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TECHNICAL ASSISTANCE REPORT

on the

NEPAL HOUSING DEVELOPMENT FINANCE COMPANY

Prepared for

**Ministry of Housing and Physical Planning, Nepal
Regional Office of Housing and Urban Development
(RHUDO/Bangkok), USAID/Nepal**

Prepared by

Daniel S. Coleman

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May, 1992

TECHNICAL ASSISTANCE REPORT

ASSISTANCE TO THE NEPAL HOUSING DEVELOPMENT FINANCE COMPANY

APRIL 1992

1. Introduction.

The purpose of this trip was to continue to assist the Nepal Housing Development Finance Company to become operational. It follows an earlier trip in June of 1991, during which time I assisted the NHDFC to prepare a Business Plan and to schedule a program of activities which would permit the Company to initiate its planned programs. This second trip was more focused on helping the NHDFC to prepare the documents and plans it would need to implement specific programs as a part of its overall mandate to undertake a saving and loan operation in Nepal.

This trip report is composed of five sections, as follows:

- **Progress to Date**, which discusses NHDFC's progress during the nine month period between my two visits;
- **Assessment of NHDFC's Prospects**, which covers my assessment of the Company's future and offers some solutions for resolving the problems that are identified;
- **The Scope of Work**, which details the accomplishments during this visit based on the scope of work for the assignment;
- **Next Steps**, which discusses what needs to be carried out over the short term and who will do it; and
- **Recommendations and Conclusions**, which is self-explanatory.

2. Progress to Date.

Progress since my departure has been much slower than anticipated. The Business Plan, which was prepared in conjunction with the NHDFC, contained a Bar Chart which showed the key activities to be carried out over the following year and a timetable for achieving those activities. However, the Company is now about six months behind where it had expected to be at this time in its operations, that is only about three months of planned work has occurred over the nine month period. Of the four initial activities that were deemed so crucial in getting the Company off and running, the status is as follows:

- Complete the Business Plan and secure the Board's approval. This has been achieved, however the plan is now being updated to take into account the delays as discussed above as well as

a request from the IFC for more detailed marketing information.

- Prepare and submit a banking application to Rastra (Central) Bank. The Rastra Bank's approval was obtained, however, a license to operate the Company still has not been received from the Department of Commerce, as required under the Finance Companies Act of 1985.
- General Manager undertakes a study tour to HDFC/India. This trip occurred although it was as a part of a training exercise held at the HDFC/I training center outside Bombay. The GM therefore was unable to spend any significant time studying the operational aspects of comparable financial institutions in India.
- Negotiate a Technical Assistance package with HDFC/I and donor agencies. This is still in progress although no agreements have yet been reached.

In addition to these four key activities, the NHDFC has made some progress in other areas, as follows:

- The Board decided to initiate an Experimental Lending Program, using Rs2.4 million in interest earnings on the shareholders capital. A basic program was approved, which focused on small loans of up to Rs100,000 for the expansion, completion and improvement of homes and Rs 150,000 for new construction.
- As a first step in implementing this program, an announcement was placed in the newspaper to ascertain interest in the Program, and a stab was made at preparing some of the lending forms required for its implementation.
- A computer was purchased, although until its arrival, the Company is using a loaner from the vender. Also the Company has investigated software requirements and has tentatively selected a banking program called MicroBanker, by Oracle to help manage its savings and loan program.
- A lawyer has been retained to advise the Company and vet the various documents and forms being prepared for the Experimental Lending Program.

During my second stay here, the Company's staff and I prepared a draft of the Lending Guidelines and Procedures, completed all the forms required for the Lending Program and obtained the temporary secondment of a lending officer from another agency of the Government. Also a draft of the Market Analysis, as required by the IFC, was prepared, using the recently published (March 92) UNCHS financed report on the Nepal Shelter Sector for the basic information. The schedule in the Business Plan has been revised

while other necessary changes in this same Plan have been discussed, and in some cases, key sections rewritten.

3. Assessment of NHDFC's Prospects.

The slow pace of NHDFC's progress so far raises many questions. On the one hand, if the slow pace is merely endemic to Nepal, then it is probable that situation will simply continue the way it is now, and eventually the institution may or may not be successful. On the other hand, if the slow pace is symptomatic of some underlying problems in the Company, then something must be done to rectify the situation in order to ensure the Company's success. I believe there is something fundamentally wrong with the way the Company is organized and managed.

My overall assessment of the situation is that the General Manager has been given a mandate to develop the NHDFC, but he has not been given the necessary tools to carry out this mandate. Developing the NHDFC implies initiating mortgage lending programs as well as resource mobilization programs. To do this requires trained staff in disciplines related to these activities. Since the General Manager is not a trained Banker, nor is the one professional who is seconded from the Government to assist him, it is necessary for the Company to hire these types of professionals.

While the Government and his Board have not stopped him from hiring trained bankers, serious obstacles have been encountered. If he attempts to hire a professional banker from the private sector, he will have to pay double, triple or even more than what the Government and his Board will allow the NHDFC, as a Government Bank, to pay. Therefore he cannot hire from the private sector because he cannot meet the salary demands. On the other hand, if the General Manager attempts to hire someone from the public sector banks, he is faced with asking that person to leave a secure position to go to a possibly insecure position in a new institution at the same salary, something that so far, has been impossible to arrange. The best he has been able to do so far is to obtain the temporary services, as of April 19, 1992, of a banker from another government program for a two week period.

An alternative solution currently being explored is to hire a Banker who has retired from one of the public banks. With his retirement pay, a relatively low salary from NHDFC may be sufficient. However, the General Manager has to be sure that the lifelong habits he has acquired from working at a poorly managed government bank are not passed on to the NHDFC.

Staff has been only one of the tools the General Manager has been denied. Training opportunities have been lost, equipment purchases delayed and basic management decisions postponed. All of this has cost the NHDFC time and effort.

There are three fundamental reasons, in my opinion, why the NHDFC finds itself in the position of being given a mandate yet unable to fill that mandate.

- **Reason # 1.** The first and foremost reason is that the NHDFC is a public or government institution and is operating like one. It is clear that a government bank's way of doing business is simply antithetical to the proper management and operation of any sort of profit oriented enterprise. Yet because of the ownership, composition of the Board and influence of the Government, NHDFC is functioning exactly as a government agency or institution.

The above mentioned Shelter Sector Study makes some pointed comments about the different types of financial institutions in Nepal. In talking about the two Government controlled banks, it says "...bad loans to the public sector are large....there are weaknesses in internal accounting, information systems, and management. Overall profitability is near zero." About the two Government owned development banks, it says "Both development banks have consistently registered poor profit results, due to bad loan repayment, management weaknesses, and external pressures." But about the three Joint Venture Banks, which are privately controlled, it says "Their success can be attributed to a higher level of service, professionalism, and access to international networks."

My perception is that the NHDFC is going the route of the Government owned and controlled banks--not the Joint Venture Banks. As long as it operates as a government bank, it will function like a Government Bank, with its attendant problems.

- **Reason # 2.** The second reason is the relationship between the Board of Directors and the General Management. Actually there are two problems here. One is the active involvement by the Board in the day-to-day operations of the Company, which by all management guidelines should not be permitted. But this appears to be quite common in the government sector in Nepal, where lines of responsibility are very unclear, and active involvement by the Boards of the various parastatals in day-to-day management is the rule. A corollary to this problem is the fact that of the six Board members, five members work for government or government owned institutions, therefore the government mentality is imposed on the Board's actions.
- **Reason # 3.** The final reason has to do with the ability of NHDFC to have access to assistance in management and operational areas where it lacks experience. One of the hallmarks of the Joint Venture Banks, as mentioned above,

was their "access to international networks." NHDFC does not have any sort of access so far, although efforts to obtain technical assistance from various donors would in some degree obviate the need for an international network of information and assistance. This problem is all the more acute due to the inability of NHDFC to recruit well trained private sector bankers. While some technical assistance has been made available to date through USAID and GTZ, it is far from adequate.

My suggestions for resolving NHDFC's fundamental problem as mentioned above are as follows:

- **Solution # 1. Private or Public Sector Control.**

Move forward as quickly as possible to put the NHDFC under private sector management and control. As a first step the Board should be reconstituted. The Board of Directors is now composed of one representative of a government ministry, one from the National Insurance Agency, one from a Joint Venture Bank and three from Government Banks. I recommend that two of the three Government bank representatives resign from the Board of Directors, and instead, the remaining directors appoint two representatives from the private sector to the Board until the next Annual Meeting. This will leave a Board composed of three representatives of the Public Sector and three from the Private Sector. At the least this will balance the board between the two sectors. And if and when the IFC acquires shares in the Company, its representative will become the seventh member of the Board, which will effectively give the private sector control of the Company. (The Law governing the Company permits up to seven Board members.)

- **Solution # 2. Board and Management Responsibilities.**

For the sake of good management, it is important to clarify the role and responsibilities of management and the Board. As a first step, management should prepare, for the Board's approval, an outline of the role and responsibility of the Board as well as of managements'. Along with this analysis, job descriptions of the key positions, including the Directors of the Board of Directors and the three principal managerial positions (General Manager, Operations Manager and Lending Manager) should be prepared. A first draft of this effort is contained in Attachment A of this report.

- **Solution # 3. An International Network.**

The NHDFC should move quickly to establish an international network, which can be done if the Company begins to function as a private bank. There are two possibilities here. A

foreign bank engaged in similar banking activities could acquire an equity interest in the NHDFC. Such was proposed in 1988, with HDFC/India expected to acquire a small equity interest in the Company, thereby giving NHDFC access to HDFC/India's information and management network. There is a reason to believe that could not occur today.

Alternately a donor agency could provide sufficient funds for NHDFC to hire the short- and long-term expertise it needs from outside sources, somewhat along the lines being proposed by HABITAT today.

Both solutions would meet most of NHDFC's need for an assistance network, and in fact the two solutions are not exclusive. Combining both of these solutions might be the best of all possible worlds.

4. The Scope of Work.

The Scope of Work called for the Consultant to assist the NHDFC in a number of areas. The results of my work with NHDFC in these areas are as follows:

a) Assist the NHDFC in the overall implementation of the Business Plan, with emphasis in several sub-areas.

- Target groups. With the assistance of the recently published HABITAT financed study, "Nepal Shelter Sector Background Report, March 1992, NHDFC was able to better identify the target group for its initial lending program, the Experimental Lending Program. In the beginning, the target group will be families with incomes in the upper 50th percentile (but not the highest few percent) of Kathmandu's population. As the Company gains experience and profitability, it will seek to serve families in the lower income strata.
- Types of Loans. The Company has also decided to limit its lending program to loans for home improvement, completion and expansion as well as loans to lot owners to initiate the construction of a home. Loan ceilings will be Rs 100,000 and Rs 150,000 respectively. With the experience gained from this initial lending activity, other types of lending programs, as yet identified, will be considered. (See Page 5 of Attachment B of this report)
- Loan Marketing. Instead of preparing a loan marketing program, the Company has prepared a market analysis to determine the feasibility of the Experimental Lending Program. Once this small program is underway, the Company will focus on ways to expand the program and thus prepare marketing programs to sell the expanding lending programs.

- Public Offering. Given the delays in initiating the savings and loan programs to date, the Company is not in a position to prepare a prospectus for a public offering at this time. It is anticipated that once the Company initiates its programs, converts to a more privately held company and welcomes foreign investor(s), it will be ready to prepare the documentation for a public offering.
- Savings Schemes. The HABITAT Housing Finance Advisor, Mr. George Joseph, was recently in Kathmandu to assess the prospects for UN assistance to the NHDFC. As a part of his trip report, he reviewed the various savings mobilization schemes that might be appropriate for the Company to pursue. It is expected that on his return visit to Nepal in May, 1992, he will work with the NHDFC on selecting one or more of these schemes to implement in the near future. It was therefore felt that it was more appropriate for him to continue his efforts in this area rather than me.
- Program Guidelines. General operational guidelines were prepared for the Experimental Lending Program, which are described more fully later in this report. The preparation of savings guidelines are contingent on identification of the specific types of savings programs to be implemented, which will be determined with the assistance of the HABITAT housing finance advisor.

b) Assist NHDFC develop its organizational structure and suggest manpower requirements and propose job descriptions of the critical positions (section/division heads).

In my earlier assignment, I recommended a specific staffing pattern for a saving and loan operation, with back office support. This has not changed, however, given the management/board division of labor problem, more specific suggestions are made with respect to the role and responsibilities of each were made. Along with this analysis, job descriptions of the Board of Directors, General Manager, Lending Manager and Operations Manager were prepared. (See attachment A of this trip report).

c) Make specific recommendations on the scale at which NHDFC should function with details on organizational aspects.

Numerous discussions were held with the NHDFC's General Manager and his staff about how the Company should function in order to carry out its mandate to provide mortgage loans to qualified borrowers. The purpose of these conversations were to assist NHDFC's staff to comprehend its role as a lending institution and to prepare itself organizationally to carry out this role. However, no specific recommendations were made, other than those already proposed and accepted in the Business Plan.

d) Assist NHDFC in the implementation of the Experimental Lending Program (EL), including:

- Development of guidelines for the evaluation of the applications;
- Preparation of an Operation Manual & MIS, including computer applications;
- Assistance in the preparation of a lending policies manual.

A comprehensive Lending Guidelines and Procedures Manual was prepared, which included the various forms and contracts required to implement the program. Prior to my arrival, some work had been done with respect to preparation of the forms. This work was then completed, along with the Guidelines and Procedures. Also the forms and guidelines were and will continue to be reviewed by a local lawyer to insure that they are legal and appropriate for the program. (See attachment C of this trip report. Please note that the many forms are not attached--although they have been prepared--since some were prepared in Nepali and some in English for later translation to Nepali).

It should also be pointed out that in addition to completion of the Scope of Work as outlined above, I undertook to revise the Business Plan prepared last year. This included:

- Rewriting the Market Analysis to reflect the new information from the HABITAT study;
- Revising the section on Mortgage Lending to cover the Experimental Lending Program;
- Adding the financial statements and analyses from the first year audited statements and the first nine months of this financial year; and
- Recalculating the five year financial projections.

5. Next Steps.

There are a number of steps or activities that are underway and should be continued regardless of any political decisions being considered. After each activity listed below is the deadline for completing the activity, and the name of the staff person primarily responsible for ensuring that the activity is done.

- Experimental Lending Program (ELP). The Lending Guidelines and Procedures must be finalized and the English documents translated into Nepali. The Lawyer on retainer to the NHDFC must approve the Guidelines and all the accompanying

documents and forms. The documents must then be printed in sufficient numbers to satisfy the expected demand for applications.

Deadline: May 31, 1992
Responsibility of: J. Prahdan

- Hiring a Legal Assistant and an Office Assistant. These two positions are required to implement the EL. Therefore they should be filled no later than 2 weeks prior to initiating the ELP.

Deadline: 2 weeks prior to ELP opening
Responsibility: J. Joshi

- Preparation of the Unit Cost Estimating System. This system is required in order for the NHDFC to verify the value of the improvements as requested by the applicant. It must be completed prior to initiating the ELP.

Deadline: May 15, 1992
Responsibility: D. Manndhar

- Obtain permission from Department of Commerce. This is crucial. If this license is not received by the time the EL is started, it is possible that there will be a delay. The Lawyer must be encouraged to assist in this matter.

Deadline: May 15, 1992
Responsibility: J. Joshi

- Lending Officer. Mr. Prahdan will complete his secondment with NHDFC on the 1st of May. If he or someone else with similar qualifications is not employed after that date, then the ELP will grind to a halt. He must be continued in this job or a replacement found.

Deadline: May 1, 1992
Responsibility: J. Joshi

- Reconstitution of NHDFC's Board.

Deadline: May 31, 1992
Responsibility: M. Mathema

- Preparation of draft of proposal for NHDFC management organization and job descriptions.

Deadline: May 15, 1992
Responsibility: D. Coleman

- Rewrite the Business Plan to update and to incorporate the

revised market analysis and submit it to the IFC.

Deadline: May 31, 1992
Responsibility: D. Coleman

5. Recommendations and Conclusions.

A. Conversion to a Private Sector Organization.

I believe that the prospects for NHDFC's success are good if the following occurs:

- NHDFC becomes a private sector organization;
- NHDFC's management and Board develop a good and complementary relationship; and
- NHDFC is able to hire good staff, supported by a reasonable level of technical assistance.

If these events do not occur over the next three months or so, then I would advise the NHDFC to close its doors and distribute the remaining assets to its shareholders. The alternative is the continued operation of just another Government bank with all the problems, inefficiencies and losses that go hand in hand with government parastatals.

Given the crucial nature of private sector control of the NHDFC, I strongly recommend that USAID should only consider continuing to provide assistance to the NHDFC if and when the institution is converted to a private sector institution. In my opinion, the conversion would essentially take place when 2 of the 3 board members from the Government controlled banks resign and are replaced by private sector representatives.

I would recommend further that the IFC condition its equity contribution on the conversion of the NHDFC to a private sector company.

B. Technical Assistance.

Technical assistance is crucial for the Company to survive and succeed. The only prospect on the horizon for this aid is HABITAT, which is considering providing up to \$300,000 to the housing finance sector, part or all of which would be allocated to NHDFC. My memo to Dr. Joshi (Attachment C) gives my suggestions as to the best use of these funds. In my opinion, unless these funds are made available to NHDFC, it will be almost impossible for the Company to make any progress.

C. The Experimental Lending Program.

To initiate this Program, NHDFC must employ the services of a full-time lending officer. Without such a person on board, NHDFC should not initiate the ELP. At this time, it would appear the Mr. J. Pradhan, who has been seconded from another government agency to work in this capacity with NHDFC, would be an appropriate person for this position, and in my memo to Dr. Joshi, I confirmed this recommendation (see Attachment D). However, I still believe and recommend that he should spend at least one week in Bombay studying the lending operations and procedures of HDFC/I before the Company initiates the Experimental Lending Program.

ATTACHMENTS:

- A. Management Structure
- B. Lending Guidelines and Procedures
- C. Memo on Technical Assistance
- D. Memo on the Lending Officer

MANAGEMENT STRUCTURE

The organizational structure of NHDFC is relatively straight forward and apparently follows common practice in Nepal. In the Company's articles of incorporation, the Board of Directors is given a broad mandate for managing the Company, much in line with what all Nepali public companies--private and government owned--are given. In fact, the articles of incorporation intentionally follow the guidelines given in the Finance Companies Act of 1985 under which NHDFC is incorporated. In turn, the Board appoints a General Manager who is given responsibility for managing the Company's activities. The General Manager at this time is not a member of the Board, although it is possible for him to be a member, in which case, he would then be the Managing Director.

It has never been made clear within the Company the extent and limit of the Board's authority and responsibility with respect to those of the Company's management, as reflected by the General Manager. The purpose of this exercise is to attempt to provide the NHDFC with some basic guidelines in this matter.

First, the role and responsibility of the Board of Directors.

- The primary function of NHDFC's Board should be to set the overall policies and direction of the Company. The goals and objectives as expressed in the Business Plan are clearly those of the Board of Directors, and it is only the Board that can and should changes those directives.
- The second major function of the Board is to approve the initiatives and activities requested by NHDFC's management. Again in the Business, the initiatives and activities are the savings and loans programs, with the terms and conditions of each program. The Board does not have the expertize to design these programs--only management can do that--but it does have the responsibility to approve them.
- The third major Board function is to name the General Manager. In this respect the Board should make it very clear to the General Manager what it expects from him, i. e. his mandate, and concomitantly, provide him with the necessary resources to fulfill that mandate.

If the Board of Directors of NHDFC acts responsibility with respect to the three functions listed above, it will have more than fulfilled its role.

Next is the role of Management vis-a-vis the Board of Directors.

The most important function of the General Manager is to take responsibility for the day-to-day management of the Company. This in fact has nothing to do with the Board, it is merely a statement

of fact. But it is an important statement of fact in that, if accepted by the Company, it precludes the Board of Directors from taking any role whatsoever in the day-to-day management of the Company. Of course, in the event the Board is not satisfied with the day-to-day management of the Company, it should in most instances replace the General Manager, rather than take on his responsibilities. The truth is that the Board, by its very nature, is not qualified to manage the Company on a daily basis. Given this truism, what are the functions of the general management of the Company.

- First of all, the General Manager is responsible for keeping the Board fully informed and aware of all matters relevant to the Board's responsibilities. This sort of communication is crucial not only to the Board's ability to carry out its functions properly, but also to maintain an open dialogue between the Board and management. If the Board is not aware of what is going on in management's quarters, then the Board will in all likelihood make incorrect decisions based on inadequate information. In this light, management should provide the Board with full and comprehensive agendas for Board meetings as well as periodic status reports on the Company's condition and results.
- The second function of NHDFC's management is to prepare the plans, programs and budgets which the Board will approve and management will execute. Planning, programming and budgeting are critical management functions, without which NHDFC cannot properly carry out its mandate.
- The third major function of the General Manager is to select his management team. Since the General Manager will work with his staff on a day-to-day basis, and moreover is responsible for their performance, he and he alone should select those staff members. The Board should in no way involve itself in the selection process.

If the Board agrees to the three major management functions as listed above, while at the same time, limits itself to its three major functions, NHDFC will have made a significant step to putting into place a strong and sensible management system, albeit a simplified system. Establishing a good working relationship is more than words on paper, but it is a good start.

Finally it is true that the Board/management relationship outlined above is based on the Western model of business management. The Nepali culture and mores may be such that this relationship will not work or perhaps not work too well, however, it should be tried, given that the Nepali way has not necessarily worked well either. Institutions such as NHDFC also have a responsibility to bring about change, particularly if they expect to compete with successful companies that are to a large degree based on Western management practices.

In an effort to clarify the responsibilities and duties of both NHDFC's Board and management, simplified job descriptions for the four key positions have been prepared. These positions include Director (of the Board of Directors), General Manager, Lending Manager and Operations Manager. By adopting these job descriptions, even in the form they are now, would in a sense be adopting the management structure outlined in this paper.

JOB DESCRIPTION

DATE: _____

TITLE: General Manager

MAJOR FUNCTION: Manage the day-to-day activities of the Company

REPORTS TO: The Board of Directors

COMPENSATION: Rs _____ to Rs _____

MINIMUM QUALIFICATIONS: An MBA, M. Econ. or M. Com., plus 10 experience in a senior managerial post, preferably with a financial institution. Must be a fluent English speaker.

JOB DUTIES:

1. Select and hire all Company employees.
2. Prepare an annual operating budget for submission and approval by the Board.
3. Direct the Company's strategic planning activities.
4. Approve all loans for amounts of less than Rs 100,000.
5. Lead the Company's efforts to raise additional capital.
6. Ensure the implementation of the Company's lending and resource mobilization programs.
7. Prepare the agenda and documents required for Board meetings.
8. Motivate and train the Company's employees.
9. Report monthly in writing to the Board the status of the Company's activities and programs.
10. Set up programs to monitor and measure the Company's progress.
11. Coordinate and liaise with HMG and the Public.
12. Act as the Company's representative in public functions and with the Shareholders.

JOB DESCRIPTION

DATE: _____

TITLE: Lending Manager

MAJOR FUNCTION: Manage the Company's Mortgage Lending Portfolio and Programs

REPORTS TO: General Manager

COMPENSATION: Rs _____ to Rs _____

MINIMUM QUALIFICATIONS: An MBA or M. Com., plus 5 years as an officer of a Bank, of which 2 years were as a senior lending officer. English proficiency required.

JOB DUTIES:

1. Manage the day-to-day mortgage lending programs and activities.
2. Design and implement mortgage lending programs.
3. Prepare and maintain the Company's Lending Guidelines and Procedures.
4. Recommend qualified borrowers for mortgage loans.
5. Appraise or have appraised collateral to back up mortgage loans.
6. Administer the lending portfolio, in conjunction with the Accounting Department, and collect delinquent and past due loans.
7. Prepare loan packages for the approval of the appropriate Approval Body.

JOB DESCRIPTION

DATE: _____

TITLE: Operations Manager

MAJOR FUNCTION: Manage the internal operations of the Company, including the resource mobilization activities.

REPORTS TO: General Manager

COMPENSATION: Rs _____ to Rs _____

MINIMUM QUALIFICATIONS: An MBA or M. Com., plus 5 years experience in a senior managerial position in a bank. English proficiency required.

JOB DUTIES:

1. Manage the day-to-day administrative functions of the Company.
2. Design, implement and manage resource mobilization programs.
3. Manage the financial accounts.
4. Prepare the financial reports in an accurate and timely manner.
5. Supervise the teller, cash receipts and payments, and the safe keeping operations of the Company.
6. Provide for the security and accounting of cash money.
7. Undertake all cash and financial management functions.
8. Advise the General Manger of personnel requirements and sugest staffing arrangements.
9. Manage the management information systems.
10. Administer the general service and support systems.
11. Prepare and maintain the Administrative Manual.

JOB DESCRIPTION

DATE: _____

TITLE: Director

MAJOR FUNCTION: As a member of the Board of Directors, to ensure that the Company is efficiently and profitably managed.

REPORTS TO: The Shareholders

COMPENSATION: Rs _____, per Board meeting attended

QUALIFICATIONS: Not applicable; Elected by Shareholders

JOB DUTIES:

1. Select and hire the General Manager.
2. Approve the annual operating budget presented by Management.
3. Set compensation ranges for all Company employees.
4. Approve all loans in excess of Rs 500,000.
5. Designate one Board member to sit on the Credit Committee.
6. Approve all lending programs.
7. Approve all resource mobilization programs.
8. Publish an annual report to Shareholders.
9. Prepare and modify the Company By-Laws.
10. Authorize issuance of new share capital.
11. Authorize issuance of new debt instruments.
12. Authorize payment of dividends.

15

LENDING GUIDELINES AND PROCEDURES MANUAL**Introduction.**

The purpose of this manual is to provide guidance and direction for NHDFC's lending division and staff in the granting of mortgage loans. It is primarily based on a small lending operation, more specifically the Experimental Lending Program which the NHDFC intends to initiate in the next few months. It also presupposes a relatively small lending division, probably with one Lending Officer and a minimum of two Clerks: a legal assistant and an office assistant. The volume of work may dictate that additional staff be hired. It should be pointed out that these guidelines and procedures can and should be changed and modified as the NHDFC gains in experience and its operations grow. Moreover they should be constantly reviewed to insure that they are adequate to meet the lending tasks. Whenever there is a need to make changes in the guidelines and procedures in the lending task, this manual has to be updated simultaneously.

This Manual is organized by chapters, with each chapter covering a specific aspect of the lending procedure. Chapter 1 discusses the organization of the mortgage lending division and the filing system. Chapter 2 is a description of each of the various loan programs being offered by the NHDFC. (As of the preparation of this Manual, only one program, the Experimental Lending Program, is being offered.) The remaining chapters (3 through 8) cover each of the six separate lending processes or operations necessary to grant a mortgage loan. These processes are:

-**The Application Process**, which involves the gathering of information from a prospective borrower necessary to determine whether a loan can be made;

-**The Verification Process**, which involves determining whether the information submitted on the application form;

-**The Mortgaging Process**, by which the loan in question is secured by one or more pieces of collateral;

-**The Approval Process**, which covers the presentation of the loan request to the approving body;

-**The Closing Process**, which occurs if the loan is approved, and results in the NHDFC handing over the loan proceeds in part or whole to the borrower; and

-**The Collection Process**, which covers the repayment of the loan.

Attached to each Chapter on the lending processes are the various forms required for the particular process.

Some of the key definitions used in this manual are given below:

"Applicant", a person or persons applying for a mortgage loan;

"Borrower", the status an applicant reaches when he secures a mortgage loan;

"Lending Officer", the NHDFC staff member responsible for processing a mortgage loan;

"Appraiser", the NHDFC consultant or staff member responsible for carrying out property appraisals;

"Clerk", the office or legal assistant who works for the Lending Officer in the NHDFC;

"Collateral", the underlying real property that secures the mortgage loan;

"Approval Body", any one of three bodies or persons authorized to approve or disapprove a mortgage loan;

CHAPTER 1

ORGANIZATION OF NHDFC

The department in charge of mortgage lending is the Mortgage Loan Division. Normally, this Division will be headed by a Mortgage Lending Manager, with one or more lending officers and clerks reporting to him. As mentioned earlier, this division will initially be staffed by a lending officer, who may also function as acting division manager, and two clerks who will be responsible for the filing system and any legal chores such as title review.

Before beginning lending operations, the Division must set up an application filing system and procedures. The first step is to assign the responsibility for maintaining a filing log to the first lending officer hired by NHDFC. This lending officer will then set up the system for assigning an application number for each and every application filed.

The file system will be maintained on an annual basis. The number system will consist of the last 2 digits of the current year, for example, 92 for 1992. Each application submitted in the year 1992 will begin with 92; for 1993, the first 2 digits will be 93, and so on. A space (-) will then be entered after the first two digits. The next three digits in a particular year (or 4 as volume increases in later years), beginning with 001, will be assigned to each applicant, in sequence. For example the file number 92-125, indicates that it is the 125th application written up in 1992. A log will be kept also, which gives the name of the applicant, the file number and the date the application was made. Processing an application can only be initiated after the application information is entered in the log. All unused applications will be kept in a central location together with the application log for ready access by the Lending Officers.

CHAPTER 2

THE LENDING PROGRAMS

This chapter contains a description of each of NHDFC's lending program. Each program must contain the following information:

1. The Name of the Program.
2. The amount of funds reserved for this Program (if applicable).
3. The maximum amount of a loan granted under this Program.
4. The term (tenor) of the loan.
5. The interest rate.
6. The grace period (principal and/or interest), if applicable.
7. Geographic restrictions.
8. Fee required, with a schedule.
9. Family income restrictions, if any.
10. Collateral requirements.
11. Any other terms and conditions that are relevant to a particular program.

The following pages describe each of the lending programs.

PROGRAM NO. 1

1. Name: Experimental Lending Program
2. Funds Available: Rs 2.4 million
3. Maximum loan amount:
 - a) Up to Rs 100,000 for home improvement, completion and expansion loans.
 - b) Up to Rs 150,000 for new home construction loans.
4. Tenor: 5 years for a) above and 7 years for b) above.
5. Interest rate: 18.5% (18.0% if the collateral property is insured.)
6. Grace Period: None
7. Geographic restrictions: Inside Kathmandu's ring road.
8. Fee Requirements: See Lending Manual
9. Family income restrictions: Family income must exceed monthly mortgage payment by a factor of three.
10. Collateral requirements: The value of the collateral property must be double the amount of the loan.
11. Other conditions: Borrower must take out a Term Life Insurance Policy equal to the amount of the loan balance.

CHAPTER 3

THE APPLICATION PROCESS

3.1 Applications can only be made by the person or persons requesting the loan. Applications will be accepted only at an office of the NHDFC. Each applicant will be assigned to a lending officer who is responsible for processing the loan from the initial application step discussed here through the closing step.

3.2 When a potential applicant enters the NHDFC office with the intention of requesting a loan, the receptionist will give him or her (hereafter all persons are referred to in the masculine tense) a copy of the loan program Information Sheet to read (See Attachment A). The purpose here is for applicants, by studying the Information Sheet, to perhaps realize that they will not qualify for the loan program in question and thereby eliminate themselves. But, if after reading the Information Sheet, the applicant still believes he is qualified, the receptionist will lead the applicant in to meet a lending officer. If the Lending Officer is busy, then the applicant may meet with an Assistant to discuss the lending program as indicated in the paragraph below. If neither the Lending Officer nor an Assistant is available, then the applicant may wait for the next available staff member or come back later. Applicants are received on a first come, first serve basis. No appointments are accepted.

3.3 The Information Sheet must clearly state the fee schedule and when each fee is due. The applicant must be informed by the receptionist, as stated on the information sheet, that the application fee must be paid at this initial meeting. If the applicant does not have cash or a check with him, he cannot begin the application process.

3.4 When the applicant is seated, the Lending Officer (or the Clerk) will ask him a number of pertinent questions to ensure further that the applicant is apparently qualified and is ready to begin the application process. Questions include:

- Applicants and Co-Applicants income;
- Uses of this income;
- Amount of loan to be requested;
- Type of improvements contemplated;
- How the loan will be repaid.

This initial interview should take no more than 5 minutes. Once the Lending Officer ensures himself that the applicant is serious, he can then initiate the lending application process. (If an Assistant has been meeting with the applicant up to this point, and the Assistant has determined that he is qualified, he must turn the

applicant over to a Lending Officer to complete the application process; the Assistant is not qualified to take an application.)

3.5 The next step is very important. The Lending Officer tells the applicant that before continuing further, he must pay a loan application processing fee as follows:

Fee	Loan Amount
Rs500	Rs0-100,000
Rs600	Rs100,001-200,000
Rs700	Over 200,001

He will explain that the purpose of the fee is to pay for the cost of processing the application. The loan processing fee is not refundable and is paid in cash or cheque.

3.6 Other fees to be paid during the lending procedure are as follows:

-An appraisal fee is paid directly to the appraiser appointed by the NHDFC, with the amount based on a sliding scale percentage of the final appraised value of the collateral as determined by the appraiser and agreed to by NHDFC. (See paragraph 8.3 of this document for the fee schedule);

-A Mortgaging Fee of Rs250, per collateralized property, which will be deducted from the loan proceeds;

-Registering deed costs are borne by the applicant.

3.7 Once the application fee is paid, the Lending Officer goes to the central location to obtain an Application Form. At the same time, he fills in the application log, entering the applicant's name, the day's date and the next number in sequence. He enters the same information on the Application Form, making sure that the first three pieces of information on the log and on the form are identical.

3.8 The Application Form is a 6 section document which must be filled out carefully and completely in order to initiate the lending procedure (Attachment B). It is the job of the Lending Officer to complete the Application Form in the presence of the applicant by asking him to answer questions as they appear on the Application Form. Completing the Form should take between 30 and 60 minutes. If the applicant is not prepared to provide the information, either because he does not have it, or has forgotten something, or for some other reason, then the application process is deferred. The Application Form is put aside until the applicant returns with the missing information. If the applicant does not return within 30 days, his Application Form is voided and the fee is forfeited. The file number in the application log is also

voided.

3.9 If there is more than one applicant, then the Application Form must be completed for all the applicants. In this case, more time will be needed to complete the Application Form.

3.10 After the Lending Officer completes the Application Form, he takes out a Loan Worksheet (Attachment C) on which he makes some preliminary calculations to assure himself that the applicant meets all the basic loan criteria. These criteria are:

-The applicant must have Nepali citizenship;

-The real property to be mortgaged must be located in the Kathmandu valley;

-The total monthly income of the applicant and co-applicants after deducting other monthly debt service payments must exceed the monthly loan payment by a factor of 3.

-The amount of the loan will not be less than 60% of the appraised value of the collateral.

3.11 The applicant(s) sign and date the Application Form. The Lending Officer then gives the applicant a Documents List Sheet (Attachment D) on which is listed the various documents and certificates the applicant must obtain in order for the application to be complete. The Lending Officer will write on the Documents List in the appropriate spaces, the name of the applicant, the application number and the name of the Lending Officer. The applicant then leaves the NHDFC office with clear instructions to obtain all these documents before returning to the Office. (Bringing the documents to the office one by one is not acceptable; all documents must be brought in together.)

3.12 When the applicant returns to the NHDFC office with all the required documents, he gives them to the same Lending Office whose name appears on the Documents List. The Lending Officer then reviews each document to ensure that it is correct. He attaches all the documents to the Application Form. At this point, the Application Form is complete.

3.13 Forms that are required for this process are:

-A. Information Sheet

-B. Application Form

-C. Loan Worksheet

-D. Documents List

CHAPTER 4

THE VERIFICATION PROCESS

4.1 The next step is to verify the information on the Application Form. There are three separate evaluations that must take place, as follows:

-Credit Review, which encompasses a assessment of the applicants income and ability to pay;

-Title Review, which ascertains that the title to the collateralized property is clear; and

-Loan Request Review, which confirms that the amount of the loan requested is adequate to the cover the use of the loan.

4.2 In the Credit Review, the Lending officer himself reviews the financial information with respect to salary and income, both for the applicant as well as co-applicants. He may contact any of the persons listed on the Application Form to verify information provided by the applicant. (The Application Form contains a statement to the effect that the applicant, on signing the form, gives NHDFC the right to contact any and all persons and institutions listed on the Form.) Contact may be made with his employer, banks, neighbors, etc. The Lending Officer also makes the necessary financial recalculations to ensure that the applicant still meets all the financial criteria. This information is contained in the Credit Review form, which the Lending Officer completes (Attachment E).

4.3 It is necessary to verify that the collateral to be provided by the applicant is clear with respect to ownership, other mortgages, etc. This will be done initially with the help of the Legal Advisor who will be responsible for training the legal assistant in this job in the case of uncomplicated collaterals. Additionally the approximate market value of this collateral after deducting a 60% margin should be verified to ensure that it is sufficient to covers the loan in question. If it is not, the applicant is notified and the application process stopped unless a rectification is made by the applicant within 10 working days. (This verification is carried out by filling the Title Review Form, Attachment F.)

4.4 Finally the Lending Officer must verify that the cost estimate provided by the applicant on his Application Form is accurate. The NHDFC expects to have established an internal cost estimating system which will not require the services of an appraiser to put a value on the improvements. (Unit Cost Estimate Review Form, Attachment G.) However until and unless this system is in place, it may be necessary to contract an Appraiser (or Quantity Surveyor)

to assess the value of the proposed improvements. The Lending Officer must determine that the cost estimate provided internally or by the Appraiser is equal to or exceeds the value of the improvements on the property as stated on the Application. If the appraised value is less, then the Lending Officer may reject the application, or alternately, negotiate a reduced loan amount with the applicant.

4.5 Forms required are:

- E. Credit Review Form.
- F. Title Review Form.
- G. Unit Cost Estimate Review Form.

CHAPTER 5

THE APPROVAL PROCESS

5.1 If there are no obvious problems with respect to the applicant's credit, property appraisal or property title, then the Lending Officer can recommend that in his opinion a loan can be made. He completes a loan recommendation proposal form (Attachment H) directed to the appropriate NHDFC approval body. This proposal form contains the name of the borrower, the amount of the loan and its terms and conditions. This is then attached to the loan file and a proposal containing the entire loan package is presented to the addressee.

5.2 Depending on the size of the loan, the letter will be addressed to one of three approval bodies, as follows:

-The General Manager of the NHDFC is vested with full authority to approve loans not exceeding Rs 100,000;

-A three person Credit Committee composed of one representative of NHDFC's Board of Directors, the General Manager and the Mortgage Loan Manager is vested with full authority to approve loans ranging from above Rs 100,000 to Rs 500,000;

-NHDFC's Board of Directors is vested with the authority to approve loans in excess of Rs 500,00.

5.3 Whenever a loan proposal is approved by the appropriate authority it should be realized that this approval is always contingent on the satisfactory fulfillment of the Mortgaging Process to follow this approval step. The applicant is immediately issued a contingent approval letter (Attachment I) requesting him to be prepared to have his collateral valued as well as have the mortgage registration transferred immediately thereafter.

5.4 If the approval body disapproves a loan, it must indicate in writing why the loan was disapproved. This letter will be entered into the loan application file, and the applicant so informed in writing.

5.5 Forms required are:

-H. Loan Recommendation Proposal Form

-I. Loan Approval Letter

CHAPTER 6

THE MORTGAGING PROCESS

This process consists of two basic activities, ie., a) valuation of the collateral(s) and b) the actual mortgage registration as a lien to secure the loan.

6.1 It must first be determined whether the properties to be pledged as collateral to NHDFC need be professionally valued. Such properties need not be professionally valued if they meet both of the following criterion:

-They will cover loans within the lending authority of the General Manager; and

-Properties whose market values are estimated by both the General Manager and the Lending Officer to be at least three times the amount of the loans.

On meeting both these conditions, a valuation waiver form (Attachment J) is signed by both the General Manager and the Lending Officer and placed in the applicant's credit file.

6.2 For all other loan(s), their respective collateral(s) have to be professionally valued and the final value figure (which must be mutually agreed by NHDFC and the Appraiser) must be twice the loan to qualify as a suitable collateral.

6.3 For purposes of valuation, NHDFC intends to sign exclusive contracts with a minimum of three appraisers initially chosen randomly from a list of 10 appraisers composed of two appraisers each working on behalf of Nepal Indosuez Bank, Nepal Grindlays Bank, Nepal Bank, Agriculture Development Bank and Nabil.

The Lending Officer assigns one of the above appraisers on a rotation basis to value collaterals not meeting the waiver terms. The appraiser will then value the collateral at the earliest mutually convenient time, but no later than 7 working days from the date of approval.

The applicant is notified again that the fees charged for the valuation are to be paid directly to the appraiser. The fees will be based on a sliding percentage basis, as follows:

Collateral Value--Fees based on Percentage		Amount
First Rs50,000	2.0%	Rs1,000
Next Rs50,000	1.5%	Rs 750
Next Rs50,000	1.0%	Rs 500
Over Rs 150,000	0.5%	To be calc.

Once the collateral is valued and found adequate to cover the loan, the mortgage is officially registered as indicated below.

6.4 After the contingency approval letter is given, the legal adviser is notified about the impending mortgage registration process whence he starts preparing all the necessary legal documents required for the deed. After this and at the earliest mutually convenient time, the legal assistant and the applicant go to the Land Revenue Office with the above documents for the registration deed. The applicant is responsible for all expenses incurred during this process.

6.5 Upon completion, 2 copies of all registration documents are made. One set is given to the applicant, the other put in his credit file, while the original set is sealed in a large envelope on which are written:

- the application number;
- the applicants name; and
- the loan number.

The last number is a new one to be made by the lending officer and will consist of one 3 digit and two 2 digit numbers separated by dashes to identify the applicant who is about to become a borrower. For example 033-01-92 would identify the 33rd borrower from branch #1 in the year 1992. After entering all these identifications into a roster of collaterals pledged to the bank. This sealed envelope is then locked in the vault after which the Lending Officer and the General Manager are notified that the applicant has fulfilled the terms of the approval letter.

6.6 Forms required are:

- J. Valuation Waiver Form

CHAPTER 7

THE CLOSING PROCESS

7.1 After the successful mortgaging of a collateral the Lending Officer jointly with the General Manager will send a loan agreement letter (Attachment K) to the applicant stating that his loan request is ready for disbursement on the mentioned terms and conditions. Once this letter is signed as accepted by the applicant and delivered personally to the Lending Officer or the General Manager, the applicant officially becomes a borrower and is given his credit number (same as the loan number) by the Lending Officer.

7.2 This letter also gives the date for closing or settling on the loan, and informs the Applicant that he will have to sign a promissory note (Attachment L) and/or other suitable guaranty documents prior to disbursement. Such documents might include a Letter of Setoff, Guaranty, Hypothecation or General Indemnity (See attachment M, N, O, and P respectively). Once the loan agreement letter and the promissory note are signed and the mortgage registered, the lending Officer is authorized to present the client with the loan proceeds less the mortgage fee and the closing takes place.

7.3 A commitment fee equal to 1% of the unutilized balance of the loan funds will be charged, unless the NHDFC is given a one month notice.

7.4 Depending on the size of the loan, the loan proceeds can be disbursed on a staggered basis to reflect the rate of utilization. Therefore additional disbursements may be required at later dates. In this case, the borrower will be presented with a loan disbursement schedule (Attachment Q).

7.5 If the loan disbursement is staggered, the borrower will be charged a simple interest rate of 15% on the outstanding balance of the loan until the loan is completely disbursed. This simple interest will be paid monthly on the outstanding balance. Once the loan is disbursed, the amortization period will begin.

7.6. Forms required are:

- K. Loan Agreement Letter
- L. Promissory Note
- M. Letter of Setoff
- N. Guaranty Form
- O. Hypothecation Document

-P. General Indemnity

-Q. Loan Disbursement Schedule

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CHAPTER 8

THE COLLECTION PROCESS

8.1 At closing, the borrower will be given written instructions on the loan repayment terms and conditions (the Loan Repayment Instructions, Attachment R). These instructions will include:

- The amount of the monthly payment and the due date;
- When to make the first payment, which is particularly relevant if the borrower has been granted a grace period on payment of the interest;
- The penalty to be paid if he makes a late payment as well as the consequences of non payment;
- Where he must make each loan repayment, including what information the borrower needs to present to make a payment.

The borrower will also be presented with a Loan Amortization Schedule (Attachment S) which will allow the borrower to keep a running record of his loan repayments and loan balance.

8.2 NHDFC will establish a loan repayment administration department in its offices where borrowers will make monthly loan repayments.

8.3 In the event this department is not operational by the time loan repayments are due to take place, then the lending division of NHDFC will be responsible for this function. The office assistant to the lending Officer will be trained to present with the Lending Officer at appropriate times a printout of all borrowers with his name, credit number, his loan amount, and his repayment status. He will be responsible for recording repayments.

8.4 In the event a borrower is delinquent in his repayment by more than a fortnight, he is visited by the lending officer and persuaded to make prompt repayments. If no positive results are forthcoming within a week, the Lending Officer issues him a warning letter requesting him to make repayments due to NHDFC within 15 days. This is done yet another time if the borrower still does not pay up. If the results are still not positive, appropriate legal actions are initiated to liquidate his collateral.

8.5 Forms required are:

- R. Loan Repayments Instructions
- S. Loan Amortization Schedule
- T. Loan Collection Letters

To: Jibgar Joshi, G.M., NHDFC
From: Dan Coleman, Consultant
Subject: Technical Assistance--Habitat
Date: April 21, 1992

I have had the opportunity to review George Joseph's Mission Report on Nepal, dated February, 1992. Below are my suggestions relating to his Report, including how you might make best use of any technical assistance from Habitat.

1. His report stresses the need for NHDFC to focus on resource mobilization, and he offers some 12 to 15 different schemes that NHDFC might want to consider to mobilize these needed resources. Some of these schemes we have discussed already, such as tapping the Provident Fund, others I have seen in action or read about, while the remainder are new to me. Nevertheless, he is 100% right that you need to generate additional resources for mortgage lending. If the Experimental Lending Program is a success--and I have no doubt it will be--then you are may have to struggle to come up with all the funds to meet the loan demand. If you do not, that is, if you start to turn away qualified borrowers just because you do not have available funds, then you are going to face a real credibility problem. My suggestion to you is that you should ask Mr. Joseph to help you on his next trip here to identify which of the many schemes he suggested would be most appropriate to consider first. Based on his worldwide experience, he could help you to reduce the number to a more manageable few, at least during, say, the first year.

2. Looking to Habitat to fund 2 Nepali advisors to function in an operating capacity will help you to surmount the salary ceiling constraint for hiring top flight banking professionals. However eventually, you will have to face up to this salary problem, and the sooner it is done, the better for the institution. But then I am not telling you here anything you do not already know. On the other hand, the amount of money required to hire 2 Nepalis should not exceed a total of \$10,000 annually for both, so it is not a big chunk of Habitat's proposed technical assistance program.

3. As you know, my feeling is that the immediate technical assistance need is for "nuts and bolts" type of advisory assistance. Given the paucity of Nepalis with strong experience in housing finance and mortgage lending, I believe you are going to have to go outside the country for this kind of hands-on experience. The important thing now is to get the NHDFC off the ground and running, and if you need help from outside the country you have got to be able to access it. Therefore I would suggest that the remaining funds in the Habitat pot should be used not only for training, as Mr. Joseph recommends, but also to fund these short-term advisors in home savings and lending. It is still hard to determine just what areas of training and technical assistance will be required, given that you have not yet selected your staff

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and therefore cannot know what gaps there are in their training and experience. But I can guaranty you that from the first day you open your doors you will begin to recognize the many areas in which you will need help.

4. As an adjunct to the above paragraphs, the local international banks here in Nepal (Indo-Suez, Grindleys, Nepal Arab) merely pick up the phone and call their regional or international office when they have a problem or need assistance. If the problem can not be solved with a phone call, then someone gets on a plane to Nepal. You do not have access to that kind of service, but you need it. But it is the kind of service that an institution like HDFC/India or some other institution in the region might be able to provide. Perhaps the new housing finance center being set up for Asia could help. I can not stress enough the importance of making an arrangement with an outside operating institution to fill your need for information and assistance. I would hope that HABITAT could help you in this area.

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To: Jibgar Joshi, G.M., NHDFC
From: Dan Coleman, Consultant
Subject: Experimental Lending Program
Date: April 22, 1992

I am pleased with the progress you have made in the past few weeks in designing and developing the Experimental Lending Program. As you know, the Lending Guidelines and Procedures, including the many forms and documents that complement this paper, are well advanced, and should be ready for the Lawyer's review. I also understand that you are making progress on the development of the internal unit cost estimating system that we discussed with Mr. Mathema. At the rate you are now going, I see no reason why you should not be able to initiate this key program within the next few months.

However, one thing does bother me. We both know how valuable Mr. Prahdan has been in the few days he has worked here. Without him, we would not have progressed as far as we have in the development of the Lending Guidelines. My understanding is that he will only be here through next week, and if he leaves, I do not believe you will have sufficient capability to begin any sort of banking operation. Mr. Pradhan has the kind of banking skills that you need on your staff, and if he does not remain with you or you find someone else with comparable skills, then, in my opinion, you will not be able to initiate the Experimental Lending Program.

I am going to repeat what I have said before: You cannot operate a bank without a banker, and certainly you cannot initiate and manage a lending program without someone with lending experience.

cc: Mr. Mathema