic work	28%	63%	66%

Table D-1 - Official Development Assistance by DP (USD)

Donor (nbr projects) [1/]	Actual Commitments	Actual Disbursement	Undisbursed Balance	FY11	FY12	FY13	FY14
				Actual Disbursemt	Planned Disbursemt	Planned Disbursemt	Planned Disbursemt
Asian Development Bank (63)	1,241,658,231	385,925,324	855,732,907	354,172,355	232,614,500	154,072,500	102,596,500
World Bank Group (25)	1,128,017,588	324,780,740	803,236,848	67,780,783	262,242,347	214,545,689	114,139,066
USAID (11)	442,000,000	63,970,000	378,030,000	30,800,000	-	-	-
United Kingdom (29)	338,164,296	123,585,997	214,578,299	24,245,989	52,178,904	19,405,220	13,220,955
United Nations (32)	174,645,807	18,945,218	155,700,589	9,281,475	5,098,018	130,000	-
European Union (44)	140,691,510	1,157,681	139,533,829	-	-	-	-
Germany (18)	350,230,906	255,588,585	94,642,320	1,776,389	9,770,115	3,663,793	-
Japan (11)	142,234,700	59,497,922	82,736,778	36,356,802	6,052,589	-	-
OPEC (6)	72,700,000	3,322,000	69,378,000	-	12,969,000	11,445,000	712,000
Finland (9)	81,121,437	17,527,642	63,593,795	14,658,990	16,344,864	16,999,539	12,927,855
India (7)	61,035,274	-	61,035,274	-	-	-	-
Norway (9)	92,714,886	36,112,458	56,602,428	15,990,441	12,598,659	5,558,232	-
Korea (3)	55,680,000	4,332,028	51,347,972	1,824,576	-	-	-
Denmark (17)	121,605,116	79,688,335	41,916,781	13,381,178	12,795,328	5,128,714	-
Australia (5)	43,627,432	10,044,277	33,583,155	2,794,268	9,887,157	9,887,157	4,298,764
Switzerland (26)	161,380,660	128,842,788	32,537,872	20,498,311	5,328,648	4,430,855	2,857,010
China (2)	21,960,325	-	21,960,325	-	-	-	-
GFATM (3)	42,423,453	20,635,324	21,788,129	15,479,746	-	-	-
Canada (6)	23,616,438	3,799,995	19,816,443	2,597,882	3,800,000	-	-
Saudi Arabia (1)	15,420,000	-	15,420,000	-	-	-	-
Netherlands (17)	15,393,902	-	15,393,902	-	-	-	-
GAVI (1)	14,540,690	-	14,540,690	-	-	-	-
Govt Agency/Ministry (4)	7,737,513	-	7,737,513	-	-	-	-
Nordic Development Fund (1)	6,762,468	-	6,762,468	-	-	-	-
KOWEIT (1)							
TOTAL (289)	**4,795,362,632**	**1,537,756,314**	**3,257,606,318**	**611,639,185**	**641,680,128**	**445,266,699**	**250,752,151**

[1/] AMP data entry is still on-going for a number of donors, so amounts are subject to change. ADB calendar year disbursement data is in the process of conversion to Nepali fiscal year.

Table D-2 - Official Development Assistance by Sector (USD)

Sector / Sub-Sector (nbr projects) [1/]	Actual Commitments	Actual Disbursements	Undisbursed Balance	FY11 Actual	FY12 Planned	FY13 Planned	FY14 Planned
ON BUDGET							
Agriculture, forestry, fishing (20)	264,397,123	76,547,273	187,849,850	38,617,059	44,396,154	44,112,601	10,433,276
Fuel and energy (19)	676,271,351	294,299,994	381,971,357	(1,369,693)	105,952,349	95,041,410	10,101,029
Transport (12)	393,145,493	198,337,884	194,807,609	65,070,107	48,806,033	32,528,294	18,863,430
Other Economic Sectors (24)	608,141,454	192,834,205	415,307,249	114,590,712	53,203,084	41,148,258	56,616,092
Education (11)	495,556,978	141,171,132	354,385,846	92,137,661	127,659,480	53,506,203	48,513,554
Environmental Protection (15)	84,019,009	40,632,612	43,386,397	29,838,444	2,741,209	3,778,295	2,018,920
General Public Service (10)	396,234,606	162,051,457	234,183,149	57,581,715	63,317,508	39,584,344	11,000,709
Health (12)	398,931,818	38,702,029	360,229,789	20,282,877	52,273,125	45,905,883	38,839,288
Housing and Community Amenities (2)	151,172,980	64,849,698	86,323,281	64,357,739	38,600,209	17,079,000	-
Public Order and Safety (7)	157,499,556	59,017,441	98,482,115	8,603,856	36,256,072	12,447,353	8,000,000
Recreation, Broadcasting, Culture (2)	9,020,000	42,000	8,978,000	42,000	1,674,000	6,857,000	-
Social Protection (12)	25,324,334	12,070,762	13,253,572	4,649,657	3,047,047	682,853	571,330
Water supply (7)	292,668,508	81,824,992	210,843,516	47,558,968	49,434,725	40,997,552	33,894,523
Unallocated (1)	1,500,000	-	1,500,000	-	-	-	-
TOTAL ON BUDGET (154)	**3,953,883,209**	**1,362,381,479**	**2,591,501,730**	**541,961,100**	**627,360,995**	**433,669,046**	**238,852,151**
Off Budget Projects (138)	841,479,423	175,374,835	666,104,588	69,678,085	14,319,134	11,597,653	11,900,000
TOTAL ON AND OFF BUDGET (289)	**4,795,362,632**	**1,537,756,314**	**3,257,606,318**	**611,639,185**	**641,680,128**	**445,266,699**	**250,752,151**

[1/] AMP data (including sector attributions) still in process of validation; disbursement estimates still being entered by DPs.

Attachment E
Results Framework

Country Strategic Areas & Key Issues	ISN Activities	World Bank Group Program (ongoing/planned)
Cross Cutting Theme 1: Strengthening Governance and Accountability		
Strengthening public financial management and procurement	> Roll out of Treasury System Account (TSA) in at least 50% of the district > Implementation of international standards in public sector accounting > Strengthen audit practice and enhance quality of audits > Support the implementation of government roll out of e-bidding > E-bidding operational in at least 2 municipalities	**Trust Fund Financing:** Multi Donor Trust Fund (MDTF) IDF on PPMO Emerging Towns Project
Promote Social Accountability (SA)	> Training and capacity building on SA provided both to government and CSOs > 5 SA resource centers established at district level > Mid-term impact evaluations conducted for SA pilot projects and 4 studies completed and disseminated	**Trust Fund Financing:** Program for Accountability in Nepal (PRAN)
Improving Regulatory Reform and Corporate Governance	> Public Private Dialogue (PPD) to have resulted in 50 procedures improved or eliminated by GON out of 200 reform recommendations proposed > SEZ component to have facilitated private sector participation in managing/developing zones as well as an investment in zones leading to the creation of 4000 new jobs by 2014.	**Lending/Technical Assistance:** IFC Investment Climate Reform Program
Improving fiscal and financing frameworks for local service delivery	> Revised systems and norms for intergovernmental fiscal transfers to municipalities adopted and implemented by the Ministry of Local Development > Revised systems and norms adopted and implemented for urban infrastructure financing by the Town Development Fund	**Lending/Technical Assistance:** Emerging Towns Project
Cross Cutting Theme 2: Fostering Gender Equality and Social Inclusion		
Operationalize gender and social inclusion framework into Bank operations and lending portfolios	> Incorporate gender and social inclusion considerations and strategies in all new operations > Regularly monitor gender impact during project implementation and portfolio reviews	**Planned Analytical Work/ TA:** Social Inclusion and Gender NLTA
Actively promote gender and social equality as well as inclusive development in Nepal	> Strengthen the capacity of country systems to implement gender and social inclusion concerns, policies and frameworks > Enable capacity-building of the Ministry of Women, Children and Social Welfare to allow it to effectively assume its responsibility of planning, programming and managing development activities related to gender	**Planned Analytical Work/ TA:** Social Inclusion and Gender NLTA
Strengthen government's capacity to better address the issues of IPs, natural resource management and development	> Facilitate broad consultation process to explore the relationship between natural resource usage, development interventions and indigenous groups. > Assist in developing policies, approaches, and operational recommendations that are sensitive to the needs and rights of Indigenous People	**Planned Analytical Work/ TA:** Indigenous People NLTA
Strengthen Bank's core diagnostics on Gender and Social Inclusion	> Integrate gender and social inclusion issues in the Nepal Living Standards Survey III and Poverty Assessment	**Planned Analytical Work/ TA:** NLSS III, National Poverty Assessment, Thematic Notes

Attachment E

PILLARS

Country Strategic Areas & Key Issues	Outcomes/Outputs by the end of the ISN Period	Indicators		World Bank Group Program (ongoing/planned)
		Baseline (2011)[31]	Target (2013)	
Pillar 1: Enhancing Connectivity & Productivity for Growth				
Energy > Poor reliability and low access to power	**Outcome 1: Increased access to electricity and improved reliability of power supply in the targeted areas as measured by:** • Number of households with access to electricity generated by micro-hydro schemes • MW of existing generation capacity rehabilitated • Cross border transmission construction underway	44,595[32] HH 0 0% tower foundation	80,742[33] HH 53MW 40% tower foundation completed	**Ongoing Lending:** Power Development (FY03) Poverty Alleviation Fund II (FY07) Kabeli Transmission* (FY11) Nepal-India Electricity Transmission and Trade* (FY11) **Planned Lending*:** Kabeli 'A' Hydroelectric (Jointly with IFC) (FY12) IFC's Hydropower Credit Line **Planned Analytical Work/TA:** IFC's Hydropower Sector Study IFC's Sustainable Energy Financing (FM Advisory)
Roads > Lowest road density in South Asia > Inadequate road network and poor road maintenance	**Outcome 2: Improved access to all season road in the Bank supported areas as measured by:** • Road constructed and upgraded ** • Road rehabilitated and maintained (including backlog maintenance)[34] ** Number of trail bridges constructed	Rural: 664 km Non-rural:285 km Rural: 2,225 km Non-rural: 800 km backlog+386 km periodic 143	Rural: 1305 km Non-rural: 297 km+130 km Rural: 4,500 km Non-rural: 1000 km backlog+750 km periodic 317	**Ongoing Lending:** Road Sector Development (FY08) Rural Access Improvement & Decentralization (FY04) **Planned Lending*:** Results Based Bridges (FY12) **Planned Analytical Work/TA:** Road Sector Assessment
Agriculture/ Irrigation > Low agriculture productivity > Inefficient irrigation system	**Outcome 3: Increased agriculture productivity as measured by** • Percent increase in productivity of selected crops • Number of irrigation schemes and areas rehabilitated	Potato: 10 MT/ha Paddy: 2.9 MT/ha Schemes: 16 Areas: 2,067 ha	Potato: 14 MT/ha Paddy: 3.5 MT/ha Schemes: 105 Areas: 17,180 ha	**Ongoing Lending:** Agriculture Commercialization and Trade (FY08) Irrigation and Water Resource Management (FY08) RJK Irrigation* (FY12, FY13) **Planned Lending*:** Third Poverty Alleviation Fund (FY13) Pilot Program for Climate Resilience (Jointly with IFC)
PSD/Access to Finance > Inadequate access to financial services in the rural areas	**Outcome 4: Enhanced access to micro finance as measured by:** • Number of borrowers access credit from Micro Finance Institution (MFI)	95,000 (99% women)	114,156 (99% women)	**Ongoing Lending:** Financial Sector TA* (FY03) IFC offer credit and trade lines and investment in bank equity **Ongoing Non-Lending:** IFC investment in MFI **Planned Analytical Work/TA:** Financial Sector Monitoring (FIRST)

[31]Most recent available data as of June, 2011
[32]Includes 41,000 from Power project+3,595 from PAF II
[33]Includes 74,000 from Power project + 6,742 from PAF II
[34]500 kms of periodic maintenance and 1000 km backlog of road maintenance undertaken each year.

PILLARS

Country Strategic Areas & Key Issues	Outcomes/Outputs by the end of the ISN Period	Indicators		World Bank Group Program (ongoing/planned)
		Baseline (2011)[31]	Target (2013)	
Pillar 2: Reducing Vulnerabilities and Improving Resilience				
Vulnerability/ Climate change and Disaster Reduction > Moderate to severely food insecure and food deficit at the national level > Weak cash transfer systems and not responsive to the vulnerable > Many rural poor have been excluded from mainstream development with few options to improve their livelihoods > Vulnerable to climate change effects- flood and droughts;	**Outcome 5: Reduced food insecurity among poor households as measured by:** • Percent of targeted households reporting increased ability to meet their food needs • Number of districts implementing improved cash transfer systems • Number of rural household beneficiaries with increased access to livelihood improvement options, of which female beneficiaries **Outcome 6: Reduced negative impact of climate change through sustainable energy and carbon finance as measured by:** • Green House Gas (GHG) emission reduced per year	 91% 0 Total: 258,000 Of which female: 159,960 0	 95% 10 Total: 460,000 Of which female: 230,000[35] 2,000 tons per year	**Ongoing Lending:** Social Safety Nets Project (FY09) Second Poverty Alleviation Fund (FY08) Peace Support Project* (FY07) **Planned Lending*:** Third Poverty Alleviation Fund (FY13) Global Agriculture and Food Security Program TF **Ongoing Analytical Work/TA:** Global Fund for Disaster Risk Reduction **Planned Analytical Work/TA:** Social Inclusion, Gender and Indigenous People **Ongoing Trust Fund :** Pilot Program for Climate Resilience (Jointly with IFC) IFC Sustainable Energy Finance South Asian Water Initiative Strategic Environmental and Social Assessment Food Price Crisis Response Global Fund for Disaster Risk Reduction
Pillar 3: Promoting Access to Better Quality Service				
Education > Low quality > Low enrolment at secondary level, in particular for disadvantaged groups and women > Relevance: school curriculum not relevant for job creation	**Outcome 7: Improved access to secondary and higher education as measured by:** • Increase in net enrolment rate for students in grade 9-12 • Increase in share of enrolment from disadvantaged groups in participating higher education institutions **Outcome 8: Enhanced quality and relevance of education as measured by:** • Number of market relevant programs delivered at the Bachelor's and Master's levels • Completion of student learning assessment (NASA) for grade 8 • Employment of project-supported graduates for at least 6 months	 23.9% Girls: 42% Dalits & educationally disadvantaged Janajatis: 12.8% 0 Initiated 0	 25% Girls: 43.4% Dalatis & educationally disadvantaged Janajatis: 13.2% disadvantaged Janajatis: 13.2% 10 Completed 80%	**Ongoing Lending:** Second Higher Education Project (FY06) School Sector Reform (FY10) Enhanced Vocational Education and Training* (FY11) **Planned Lending *:** School Sector Reform Additional Financing (FY12) **Ongoing Trust Fund:** Adolescents Girls Employment Initiative

[35]This is out of total target of 460,000
*Not expected to contribute to ISN outcomes

Attachment E

PILLARS

Country Strategic Areas & Key Issues	Outcomes/Outputs by the end of the ISN Period	Indicators		World Bank Group Program (ongoing/planned)
		Baseline (2011)[31]	Target (2013)	
Pillar 3: Promoting Access to Better Quality Service				
Health > Chronic malnutrition of children and pregnant women	**Outcome 9: Decreased malnutrition among pregnant women within the poorest quintile as measured by** • Increase in iron and folic acid (IFA) supplement **Outcome 10: Improved coverage of fully immunized children within the poorest quintile as measured by** • Percentage of fully immunized children **	70.5% 82.6%	72% 84%	**Ongoing Lending:** Second HNP and HIV/AIDS (FY10) **Planned Lending*:** First 1000 days (FY12) **Ongoing Analytical Work/TA:** Nutrition Policy Dialogue

* Not expected to contribute to ISN outcomes
** IDA Core Indicator

Interim Strategy Note for Nepal
FY12-FY13

ANNEXES

THE WORLD BANK GROUP

Annex A1

Key Economic & Program Indicators-Change from last ISN

Forecast in last ISN		Actual			Estimated		
Economy (CY)	FY08 *	FY08	FY09	FY10	FY11	FY12	FY13
Growth rates (%)							
Real GDP /a	4.5	5.3	4.4	4.6	3.5	3.0	3.4
Exports f.o.b. (y/y percent change in US $)	12.8	5.4	0.5	-6.1	8.5	7.0	7.0
Imports f.o.b. (y/y percent change in US $)	10.8	11.2	14.1	36.5	6.5	8.5	9.5
Inflation (period average %)	6	7.7	12.6	9.6	9.5	9.2	8.3
National accounts (% GDP)							
Current account balance	2.9	2.9	4.2	-2.4	-1.3	-1.5	-1.3
Gross investment/e	19.8	30.3	31.5	35.8	34.5	31.7	31.3
Public finance (% GDP)/a							
Fiscal balance	-3.2	-2.1	-3.1	-2.5	-2.1	-3.0	-3.0
Foreign financing	1.5	2.6	2.7	2.6	2.6	2.7	2.6
International reserves (in months of imports)	7.9	11.3	6	5.6	5.3	4.7	4.1
Program (Bank's FY)	FY08	FY08	FY09	FY10	FY11	FY12	FY13
Lending ($ million)	210	210	140.14	352.5	289	202	202
Gross disbursements ($ million)	100	80.62	176	127	238	225	235

/a.GDP at market price

Source:Central Bureau of Statistics (CBS)-2011 and Nepal Rastra Bank (NRB)

* Last ISN

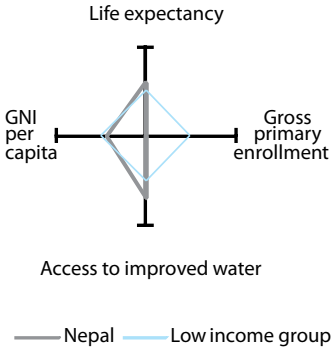
**Source:CBS and NRB

Annex 2-1

Nepal at a Glance

POVERTY and SOCIAL	Nepal	South Asia	Low-income
2009			
Population, mid-year (millions)	29.3	1,568	846
GNI per capita (Atlas method, US$)	440	1,082	512
GNI (Atlas method, US$ billions)	13.0	1,697	433
Average annual growth, 2003-09			
Population (%)	1.9	1.5	2.2
Labor force (%)	3.1	2.2	2.6
Most recent estimate (latest year available, 2003-09)			
Poverty (% of population below national poverty line)	31	..	..
Urban population (% of total population)	18	30	29
Life expectancy at birth (years)	67	64	57
Infant mortality (per 1,000 live births)	39	55	76
Child malnutrition (% of children under 5)	39	41	28
Access to an improved water source (% of population)	88	87	64
Literacy (% of population age 15+)	58	61	66
Gross primary enrollment (% of school-age population)	..	108	104
Male	..	110	107
Female	..	105	100

Development diamond*

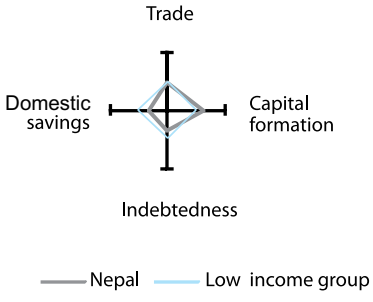


Key Economic Ratios and Long-Term Trends

	1989	1999	2008	2009
GDP (US$ billions)	3.5	5.0	12.6	12.5
Gross capital formation/GDP	21.5	20.5	31.8	29.7
Exports of goods and services/GDP	11.1	22.8	12.1	15.7
Gross domestic savings/GDP	10.3	13.6	11.2	8.0
Gross national savings/GDP	13.5	27.2	29.5	28.9
Current account balance/GDP	-7.6	4.3	2.9	4.3
Interest payments/GDP	0.8	0.6	0.3	0.3
Total debt/GDP	38.5	60.0	29.2	29.4
Total debt service/exports	16.1	6.8	4.1	3.8
Present value of debt/GDP	..	..	..	21.8
Present value of debt/exports	..	..	..	59.2

	1989-99	1999-09	2008	2009	2009-13
(average annual growth)					
GDP	4.9	3.7	5.3	4.7	..
GDP per capita	2.4	1.6	3.4	2.8	..
Exports of goods and services	..	0.5	-3.4	38.4	..

Economic ratios*



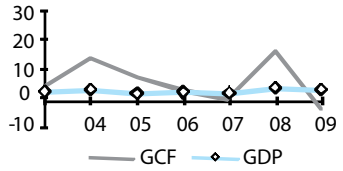
Annex 2-1 Nepal at a Glance (con't)

Structure of the Economy

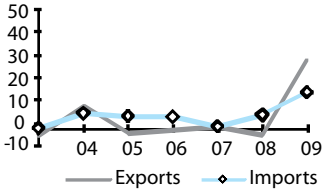
	1989	1999	2008	2009
(% of GDP)				
Agriculture	50.4	41.3	33.7	33.8
Industry	16.5	21.8	16.7	15.9
Manufacturing	5.7	9.5	7.4	7.0
Services	33.1	36.9	49.6	50.2
Household final consumption expenditure	79.7	77.5	78.8	80.9
General gov't final consumption expenditure	10.0	8.9	10.0	11.1
Imports of goods and services	22.3	29.7	32.7	37.4
	1989-99	**1999-09**	**2008**	**2009**
(average annual growth)				
Agriculture	2.4	3.3	4.7	2.2
Industry	7.5	3.0	1.9	1.8
Manufacturing	10.2	1.2	0.2	-0.5
Services	6.3	4.1	7.1	5.9
Household final consumption expenditure	..	3.6	3.3	5.5
General gov't final consumption expenditure	..	6.4	6.8	19.3
Gross capital formation	..	6.8	20.4	-3.1
Imports of goods and services	..	4.6	7.5	20.2

Note: 2009 data are preliminary estimates.
This table was produced from the Development Economics LDB database.
* The diamonds show four key indicators in the country (in bold) compared with its income-group average. If data are missing, the diamond will be incomplete.

Growth of capital and GDP (%)



Growth of exports and imports (%)

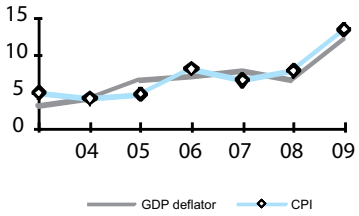


Annex A2-2 Nepal at a Glance (con't)

Prices and Government Finance

	1989	1999	2008	2009
Domestic prices				
(% change)				
Consumer prices	8.3	11.4	7.7	13.2
Implicit GDP deflator	1.3	8.9	6.7	12.1
Government finance				
(% of GDP, includes current grants)				
Current revenue	8.7	11.5	15.8	24.3
Current budget balance	-2.0	2.1	3.9	7.6
Overall surplus/deficit	-11.5	-3.9	-2.8	-4.3

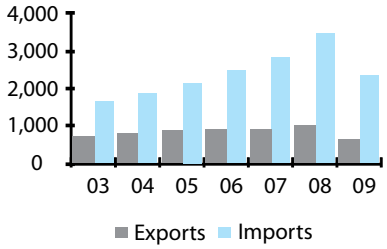
Inflation (%)



Trade

	1989	1999	2008	2009
(US$ millions)				
Total exports (fob)	163	763	913	576
Food	..	55	202	165
Pulses	..	53	32	6
Manufactures	..	199	613	357
Total imports (cif)	636	1,390	3,414	2,290
Food	73	112	244	158
Fuel and energy	44	219	413	253
Capital goods	190	266	370	408
Export price index (2000=100)	..	..	..	..
Import price index (2000=100)	..	..	..	..
Terms of trade (2000=100)	..	..	..	..

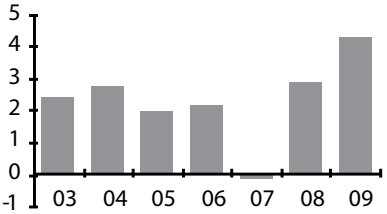
Export and import levels (US$ mill.)



Balance of Payments

	1989	1999	2008	2009
(US$ millions)				
Exports of goods and services	384	1,107	1,603	1,597
Imports of goods and services	748	1,584	4,234	4,456
Resource balance	-363	-477	-2,631	-2,859
Net income	-13	25	122	153
Net current transfers	107	671	2,812	3,245
Current account balance	-269	218	364	539
Financing items (net)	260	-63	92	-48
Changes in net reserves	9	-155	-456	-491
Memo:				
Reserves including gold (US$ millions)	218	797	2,143	2,221
Conversion rate (DEC, local/US$)	25.3	68.0	64.9	76.6

Current account balance to GDP (%)



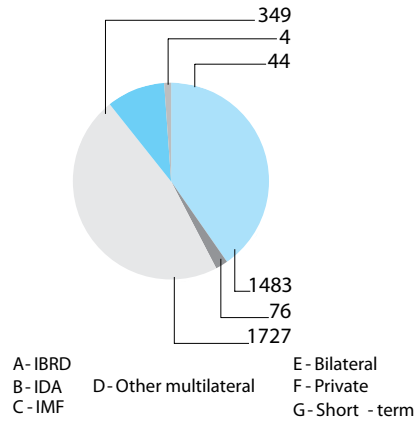
Annex A2-2 Nepal at a Glance (con't)

External Debt and Resource Flows

	1989	1999	2008	2009
(US$ millions)				
Total debt outstanding and disbursed	1,356	3,020	3,685	3,683
IBRD	0	0	0	0
IDA	572	1,147	1,507	1,483
Total debt service	62	108	162	177
IBRD	0	0	0	0
IDA	6	22	50	51
Composition of net resource flows				
Official grants	170	148	710	763
Official creditors	221	111	-23	-13
Private creditors	-9	-13	-1	-1
Foreign direct investment (net inflows)	0 4	1	38	
Portfolio equity (net inflows)	0 0	0	0	
World Bank program				
Commitments	193	85	17	156
Disbursements	110	48	31	7
Principal repayments	2	14	39	41
Net flows	108	34	-8	-33
Interest payments	4	8	12	11
Net transfers	104	25	-20	-44

Note: This table was produced from the Development Economics LDB database.

Composition of 2009 debt (US$ mill.)



Annex B2

Nepal Selected Indicators* of Bank Portfolio Performance and Management of June 30, 2011

Indicator	2008	2009	2010	2011
Portfolio Assessment				
Number of Projects Under Implementation [a]	16	16	15	17
Average Implementation Period (years) [b]	3.0	3.4	3.5	3.9
Percent of Problem Projects by Number [a, c]	6.3	18.8	20.0	18.0
Percent of Problem Projects by Amount [a, c]	6.6	15.2	22.0	16.0
Percent of Projects at Risk by Number [a, d]	25.0	31.3	73.3	41.0
Percent of Projects at Risk by Amount [a, d]	19.8	35.4	69.8	44.0
Disbursement Ratio (%) [e]	25.7	31.1	24.6	33.4
Portfolio Management				
CPPR during the year (yes/no)	yes	yes	yes	yes
Supervision Resources (total US$)	1,636	1,901	2,050	2,163
Average Supervision (US$/project)	102	112	108	103

Memorandum Item	Since FY 80	Last Five FYs
Proj Eval by OED by Number	73	5
Proj Eval by OED by Amt (US$ millions)	1,538.0	136.9
% of OED Projects Rated U or HU by Number	37.5	60.0
% of OED Projects Rated U or HU by Amt	27.6	48.1

a. As shown in the Annual Report on Portfolio Performance (except for current FY).
b. Average age of projects in the Bank's country portfolio.
c. Percent of projects rated U or HU on development objectives (DO) and/or implementation progress (IP).
d. As defined under the Portfolio Improvement Program.
e. Ratio of disbursements during the year to the undisbursed balance of the Bank's portfolio at the beginning of the year: Investment projects only.
* All indicators are for projects active in the Portfolio, with the exception of Disbursement Ratio, which includes all active projects as well as projects which exited during the fiscal year.

Note: This table was produced from the Development Economics LDB database.

Annex B3

IDA - Indicative Lending Program Summary[1]

FISCAL YEAR	PROJECT NAME	US$(M)
2011 [2]	Road Sector Development Project AF	75.0
	Enhanced Vocational Education and Training Project	50.0
	Poverty Alleviation Fund AF	65.0
	Emerging Towns Project	25.0
	Kabeli Transmission Project	38.0
	Strengthening Regional Cooperation for Wildlife Protection in Asia	3.0
	Cross-Border Transmission Project[3]	33.0
	Total FY11 Actual	**289.0**
2012	Rani Jamara Kulariya Irrigation Project - Phase 1	
	Kabeli "A" Hydroelectric Project	
	School Sector Reform Project AF	
	First 1000 Days	
	Results-Based Bridges Project	
2013	Agriculture Commercialization and Trade AF	
	Poverty Alleviation Fund III	
	Emerging Towns Expansion	
	Rani Jamara Kulariya Irrigation- Phase 2	
	North-East Trade and Transport Facilitation[4]	
2012	**Recipient-Executed Trust Funds**	
	PPCR - Building Resilience to Climate-Related Hazards	
	PPCR - Enhancing Climate Resilience of Endangered Species	
	Global Agriculture and Food Security Program (GAFSP)	
	Scaling Up Renewable Energy	
	Social Protection Pilot Program	

[1] The IDA envelope for the ISN period (FY12-13) of SDR 268.3 million is indicative. Actual allocations in these years will depend on (i) total IDA resources available, (ii) the country's performance rating; (iii) the performance and assistance terms of other IDA borrowers; (iv) the terms of IDA's assistance to Nepal (grants or credits), and (v) the number of IDA-eligible countries. US$ equivalent is dependent on prevailing exchange rate.
[2] Actual.
[3] Country portion of the regional project.
[4] Regional project.

(I) IFC Investment Operations Program

	2008	2009	2010	2011*
Original Commitments (US$m)				
IFC's Own Accounts only	0.44	15	14	12.6
Participants	--	--	--	--
IFC and Participants	0.44	15	14	12.6
Original Commitments by Sector (%)- IFC Accounts only				
Electric Power			47	
Finance & Insurance	100	35	53	98
Transportation & Warerhousing			65	
Collective Investment Vehicles				2
Total	**100**	**100**	**100**	**100**
Original Commitments by Investment Instrument (%) - IFC Accounts only				
Equity		2	2	
Guarantee	100	33	51	98
Loan		65	47	
Total	**100**	**100**	**100**	**98**

* Data as of June 30, 2011

Annex B3

(ii) IFC - Indicative Program Summary

Sector/ Business Line	Project Name/Details
Access to finance/ Financial inclusion (AS)	> FM advisory with WB on financial infrastructure relating to e-payments, credit information bureaus, secured transaction registries > Microfinance (MF) advisory service projects involving new product development, enhancing capacity in deposit mobilization, risk management, human resource and MIS > Sustainable Energy Financing (SEF) involving developing banks' portfolio for SEF by supporting banks' investments for on-lending to energy efficient (EE) projects > SME Banking involving SME department restructuring of a commercial bank in order to enhance staff capacity and quality of SME portfolio
Financial Sector (IS)	> Credit and trade lines to local banks ; supporting commercial banks by equity investments > Support MF banks/institutions to scale up their operations to under-banked and underserved regions
Investment Climate (AS)	> IFC and IDA collaborating to execute IFC led Nepal Investment Climate Reform Program (NICRP) focusing on Regulatory Reform, supporting the Nepal Business Forum; and assisting with the establishment of Special Economic Zones. > South Asia Regional Trade and Integration (SARTI)
Sustainable Business Advisory (SBA)	> Poultry Supply Chain Strengthening Project working with SME farms and two lead firms in the poultry sector > Two Climate Investment Fund (CIF) pilot programs with IDA & ADB- Pilot Program for Climate Resilience (PPCR) and Scaling-up Renewable Energy (SREP). > SME Ventures Fund: A new IFC Fund that provides a combination of investment products and advisory services to SME entrepreneurs
Infrastructure (IS)	> Planned support for small hydropower projects through credit line to selected local banks > Kabeli Hydroelectic Generation: IFC and IDA plan to contribute to the 37MW project > Nyadi Hydropower Project: IFC to invest in the 30MW project > SREP: IFC to co-design and implement the project with ADB and WB

* This table includes activities in addition to the results framework because of longer time periods expected for these projects to generate results than the ISN two year period

Annex B4

Indicative Non-Lending Activities[1] (IDA)

Task	Completion FY
Recent Completions	
Public Expenditure Review	FY10
Social Impact Assessment of Rural Energy	FY10
Migration and Remittances	FY10
Annual MTEF	FY10
Revitalizing Agriculture	FY10
South-South Exchange Trust Fund Peace Building	FY10
Fiscal Federalism	FY10
Information Infrastructure for Connectivity	FY10
Local Governance Strategy	FY11
Annual MTEF	FY11
Investment Climate Assessment	FY11
Social Protection Programmatic TA	FY11
Gender and Social Inclusion	FY11
Support to Municipalities	FY11
Input to Road Sector Assessment	FY11
Analysis of Fiscal Space	FY11
Nutrition Dialogue	FY11
Underway/Planned – AAA	
Programmatic Area 1: Economic & Financial Key Issues and Results Monitoring	
Economic Updates	FY12-FY13
Financial Sector Monitoring (FIRST)	FY12-FY13
ISN Portfolio Monitoring and Geo-coding	FY12
Annual MTEF	FY12-FY13
Programmatic Area 2: Strengthening Governance and Accountability	
Governance Issues (GPF)	FY12
PFM Strengthening (MDTF)	FY13
Social Accountability (PRAN-TF)	FY13
Programmatic Area 3: Enhancing Connectivity and Productivity for Growth	
Road Sector Assessment	FY12
NLSS Thematic Notes	FY12-FY13
ESMAP NLTA	FY12
Programmatic Area 4: Poverty, Gender and Social Inclusion	
Poverty Assessment	FY12
NLSS Thematic Notes	FY12-FY13
Gender, Social Inclusion and Indigenous People (TF)	FY12
Programmatic Area 5: Reducing Vulnerabilities and Improving Resilience	
Water Resource and Climate Change (SAWI)	FY12
Disaster Reduction NLTA (GFDRR)	FY13
Nutrition NLTA (SAFANSI TF)	FY13
Strategic Environmental and Social Assessment	FY12

[1]Includes activities funded from Bank Budget and Bank-Executed Trust Funds.

Annex B5

Social Indicators

	Latest single year			Same region/income group	
	1980-85	1990-95	2002-08	South Asia	Low-income
POPULATION					
Total population, mid-year (millions)	17.0	21.6	28.8	1,545.1	976.2
Growth rate (% annual average for period)	2.4	2.5	2.0	1.5	2.1
Urban population (% of population)	7.4	10.9	17.2	29.5	28.7
Total fertility rate (births per woman)	5.6	4.7	2.9	2.9	4.0
POVERTY *(% of population)*					
National headcount index	..	..	30.9	..	..
Urban headcount index	..	..	9.6	..	..
Rural headcount index	..	..	34.6	..	..
INCOME					
GNI per capita (US$)	160	200	400	963	523
Consumer price index (2000=100)	20	58	127	127	132
Food price insex (2000=100)	24	71	104	-	-
INCOME/CONSUMPTION DISTRIBUTION Share of income or consumption					
Gini index	..	..	47.3	..	..
Lowest quintile (% of income or consumption)	..	..	6.1	..	..
Highest quintile (% of income or consumption)	..	..	54.2	..	..
SOCIAL INDICATORS					
Public expenditure					
Health (% of GDP)	..	..	2.0	1.1	2.3
Education (% of GDP)	2.3	2.8	3.8	2.9	3.4
Social security and welfare (% of GDP)	..	..	..	0.0	0.0
Net primary school enrollment rate *(% of age group)*					
Total	..	62	79	86	80
Male	..	82	84	88	82
Female		41	73	84	78
Access to an improved water source *(% of population)*					
Total	..	78	89	87	67
Urban	..	96	94	94	86
Rural	..	76	88	84	60
Immunization rate *(% of children ages 12-23 months)*					
Measles	34	56	79	75	78
DPT	32	54	82	71	80
Child malnutrition (% under 5 years)	..	..	39	41	27
Life expectancy at birth *(years)*					
Total	51	57	67	64	59
Male	51	57	66	63	58
Female	51	58	67	65	60
Mortality					
Infant (per 1,000 live births)	117	83	41	58	76
Under 5 (per 1,000)	171	117	51	76	118
Adult (15-59)					
Male (per 1,000 population)	376	350	199	246	295
Female (per 1,000 population)	395	376	175	173	254
Maternal (modeled, per 100,000 live births)	..	..	830	500	790
Births attended by skilled health staff (%)	..	7	19	42	44

Note: 0 or 0.0 means zero or less than half the unit shown. Net enrollment rate: break in series between 1997 and 1998 due to change from ISCED76 to ISCED97.
Immunization: refers to children ages 12-23 months who received vaccinations before one year of age or at any time before the survey.
World Development Indicators database, World Bank - 23 April 2010.

Annex B6

Key Economic Indicators

Indicator	Actual			Estimate		Projected	
	FY07	FY08	FY09	FY10	FY11	FY 12	FY 13
Real GDP (annual percent change)	**3.3**	**5.3**	**4.4**	**4.6**	**3.5**	**3**	**3.4**
National accounts (% of GDP at current market prices)							
Gross domestic product	100	100	100	100	100	100	100
Agriculture[a]	32.5	31.7	33.0	35.0	35.7	35	35.1
Industry[a]	16.6	16.8	15.8	15.0	14.6	14.7	14.5
Services[a]	50.9	51.5	51.2	50.1	49.8	50.3	50.4
Total Consumption	90.2	90.2	90.6	92.6	93.3	93	93
Gross domestic fixed investment	21.1	21.9	21.4	20.2	18.0	21	21
Government investment	3.4	4.0	4.5	4.5	3.8	6.8	6.9
Private investment	17.7	17.8	16.9	15.7	14.2	14.2	14.2
Current account (% of GDP)	**-1.4**	**2.7**	**4.2**	**-2.4**	**-1.3**	**-1.5**	**-1.3**
share of Exports, f.o.b.	8.4	7.6	7.0	5.4	5.4	5.3	5.2
share of Imports, f.o.b.	26.2	26.7	28.1	31.4	31.0	30.8	30.9
Savings (% of nominal GDP)							
Gross domestic savings	9.8	9.8	9.4	7.4	6.7	7	7
Gross national savings	28.6	33.2	35.9	32.3	30.9	30.3	29.9
Memorandum items							
Gross domestic product at market prices/a (in billion US$)	10.3	12.6	12.9	15.7	16.9	18.5	20.2
Gross domestic product per capita (US$)	372	444	446	536	566	609	653
Real annual growth rates (%, calculated from 2000/01 prices)							
Gross domestic product at market prices/b	3.4	6.1	4.4	4.6	3.5	3	3.4
Gross domestic product per capita /b	1.2	3.8	2.1	2.3	1.2	0.7	1.1
Balance of Payments (in millions of U.S. dollars)							
Exports (GNFS) /b	1,434.8	1,513.0	1,587.3	1,535.6	1,613.8	1,716.6	1,825.9
Merchandise FOB	872.3	953.1	904.1	848.8	921.0	985.4	1,054.4
Imports (GNFS) /b	-3,540.6	-3,938.8	-4,429.9	-5,833.6	-6,160.0	-6,865.4	-7,500.2
Merchandise FOB	-2,701.6	-3,352.2	-3,611.1	-4,926.7	-5,246.9	-5,692.9	-6,233.7
Net current transfers	1,829.9	2,811.7	3,226.5	3,797.5	4,165.4	4,515.1	4,992.7
(including official current transfers)							
Current account balance	-12.8	364.2	535.9	-378.0	-220.6	-268.6	-267.8
Net private foreign direct investment /e	5.6	4.3	23.7	38.3	84.0	70.0	50.0
Memorandum items							
GDP at current market prices	10,324.7	12,550.0	12,852.1	15,709.6	16,900.0	18,500.0	20,200.0

Annex B6

Key Economic Indicators (con't)

Indicator	Actual				Estimate	Projected	
	FY07	FY08	FY09	FY10	FY11	FY 12	FY 13
Annual growth rates							
Merchandise exports	2.6	5.4	4.9	-3.3	5.1	6.4	6.4
(FOB)		9.3	-5.1	-6.1	8.5	7.0	7.0
Merchandise imports	13.9	11.2	12.5	31.7	5.6	11.5	9.2
(FOB)	24.1	7.7	36.4	6.5	8.5	8.5	9.5
Public finance (as % of GDP at current market prices) /c							
Total revenue	11.9	12.9	14.2	15.2	15.4	15.3	15.7
Total expenditure	15.9	17.4	19.8	20.2	20.1	21.0	21.7
Current expenditures	10.6	11.2	12.9	12.9	12.8	13.5	13.5
Capital expenditures and net lending	5.3	6.2	6.9	7.2	7.3	7.5	8.2
Overall deficit before grant	-4.0	-4.6	-5.7	-5.0	-4.7	-5.7	-6.0
Overall deficit after grants	-1.8	-2.1	-3.0	-2.5	-2.1	-3.0	-2.9
Domestic financing	1.5	2.0	3.0	2.4	2.2	2.6	2.4
Foreign financing	2.5	2.6	2.7	2.6	2.5	3.1	3.6
Monetary indicators							
M2/GDP (at current market prices)	54.3	60.7	63.8	61.5	59.4	58.1	-
Growth of M2 (%)	14.0	25.2	27.3	14.1	9.6	10.1	-
Private sector credit growth /	75.8	77.7	78.8	77.2	74.9	73.2	-
total credit growth (%)							
Price indices(2000 =100)							
Real effective exchange rate						-	-
(end of period, y/y percent change)	5.6	-3.7	3.1	6.3	2.7		
Consumer price index (% growth rate)	6.4	7.7	12.6	9.6	9.5	9.2	8.3

a. GDP components are estimated at factor cost.
b. "GNFS" denotes "goods and nonfactor services."
c. Fiscal year ends in mid-July. Data here refers to central government operations as contained in the budget.
Source:Central Bureau of Statistics (CBS)-2011; Nepal Rastra Bank (NRB); staff estimates and projections.

Annex B7
Key Exposure Indicators

Indicator	Actual				Projected		
	FY07	FY08	FY09	FY10	FY11	FY 12	FY 13
Total debt outstanding and disbursed (TDO) (US$m)[a]	3,777	3,789	3,810	3,912	3,898	3,803	3,672
Net disbursements (US$m)[a]	62	-23	-16	38	8	-49	-96
Total debt service (TDS) (US$m)[a]	147	162	177	198	207	217	228
Debt and debt service indicators (%)							
TDO/(XGS and remittances)[b]	32	26	24	21	19	17	15
TDO/GDP	37	30	30	25	23	21	18
TDS/(XGS and remittances)[b]	1	1	1	1	1	1	1
Concessional/TDO	86	87	87	85	86	86	86
IBRD exposure indicators (%)							
IBRD DS/public DS	..	..	..	..	..		
Preferred creditor DS/public DS (%)[c]	75	77	78	81	80	83	85
IBRD DS/XGS	..	..	..	..	..		
IBRD TDO (US$m)	..	..	..	..	..		
Share of IBRD portfolio (%)	..	..	..	..	..		
IDA TDO (US$m)	1,559	1,537	1,490	1,463	1,467	1,453	1,429
IFC (US$m)							
Loans	32.6	28.1	33.0	27.5	20.6		
Equity and quasi-equity	1.8	1.3	0.9	0.4	0.2		

a. Includes public and publicly guaranteed debt, private nonguaranteed, use of IMF credits and net short-term capital.
b. "XGS" denotes exports of goods and services, including workers' remittances.
c. Preferred creditors are defined as IBRD, IDA, the regional multilateral development banks, the IMF, and the Bank for International Settlements.

Annex B8

Operations Portfolio (IBRD/IDA and Grants)

As of July 6, 2011

Closed Projects	**81**
IBRD/IDA *	
Total Disbursed (Active)	605.82
of which has been repaid	0.00
Total Disbursed (Closed)	482.45
of which has been repaid	290.64
Total Disbursed (Active + Closed)	892.52
of which has been repaid	290.64
Total Undisbursed (Active)	884.65
Total Undisbursed (Closed)	0.00
Total Undisbursed (Active + Closed)	884.65

Active Projects		Last PSR Supervision Rating			Original Amount in US$ Millions			Difference Between Expected and Actual Disbursements[a/]		
Project ID	Project Name	Development Objectives	Implementation Progress	Fiscal Year	'IDA^	GRANT	'Cancel.	Undisb.	Orig.	Frm Rev'd
P087140	Agriculture Commercialization and Trade	S	S	2009	20.0			18.3	2.8	
P100342	Avian Flu	S	MS	2007	18.2		2.2	2.6	4.3	2.0
P104015	Enhanced Vocational Education & Training			2011	50.0			50.9		
P099296	Irrig & Water Res Mgmt Proj	MS	MU	2008	64.3			43.2	19.4	15.3
P071291	NP Financial Sector Technical Assistance	MU	MU	2003	16.0		6.5	0.7	5.3	
P113002	NP Social Safety Nets Project	S	S	2009	64.5			17.4	(26.7)	2.4
P105860	Poverty Alleviation Fund II	HS	S	2008	192.5		0.0	94.9	(2.4)	
P043311	Power Development Project	MS	U	2003	164.8		0.8	123.6	21.0	57.9
P112893	Kabeli Transmission Project			2011	38.0			38.1		
P110762	Peace Support Project	MS	MS	2008	50.0			27.3	27.7	11.7
P095977	Road Sector Development Project	S	S	2008	117.6			66.5	(10.2)	6.9
P083923	Rural Access Improve. & Decentralization	MS	MS	2005	77.0			46.9	2.5	4.9
P071285	Rural Water Supply & Sanitation Project	MS	MS	2004	52.3			8.7	(17.3)	
P120265	Emerging Towns Project			2011	25.0			25.5		
P113441	School Sector Reform Program	MU	MU	2010	130.0			88.3	12.2	
P117417	Second HNP and HIV/AIDS Project	S	S	2010	129.2			110.1	8.0	
P090967	Second Higher Education Project	MU	MU	2007	60.0			42.6	8.0	

Active Projects		Last PSR Supervision Rating			Original Amount in US$ Millions				Difference Between Expected and Actual Disbursements[a/]	
Project ID	Project Name	Development Objectives	Implementation Progress	Fiscal Year	'IDA^	GRANT	'Cancel.	Undisb.	Orig.	Frm Rev'd
P118179	Rani Jamara Kulariya Irrigation Project			2012	43.0			43.0		
P121210	Strengthening Regional Coop For Wildlife Protection in Asia *			2011	3.00			3.0		
P115767	Nepal-India Electricity Transmission and Trade Project*			2011	33.00			33.0		
TF056440	CDCF: Nepal biogas Support Program	S	S	2006		7.0		5.0	2.0	
TF058031	NEPAL: Biogas Support Program IV Project	S	S	2007		5.0		3.2	1.8	
TF092561	IDF-NEPAL: Strengthening Institutional Capacity of the	MU	U	2008		0.3		0.1	0.2	
TF093397	Pro Poor Targeted Secondary School Stipend	MU	MU	2009		1.9		1.6	0.3	
TF094724	NEPAL: FCPF Readiness Grant			2009		0.2		0.2	-	
	NEPAL: FCPF Preparation Grant					3.2		3.2	-	
TF096287	NEPAL' Adolescent Girls Employment Initiative			2010		2.1		1.7	0.4	
TF090264	NEPAL Micro Hydro Project					2.0		2.0	-	
TF098235	EFA-FTI School Sector Reform Project	MS	MS	2010		120.0		90.0	30.0	
TF099675	IDF: Strengthening Institutional					0.5		0.5	-	
	Capacity of the Dept of National Parks & Wildlife Conservation for the Effective									
	Mgmt of Protected Areas			2011						
Overall Result					**1,348.3**	**142.1**	**9.5**	**884.7**	**54.5**	**101.0**

* regional projects
^ country portion of regional IDA

Annex B8 (IFC)

Committed and Disbursed Outstanding Investment Portfolio
As of 6/30/2011
(In USD Millions)

		Committed					Disbursed Outstanding				
				**Quasi					**Quasi		
FY Approval	Company	Loan	Equity	Equity	*GT/RM	Participant	Loan	Equity	Equity	*GT/RM	Participant
1996/ 1997/ 1998/ 1999/											
2000/ 2001	Himal Power	2.2	-	-	-	-	2.2	-	-	-	-
1998	Bhote Koshi	1.5	-	-	1.0	1.4	1.5	-	-	1.0	1.4
1998	Jomsom Resort	4.0	-	-	-	-	4.0	-	-	-	-
2008/ 2009/ 2010/ 2011	Bank of Kathmandu	-	-	-	2.2	-	-	-	-	2.2	-
2009	Buddha Air Nepal	8.8	-	-	-	-	8.8	-	-	-	-
2009	Smartchoice	-	0.4	-	-	-	-	-	-	-	-
2009/ 2010/ 2011	Himalayan Bank	-	-	-	0.2	-	-	-	-	0.2	-
2009/ 2010/ 2011	NIC Bank	-	-	-	0.02	-	-	-	-	0.02	-
2010	Butwal Power co	6.5	-	-	-	-	-	-	-	-	-
2010	Nirdhan MFB	-	0.3	-	-	-	-	0.2	-	-	-
2011	Laxmi Bank Ltd	-	-	-	0.7	-	-	-	-	0.7	-
2010/ 2011	NIBL Nepal	-	-	-	0.03	-	-	-	-	0.03	-
2011	Ventures Nepal	-	0.3	-	-	-	-	-	-	-	-
	Total Portfolio:	**23.0**	**0.9**	**0.0**	**4.2**	**1.4**	**16.5**	**0.2**	**0.0**	**4.2**	**1.4**

* Denotes Guarantee and Risk Management Products.
** Quasi Equity includes both loan and equity types.

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