

**Nepal Rastra Bank**

Future Activities of Payment Systems in Nepal

Presenter

Nephil Matangi Maskay, Ph.D.
Director and Member,
NRB Payment & Settlement System Taskforce

For delivery at 15th SAARC Payment Council Meeting
2014 May 9, 11.45 – 13.00
Park Village Hotel, Budanilkantha, Nepal


1

**Nepal Rastra Bank**

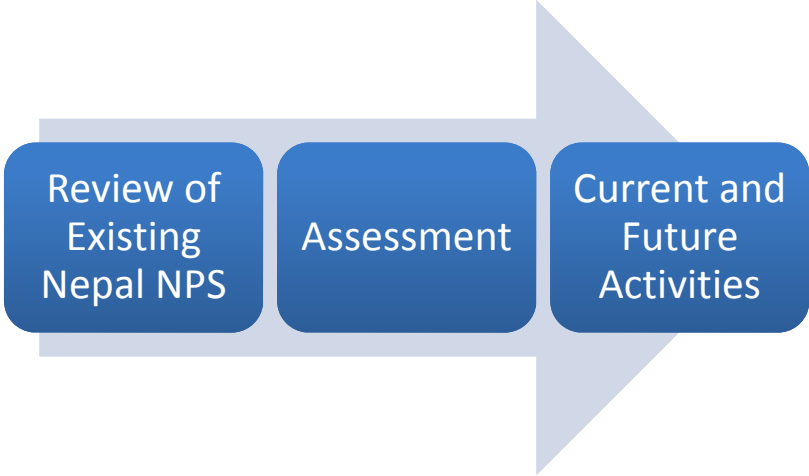
Background

- A National Payment System (NPS) covers all elements necessary for moving money safely, swiftly and efficiently between payers and payees – this consists of a defined group of institutions and a set of instruments and procedures, used to facilitate the circulation of money within the country and internationally.
- As per NRB Act, NRB is mandated “to develop a secure, healthy and efficient system of payment”
- NRB is aware that a NPS is essential for effective monetary policy, financial credibility and stability
- The presentation focuses on providing a review of current and future activities by NRB in this regard

2


 **Nepal Rastra Bank**

Outline



Review of Existing Nepal NPS Assessment Current and Future Activities

3

 **Nepal Rastra Bank**

Review of Existing Nepal National Payment System*

*This section based on Nepal Rastra Bank entitled “Review of Existing Nepal National Payments System” which has been considered by NRB’s Board of Directors and floated for public feedback

4



Domestic Market Structure

- Very Cash-fixated society
- About 50 % of households have bank accounts but confidence exist in commercial banks.
- Disincentives for opening bank accounts:
 - Lack of bank branches in the remote regions
 - Stringent Know Your Customer requirements
 - Uncomfortable feeling of the unbanked population when entering bank branches

5



Contd....

Legal Structure

- There is absence of a comprehensive legal structure in regard to payments.
- There is no coordinating body, such as National Payment Council, where discussion on payment related matters take place.
- There is no oversight body for payments.

Payment Infrastructure

- Settlement Mechanism to handle large value payments takes place semi-manually with absence of a LVPS such as a Real Time Gross Settlement System (RTGS).

6



Nepal Rastra Bank

Contd....

Retail Payment System

- Dominance of physical cash as payment instrument.
- Cheques are cleared electronically by Nepal Clearing House. However not all cheques are MICR-encoded
 - Digital Certificates are presently in process
 - Direct Credits & Debits are offered by almost all commercial banks but are mainly at intrabank basis.
 - Smart Choice Technology (SCT) is the largest supplier of card services; however it is not currently subject to supervision or oversight by NRB
- Internet Banking, Branchless Banking, Mobile Payments Exist
- International Remittances
 - Nepal is in the top 5 countries in world in terms of the flow of remittances as percent of GDP
 - Largely based on correspondence relationships

7



Nepal Rastra Bank

Contd....

Government Collection and Disbursement

- Payments such as Government Accounts Payable and Welfare Payments etc. – presently handled by NRB and a few CBs
- Revenue Receipts such as Tax (Inland Revenue Department), Customs and Non-Tax etc. – presently handled by NRB and a few CBs

Securities Settlement Systems

- Security and Exchange Board of Nepal is the regulator
- As present, most of the instruments traded at Nepal Stock Exchange are not dematerialized.
 - A commercial bank has been identified as settlement bank
- CDS & Clearing Limited – in process of introducing Central Security Depository, but presently regulation is yet to be fully developed
- Other institution, such as commodity market, is unregulated however clearing and settlement through commercial banks.

8



Contd....

Government Securities

- NRB is fiscal agent of the Government and the Bank issues Treasury bills and four types of long term bonds.
- The auction process follows issue calendar but process is entirely manual and securities are issued on paper certificates. (however scriptless is being exercised)
- Settlement are done through debiting settlement account at NRB or by cheque payment.
- Secondary Market – Dematerialization & Central Securities Depository (CSD) (not developed yet)
- Liquidity Management – Standing Liquidity Facility, Repos (carried out by exchange and endorsement of physical certificates), Interbank borrowing

9



Payment Systems in Nepal

Assessment*

*This section is also based on Nepal Rastra Bank entitled "Review of Existing Nepal National Payments System" which has been considered by NRB's Board of Directors and floated for public feedback

10



Drawbacks in the Present NPS

- Absence comprehensive laws and regulations on payment system as well as clear oversight responsibility/body
- Underdeveloped Financial Market Infrastructure.
- No direct relationship of the different stakeholders in Nepal NPS; fragmentation of domestic financial sector stakeholders
- Presence of systemic (i. e. settlement) risk in Nepal NPS
 - Bank to Bank payments are semi-manual
 - Net settlement obligations are cleared everyday however manually entered into settlement accounts.
 - High value cheques payments are entered manually (> NRs. 100 Million)

11



Contd....

NRB is aware of the situation and the potential risk to domestic financial stability.

Activities In Parallel

- Current Activities: Four documents have been produced by NRB in consultation with the International Finance Corporation;
 - That is, in addition to above the three documents are: Nepal Payment System Development Strategy (NPSDS), Nepal Rastra Bank Payment Oversight and Implementation of the Payments Oversight Function
- Future Activities: Exercise of NRB Payment and Settlement System Taskforce (PSST; international experience and implementation roadmap) which had proposed to establish and Payment and Settlement Unit.

12



Payment Systems in Nepal

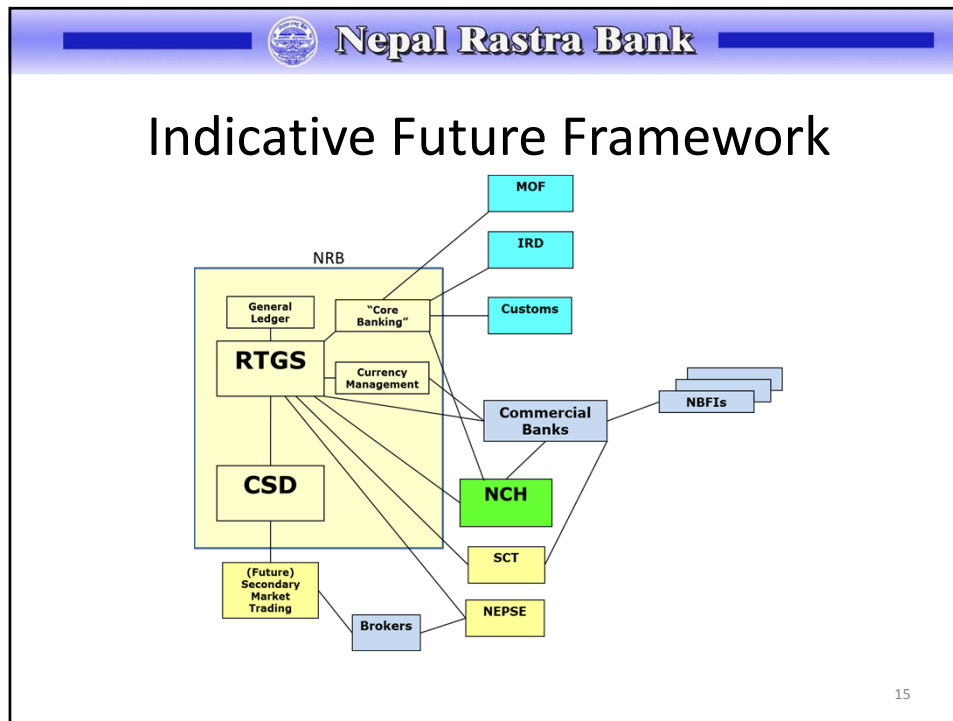
Current Activities


13



- Future activities of NRB are articulated in Nepal Payment System Development Strategy (NPSDS) for development of the NPS in Nepal. This document has recently been considered by NRB's Board of Directors and floated for public feedback
- Strategic Approach of NPSDS has the goal of "achieving a safe and efficient national payment system that effectively contributes to the country's financial stability and economic growth"

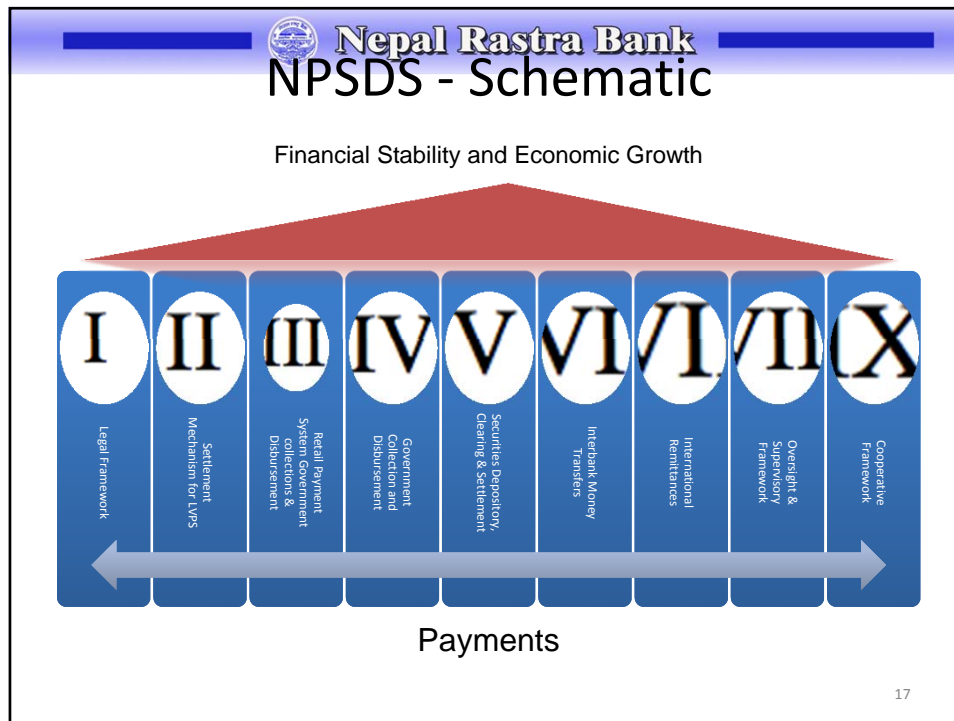
14



 **Nepal Rastra Bank**

- Executing NPSDS will require the implementation of a number of individual development projects
- These are shown schematically in next slide NPSDS numbering nine pillars as .

16



- Nepal Rastra Bank**
- **Pillar I: Legal Framework**
 - Laws and regulation of broad applicability
 - Such as insolvency and contractual relations
 - Laws and regulation that has specific applicability to the payment system
 - Such as legislation on electronic signature, validation of netting, settlement finality
 - Similar consideration apply to securities settlement system
 - Rules, standard and procedures
- 18



- **Pillar II: Settlement Mechanism for Large Value and Time Critical Payments**
 - Realization and procurement of Real Time Gross Settlement System (RTGS)
 - Development of intraday repo market (similar to Pillar VI)
 - Development of RTGS to be operated by NRB but integrated with relevant internal and external systems.

19



- **Pillar III: Retail Payment Systems**
 - NRB will continue to play a role as settlement agent, operator, participant and catalyst for change.
 - Automatic Clearing House (ACH) called Nepal Clearing House (NCH)
 - Clearing truncated cheque records in Kathmandu Valley
 - Interbank card-based payment services (ATM and EFTPOS) exist
 - Effective fraud-prevention and detection measures

20



Nepal Rastra Bank

- **Pillar IV: Government Collection and Disbursement**
 - Fully Automated interface between the Ministry of Finance which is facilitated by implementation of Treasury Single Account.
 - Work with Ministry of Federal and Local Government for distributing funds via electronic transfers
 - Work with Inland Revenue Department and Customs Department to make collection more efficient

21



Nepal Rastra Bank

- **Pillar V: Securities Depository, Clearing & Settlement**
 - Develop a Securities Settlement System (SSS)
 - Establish an automated Central Securities Depository (CSD) system
 - Instruments will be used to settle the cash leg of securities transactions

22



- **Pillar VI: Interbank Money Market**
 - Essential for liquidity management
 - Development of interbank repo market and strengthening lending operation
- **Pillar VII: International Remittances**
 - Stock taking exercise to ensure that international remittance in Nepal comply with CPSS-WB General Principles

23



- **Pillar VIII: Oversight**
 - Develop clear legislative authority for the oversight of payment and settlement system
 - Oversee all clearing and settlement arrangements
 - For carrying out this role effectively NRB is exercising for appropriate organization arrangements and staffing such forming a separate unit namely a division in NRB

24




- **Pillar IX: Cooperative Framework**
 - Establish a National Payment Council under chairmanship of NRB Governor with other regulator and stakeholder as members.
 - Cross-cutting nature of payments suggest an ecosystem which require effective coordination

25



- **Recent Developments**
 - Nepal Payment System Development Strategy, as well as other three documents, have been considered by NRB's Board of Director and floated for public feedback.
 - To assess and incorporate the feedback from the stakeholders; a High-level coordination committee under the coordinatorship of NRB Deputy Governor has been constituted.
 - To enhance participation of the aforementioned financial stakeholders, exercising for the setting up of the National Payment Council to be headed by Nepal Rastra Bank.

26


 **Nepal Rastra Bank**

Payment System in Nepal

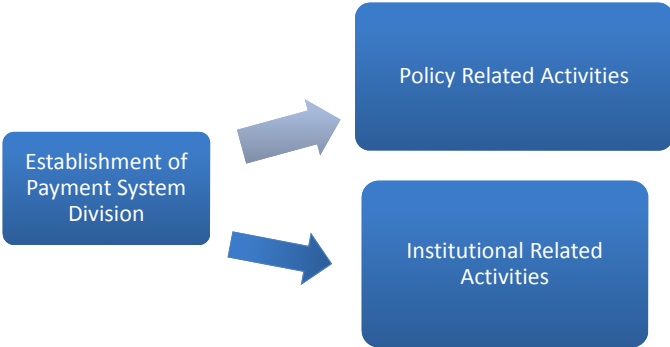
Future Activities*

*This section based on submitted draft PSST report

27


 **Nepal Rastra Bank**

Schematic of proposed activities



```
graph LR; A[Establishment of Payment System Division] --> B[Policy Related Activities]; A --> C[Institutional Related Activities];
```

28

 **Nepal Rastra Bank**

- Policy Related Activities
 - Formulation of necessary Acts
 - By-laws/Regulations
 - Policies and Procedures in this regard
- Institutional Related Activities
 - Initiate the process of procurement of RTGS
 - Establish Oversight Functions
 - Legal and regulatory framework for oversight
 - Strategic framework for oversight
 - Governance, Accountability and Transparency
 - Cooperative Arrangements

29

 **Nepal Rastra Bank**

- Formulation of NPC:
 - Proposed Chair: The NRB Governor
 - Proposed member are stakeholder in NPS such Government (MOF), Capital Markets, Financial Institutions, Nepal Telecomm Authority as well as related authorities and regulators etc.

30