

NEPAL

# THE LANDSCAPE FOR IMPACT INVESTING IN SOUTH ASIA

Understanding the current status,  
trends, opportunities, and challenges  
in **BANGLADESH, INDIA, MYANMAR,  
NEPAL, PAKISTAN, and SRI LANKA**



Dalberg

GIIN  
GLOBAL IMPACT INVESTING NETWORK

# LIST OF COMMON ACRONYMS

<b>ADB</b>   Asian Development Bank	<b>MDG</b>   Millennium Development Goal
<b>AIF</b>   Alternative Investment Funds	<b>MEB</b>   Myanmar Economic Bank
<b>BoP</b>   Base of the Pyramid	<b>MFI</b>   Microfinance Institution
<b>BRICS</b>   Brazil, Russia, India, China, South Africa	<b>MFTB</b>   Myanmar Foreign Trade Bank
<b>CA</b>   Chartered Accountancy	<b>MNC</b>   Multinational Corporation
<b>CIIE</b>   Centre for Innovation, Incubation and Entrepreneurship	<b>MICB</b>   Myanmar Investment and Commercial Bank
<b>CGTMSE</b>   Credit Guarantee Fund Trust for Micro & Small Enterprises (India)	<b>NABARD</b>   National Bank for Agriculture and Rural Development
<b>CSR</b>   Corporate Social Responsibility	<b>NASE</b>   National Association of Social Enterprises (India)
<b>DFI</b>   Development Finance Institution	<b>NEDA</b>   National Enterprise Development Authority (Sri Lanka)
<b>DFID</b>   Department for International Development	<b>OPIC</b>   Overseas Private Investment Corporation
<b>FIL</b>   Foreign Investment Law	<b>PE</b>   Private Equity
<b>FDI</b>   Foreign Direct Investment	<b>PM</b>   Prime Minister
<b>GAAR</b>   General Anti-Avoidance Rules (India)	<b>PPP</b>   Purchasing Power Parity
<b>GIZ</b>   Gesellschaft für Internationale Zusammenarbeit (German Agency for International Cooperation)	<b>RBI</b>   Reserve Bank of India
<b>HDI</b>   Human Development Index	<b>SEBI</b>   Securities and Exchange Board of India
<b>HNWI</b>   High Net-Worth Individual	<b>SIB</b>   Social Impact Bond
<b>HR</b>   Human Resources	<b>SIDBI</b>   Small Industries Development Bank of India
<b>ICT</b>   Information and Communication Technology	<b>SME</b>   Small or Medium Enterprise
<b>IFC</b>   International Finance Corporation	<b>SMED</b>   Small and Medium Enterprise Development (Sri Lanka)
<b>IFI</b>   International Financial Institution	<b>SVF</b>   Social Venture Fund
<b>IE</b>   Impact Enterprise	<b>VC</b>   Venture Capital
<b>IIC</b>   Impact Investors' Council (India)	<b>WHO</b>   World Health Organization
<b>IMF</b>   International Monetary Fund	
<b>LP</b>   Limited Partner	
<b>LTTE</b>   Liberation Tigers of Tamil Eelam	

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# ABOUT THIS REPORT

The objective of this study is to develop an understanding of the status of the impact investing markets in six countries in South Asia—Bangladesh, India, Myanmar, Nepal, Pakistan, and Sri Lanka. The full report includes an introduction and a chapter for each country. This research is intended to serve as a critical input to future investments and engagement to build and grow these markets. The key themes explored include the current status and trends in terms of the types of active investors, capital deployment, opportunities for and challenges to investing, the demand for impact capital, challenges to accessing capital and opportunities for enterprise growth, and the vibrancy and scale of the supportive ecosystem for the industry.

## Introduction

In recent years, impact investing has become prominent on the global stage as an approach to deploying capital with social/environmental goals as well as financial return objectives. Deployed in both developing and developed markets, impact investments are made across a range of sectors and asset classes.

South Asia is home to more than 1.6 billion people and has experienced dramatic economic growth over the last decade. However, this rapid growth, while changing some economies dramatically, has been uneven between and within countries; about a quarter of the region's population continues to live on less than USD 1.25 per day<sup>1</sup> and large population segments lack access to quality social services, finance, energy, and infrastructure as well as to affordable consumer products. The opportunity for impact through the deployment of capital into organizations and enterprises that increase incomes, create jobs, and provide access to essential services is significant, and the status of the impact investing industries in these countries is worthy of attention.

## Who is an impact investor?

Impact investments are “investments made in companies, organizations, and funds with the intention to generate social and environmental impact alongside a financial return.”<sup>2</sup>

The three key characteristics of an impact investor are as follows:

- Expectation of a financial return that can range from the return of capital to risk-adjusted market-rate returns and that can be derived from investments in a range of asset classes.

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<sup>1</sup> Weighted average calculated with the latest country data (2010–2012) from World Development Indicators, The World Bank; Myanmar figures are not included in the weighted average. Myanmar figures are not included in the weighted average as this indicator is not available for Myanmar.

<sup>2</sup> For more details, refer to the GIIN website, [www.thegiin.org](http://www.thegiin.org).

- Intent to generate a positive social and/or environmental impact through investments. For example, investors may seek to use investments to increase access to basic services or invest in solutions aimed at mitigating the negative effects of climate change.
- Commitment of the investor to measure the social/environmental performance of the underlying investments.

This report focuses significantly on the impact investing landscape in each of the six countries covered. Various terms may be used to refer to the impact investing landscape, including “impact capital” and “impact funds,” depending on the context. For the sake of fluency, the modifier “impact” will be dropped when the context is clear.

While the central goal of this study is to map the current landscape of the impact investing activity, there is also significant investment activity on the periphery of impact investing that is interesting to explore. In particular, we consider the following two types of investment activity:

- a. Investments in businesses serving BoP populations by investors who may not have explicit impact intention
- b. Investments where there is some intention to have social and/or environmental impact, but this impact is assumed to occur as a by-product and is not measured in any meaningful way

Such investment activity is also important for an analysis conducted to gain a better understanding of the broader opportunity landscape for impact investing going forward. When a section in the report focuses particularly on the investment activity in this peripheral region, we will explicitly refer to these as “impact-related” investments, thereby clearly differentiating them from “impact investing.” (Please note that we are using these labels purely for the ease of reference and do not intend the names to imply any subjective judgment on the nature of an investor’s investment activity or approach.)

## COUNTRY CONTEXT

### Overview

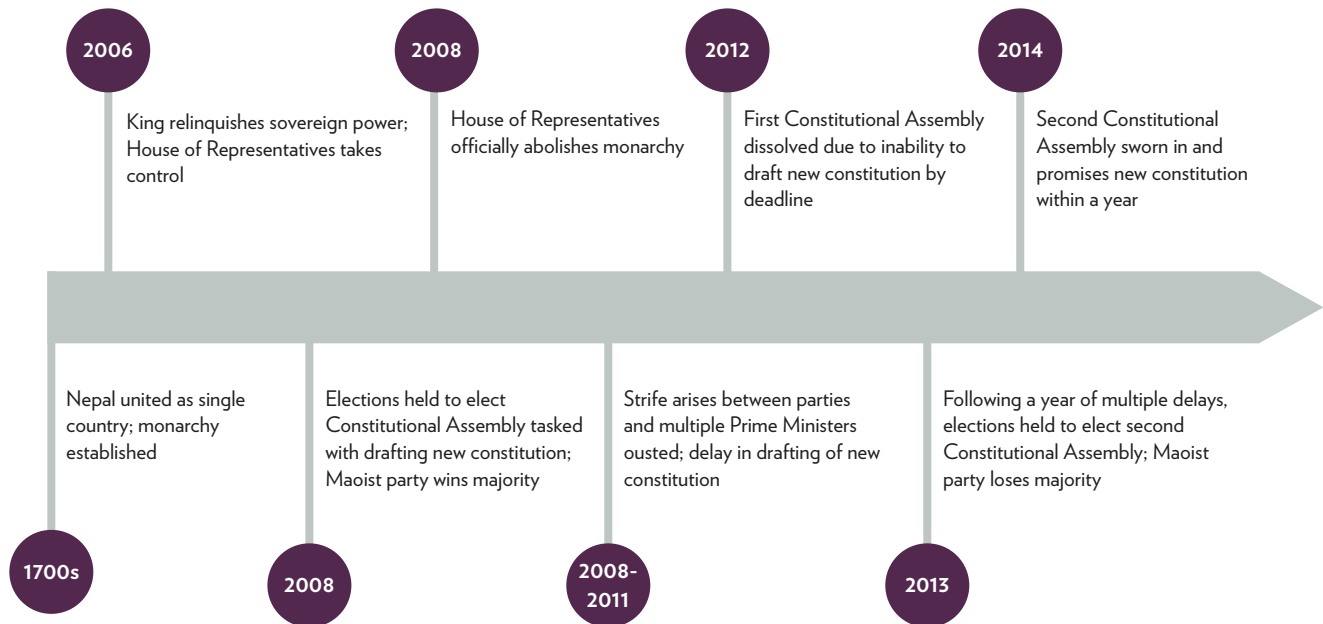
**Nepal’s small population, low GDP per capita, and political instability are deterrents to investments in the country, resulting in the country having the second smallest impact investing market by capital deployed among the countries under study (slightly larger than Myanmar).** Nepal, with a population of 27.5 million and a GDP per capita of about USD 690 (at the current USD exchange rate),<sup>3</sup> is passing through a momentous and a prolonged transition following a

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<sup>3</sup> *World Development Indicators, The World Bank, 2013.*

10-year-long violent conflict that ended in 2006. Since monarchy was abolished in 2008, there have been numerous attempts to draft a new constitution (Figure 1). Following a year of multiple delays, elections were held in 2013 to elect the second Constitutional Assembly. The Maoist party lost its majority, and the new government is now committed to delivering a new constitution by 2015.

FIGURE 1: TIMELINE OF KEY EVENTS IN NEPAL'S POLITICAL HISTORY



Source: BBC Nepal profile < <http://www.bbc.com/news/world-south-asia-12511455>>

The implications of this for investors are numerous:

- Nepal's political instability has brought about low investor confidence. Investors will only feel confident in a politically stable environment and a government that will hold for a reasonable length of time (e.g., five years). Further, Nepal's policy and regulatory environment is uncertain, highlighted by the lack of a constitution. However, there is a general belief among domestic investors that the recently sworn in Second Constitutional Assembly will have a new constitution within a year, as promised, leading to tempered optimism within the investment community.
- On the positive side, diminished Maoist power has created space for more private sector activity and a more supportive agenda for policy reform, again creating optimism among investors.
- This has also meant decreased labor volatility. In the early 2000s, labor strikes were paralyzing the country, but have since reduced in frequency and severity.

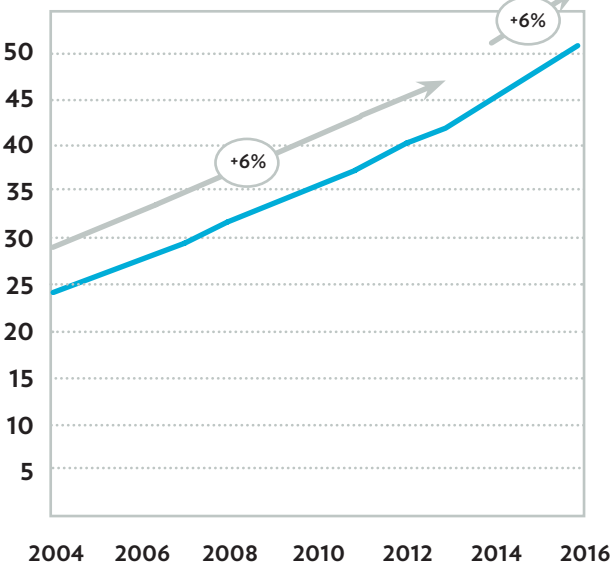
# GDP growth and drivers of FDI

Nepal has seen steady GDP growth at about 6% per annum since 2004 and is expected to continue this trend through 2016, but its GDP remains the lowest among the countries under study. Nepal's total GDP in 2013 was only 42 billion (PPP, international dollars),<sup>4</sup> as seen in Figure 2. At 6% per annum from 2014 to 2016, the forecast growth is also one of the lowest in the region.

FIGURE 2: GDP OF NEPAL (PPP, INTERNATIONAL DOLLAR, BILLIONS): CHANGE OVER TIME AND 2013 COMPARISON WITH THE REST OF THE REGION

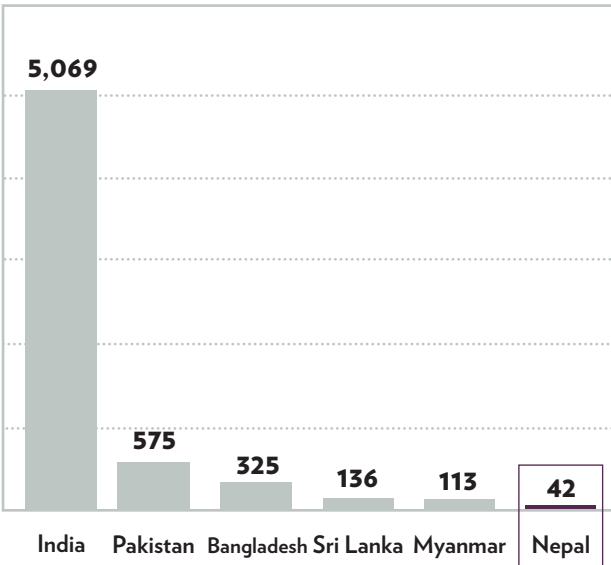
### GDP OF NEPAL

(PPP, CURRENT INTERNATIONAL DOLLAR, BILLIONS, 2013)



### GDP, BY COUNTRY

(PPP, CURRENT INTERNATIONAL DOLLAR, BILLIONS, 2013)

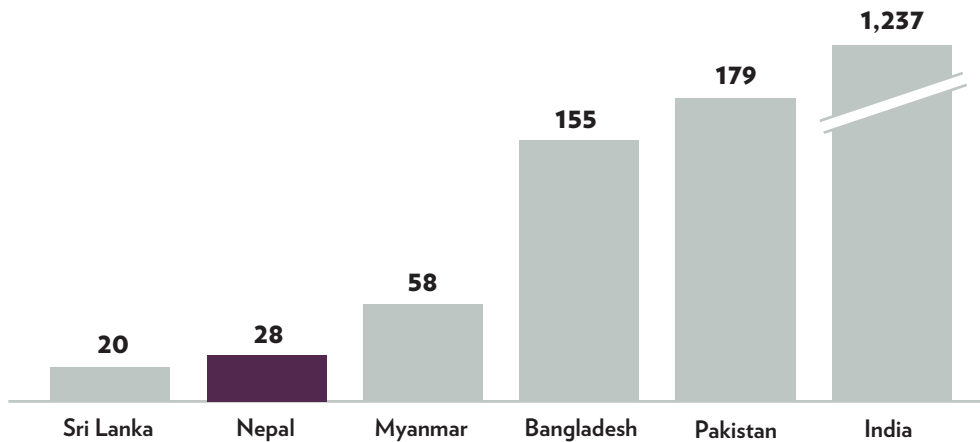


Source: International Monetary Fund (IMF) World Economic Outlook Data 2014. Notes: 1990-2013 actual, 2013 estimated, 2014-2016 forecasted figures as of June 30, 2014.

With the second smallest population in the region and the smallest GDP per capita among the countries under study, Nepal's consumer expenditure and market potential are not seen as very attractive for investors. At a population of 27.5 million<sup>5</sup> (Figure 3), Nepal is considered a small market by investors. The population size, coupled with a low GDP per capita, are seen as deterrents for investors, who express concern that low relative consumer expenditure and market potential do not warrant the high risk of investing in the country.

<sup>4</sup> IMF World Economic Outlook Database.  
<sup>5</sup> World Development Indicators, The World Bank.

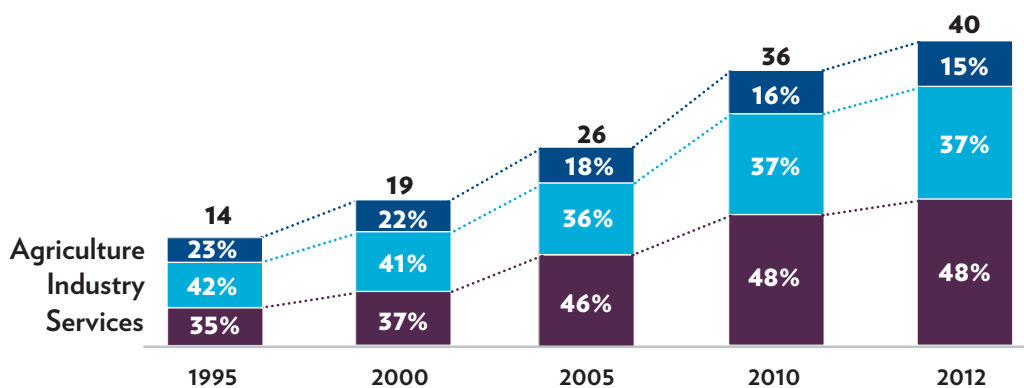
FIGURE 3: POPULATION OF NEPAL AND REGIONAL COMPARISON (MILLIONS)



Source: World Development Indicators, The World Bank

**Growth trends and investor interest are observed in some economic sub-sectors, particularly tourism and hospitality, and hydropower.** Within the services sector, tourism and hospitality is a fast-growing sub-sector, creating employment for about 20% of the economically active population and accounting for 3% of the GDP.<sup>6</sup> While holding the GDP share steady, the industry sector<sup>7</sup> is growing in absolute terms, contributing to 37% of the country’s GDP<sup>8</sup> due to the strong growth of hydropower and textiles, which continue to be attractive to investors. In fact, Nepal has one of the largest untapped hydropower resources in the world—an estimated 83,000 megawatts of hydropower potential.<sup>9</sup>

FIGURE 4: SECTOR SHARE OF GDP OVER TIME (PPP, INTERNATIONAL DOLLAR, BILLIONS)



Sources: World Development Indicators, The World Bank; IMF World Economic Outlook

6 Bishnu Prasad Gautam, *Tourism and economic growth in Nepal, 2011*.

7 Industry defined by ISIC Rev 3 as mining, manufacturing, construction, electricity, water, and gas.

8 World Development Indicators, The World Bank.

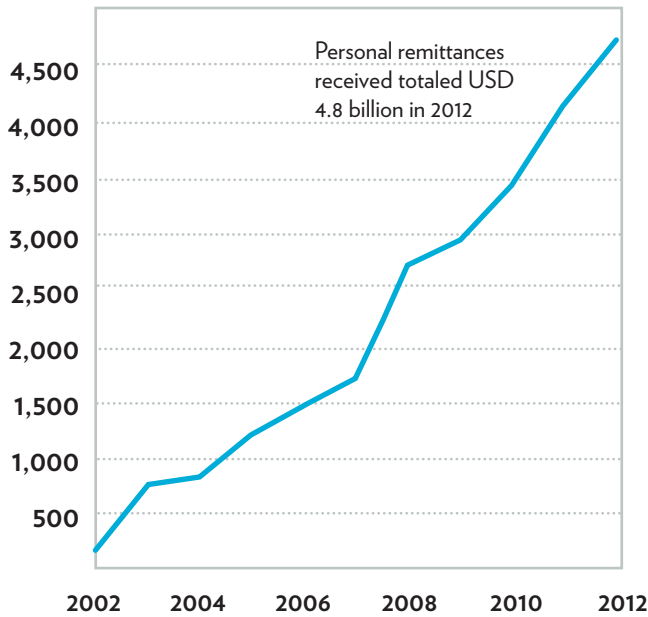
9 World Bank Nepal Overview.



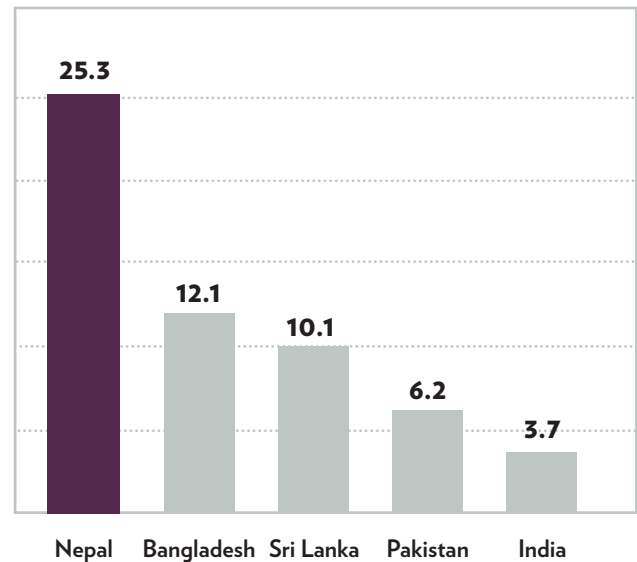
**A key driver of growth, primarily through increased consumption, is remittance income from Nepal's large migrant working population.** Personal remittances totaled USD 4.8 billion in 2012.<sup>10</sup> Remittances accounted for about 25% of the GDP, significantly higher than in any of the other countries under study. Remittances are driving increases in consumption as well as expenditure on private services such as education and healthcare. Remittance income also represents an important source of capital for asset purchase (land, houses, etc.), which in turn can serve as collateral for loans to provide seed funding to entrepreneurs.

**FIGURE 5: PERSONAL REMITTANCE INFLOWS: NEPAL OVER TIME (CURRENT USD MILLIONS) AND COMPARED WITH THE REST OF THE REGION (AS A PERCENTAGE OF GDP)**

**PERSONAL REMITTANCES SENT TO NEPAL**  
(MILLIONS, CURRENT USD)



**PERSONAL REMITTANCES SENT BY COUNTRY**  
(% OF GDP, 2012)



Source: World Development Indicators, The World Bank

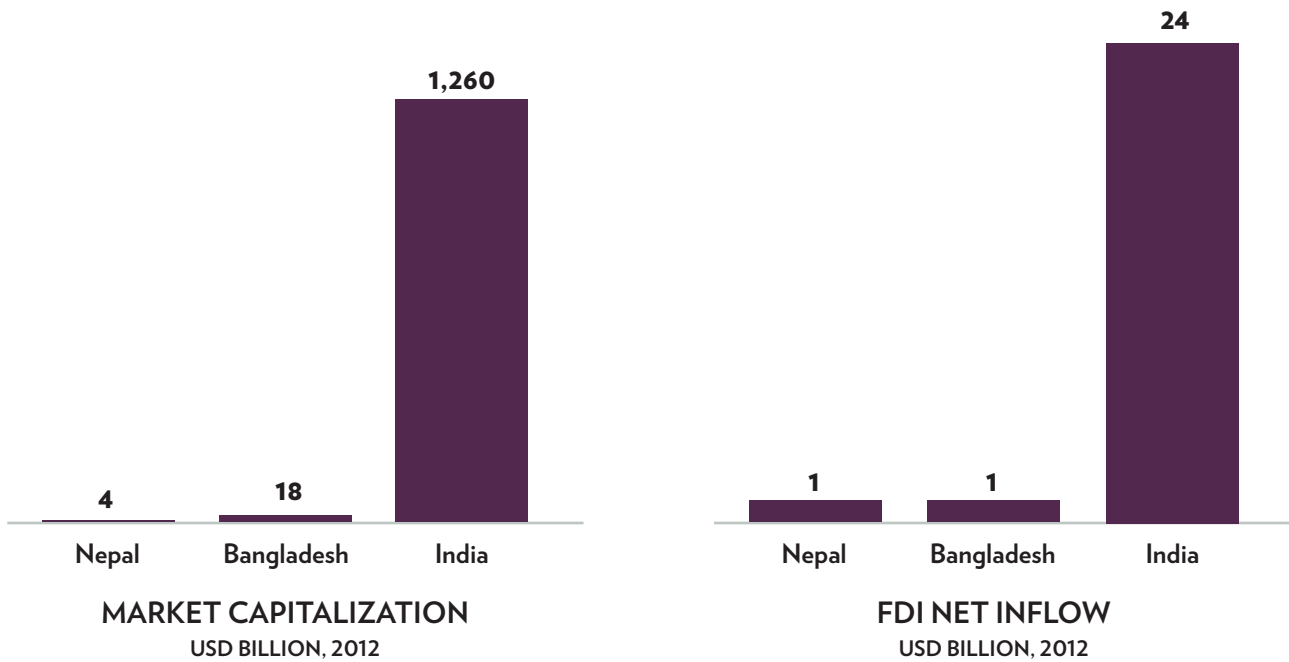
**Despite these positive markers and trends, overall investor confidence has been low, reflected in low capital market investments and FDI inflows.** In 2012, FDI net inflows reached about USD 1 billion, or about 4.9% of the GDP.<sup>11</sup> In the same year, market capitalization totaled USD 4.1 billion.<sup>12</sup> Investors considering opportunities in the region would prefer to invest in larger, more dynamic markets such as India and Bangladesh.

<sup>10</sup> World Development Indicators, The World Bank.

<sup>11</sup> World Development Indicators, The World Bank.

<sup>12</sup> World Development Indicators, The World Bank.

FIGURE 6: MARKET CAPITALIZATION AND FDI IN NEPAL COMPARED TO ITS REGIONAL NEIGHBORS



Source: World Development Indicators, The World Bank; IMF Balance of Payments database

**Domestic investors are also not heavily engaged, in large part due to the population’s low levels of access to financial services as well as a poor understanding of and a relative lack of trust in these services.** Given the extremely low levels of access to financial services in Nepal in the mid-2000s, the government and the central bank undertook extensive efforts to increase access to banking services across the country. The banked population grew considerably to approximately 40% in 2013 from 26% in 2006; however, while savings/deposits have increased, lending and investment in general remain low, reflecting low levels of familiarity with, and trust in, other asset classes. For example, the domestic capital market remains small and fairly illiquid—many listed companies are banks or financial institutions, which, by government mandate, must offer 30% of their equity to the public.<sup>13</sup>

## Key constraints and opportunities in Nepal

**Nepal’s weak basic infrastructure is a major challenge, making it costly to run businesses and difficult to access markets or build supply chains.** Despite a relatively high electrification rate (76% of Nepalis have access to electricity<sup>14</sup>), supply

<sup>13</sup> Nepal Stock Exchange.

<sup>14</sup> International Energy Agency, Key world energy statistics, 2013.

is unreliable and hours of access are few; therefore, the population is heavily under-electrified (as reflected by the low per capita energy consumption), and back-up power supplies for businesses and industry are extremely expensive. Road networks are few, leaving much of the country inaccessible and economic activity very heavily concentrated in the Kathmandu Valley.

**While these business constraints mean lower attractiveness of Nepal for investors seeking purely financial returns, investors with impact objectives have an opportunity to address significant social needs by investing to promote basic services, infrastructure, and economic opportunities.** Nepal is among the poorest countries in the world and currently ranks 157 out of 187 countries on the Human Development Index.<sup>15</sup> Although reduced from 53.1% in 2003, 24.8% of the population still lives below the World Bank USD 1.25 per day poverty line (PPP) as of 2010.<sup>16</sup> Gaps in basic services—such as healthcare and education—and poor infrastructure contribute to this poverty. For impact investors, these gaps present an opportunity to achieve their social mandate, albeit in a difficult market.

## INVESTING IN NEPAL: THE SUPPLY SIDE

**Overall, impact investing in Nepal is fairly limited, reflecting a small investment landscape at-large.** Approximately USD 17.3 million has been deployed by impact investors in Nepal to date. Investors see the small population of Nepal, low GDP growth (relative to other countries in the region), limited infrastructure, and political uncertainty as deterrents to investing in the country. As a result, in Nepal, the risk capital market is largely driven by impact investors (unlike in other markets where there is an existing set of commercial private equity (PE)/venture capital (VC) investors). For commercial players, the viability or potential of the market is unproven and unclear. Therefore, while there are few active players, those that are present are explicitly impact driven (however, even these players are still largely testing the market).

### The broad impact capital market in Nepal

**There are eight impact investors active in Nepal (Ring 1),<sup>17</sup> although half of these are in an indeterminate state.** Of these eight investors, there are five local funds, two development finance institutions (DFIs), and one regional fund, as shown in

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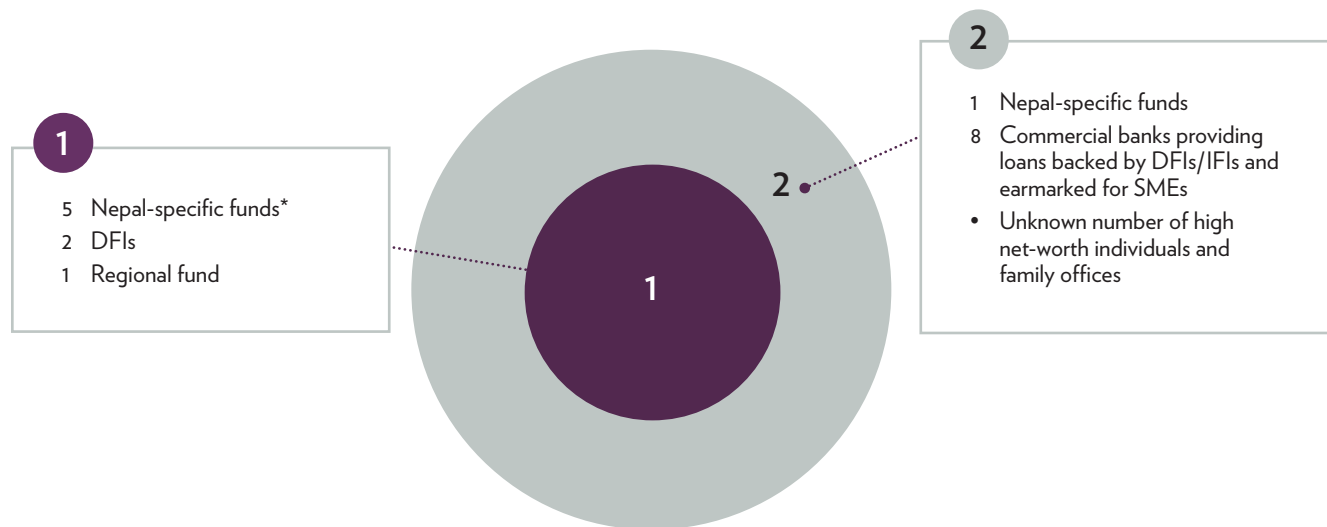
<sup>15</sup> UNDP, Human development reports, 2013.

<sup>16</sup> World Development Indicators, The World Bank.

<sup>17</sup> In this report, we use a simple framework to categorize investors. The inner ring—Ring 1—represents impact investing activity, and the outer ring—Ring 2—represents activity related to impact investing but which may lack either explicit impact intention or a commitment to measurement.

Figure 7. Four funds that have raised capital have either not yet deployed, or have been put on hold, or have closed due to management issues or the difficult market. These challenges will be discussed further in the section “*Challenges facing impact investors in Nepal.*”

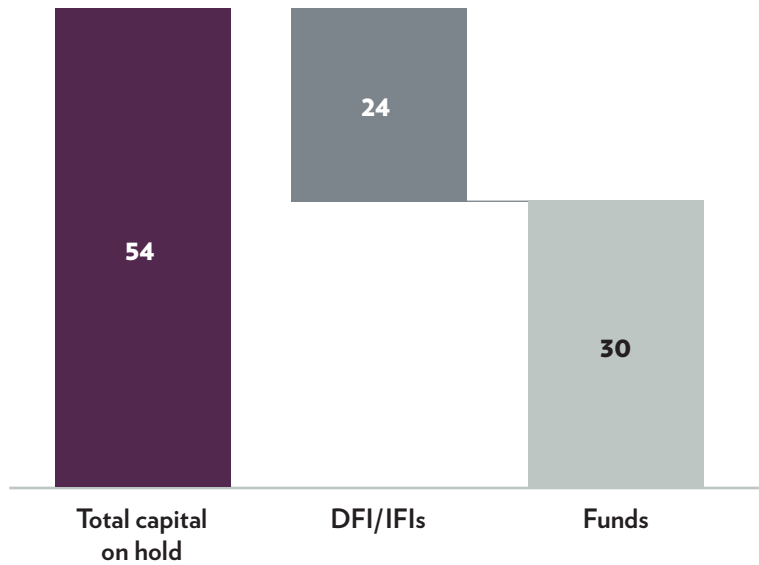
FIGURE 7: NUMBER OF DIRECT IMPACT AND IMPACT-RELATED INVESTORS ACTIVE IN NEPAL



Source: Stakeholder interviews; Investor websites; Dalberg analysis. \*Notes: Two of these funds have raised capital but have not yet been deployed; another two funds have been put on hold according to the other players in the market.

**Impact investors currently have USD 17.3 million of active investments. An additional USD 54 million is expected to be deployed soon.** This capital has been raised but put on hold in part due to internal management constraints, difficulty in closing funds, and other challenges as will be discussed later in this chapter. Of this capital, USD 30 million has been raised by two large funds and is waiting to be deployed, and the remaining USD 24 million has been committed by DFIs as direct investments into enterprises (Figure 8). While this additional capital commitment signals a growing interest in the market, it also reflects the difficulties that investors have had in securing investments.

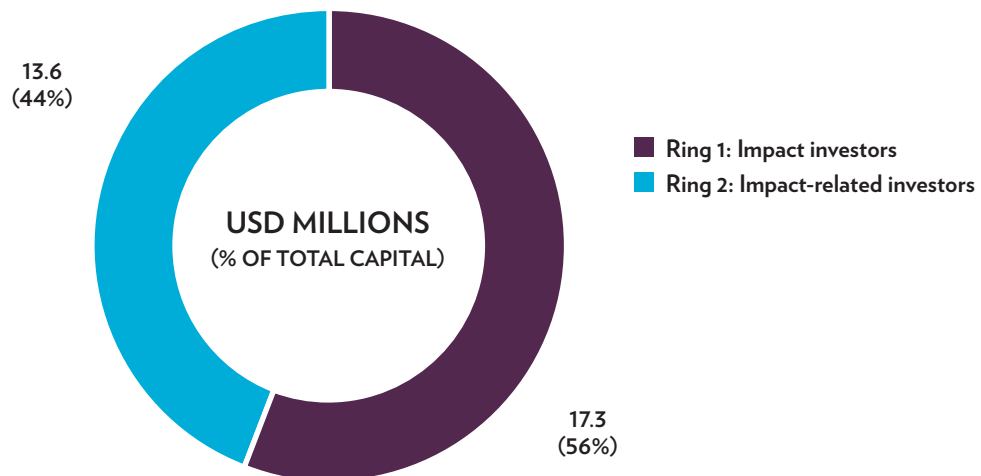
**FIGURE 8: TOTAL CAPITAL RAISED OR COMMITTED BY IMPACT INVESTORS IN NEPAL, BUT NOT YET DEPLOYED (USD MILLIONS)**



Source: Stakeholder interviews; Investor websites; Dalberg analysis

**Outside of impact investors, there are nine periphery impact-related investors active in Nepal with about USD 13.6 million in current investments.** These investors include one Nepal-specific fund making small investments ranging from USD 2,000 to USD 8,000. Eight commercial banks are also making SME loans backed by DFI funding. As shown in Figure 9, these impact-related investors have made 44% of the total investments by amount.

**FIGURE 9: TOTAL CAPITAL DEPLOYED BY RING**



Source: Stakeholder interviews; Investor websites; Dalberg analysis

## Active impact and impact-related investors in Nepal

**There is a range of different types of investors active in Nepal, but only a limited number of each type.** While we see funds, DFIs, diversified financial institutions/banks, and family offices/high net-worth individuals (HNWIs) present as in other markets, most are still testing the market with a minimal number of investments. There have been some recent efforts by local fund managers to raise new funds, but these are largely not yet active or deploying capital.

**While at present, foreign fund managers express a low appetite for investments in Nepal, domestic funds are slowly emerging, and although most of these funds are facing difficulties in closing and deploying capital, they are shaping the market.** Only one foreign fund has entered the country with a small investment. All other funds are domestic. Two of these domestic funds (both small with less than USD 1 million in capital to deploy) have made a series of small deals as they test the market. Given the dearth of commercial private equity investors and venture capitalists, these funds are playing a vital role as the first movers to demonstrate market viability and as policy advocates with the government. The largest fund to date (with a portfolio of USD 20 million) has recently closed and is expected to begin deploying capital soon. This will signal a significant step for the market as the amount of capital deployed by funds will then rival the direct investments by DFIs (as compared to other markets where DFI investments dwarf investments made by fund managers).

**DFIs are the most active players in the market by capital deployed, but these too have only entered the market recently and are still very much testing the waters.** In contrast to other countries where DFIs are trying to play a more catalytic role and to move the market, in Nepal, DFIs are still quite wary. As direct investors, DFIs are only making deals less than USD 10 million. Even though DFI activity is less than in Nepal's regional counterparts—in terms of both the number of deals and the size of these deals—DFIs are still a large segment of the impact investing market, accounting for 93% of the total deployed impact investing capital (56% if we include the committed capital yet to be deployed).

**Recognizing their potential role as market catalysts, DFIs are using guarantees as an investment instrument in Nepal as well as their direct lending to commercial banks.** As in other countries, DFIs are backing SME portfolios for commercial banks to increase lending to these enterprises. The guarantees have been to five banks to promote SME lending in the range of USD 40,000 to USD 8 million each (totaling USD 12.3 million) and three loans to banks in the range of USD 260,000 to USD 800,000 (totaling USD 1.4 million). These investments reflect the DFI interest in testing the market without excessive exposure, as well as their interest in increasing SME access to finance in the country.

**DFIs are also acting as limited partners (LPs) for two funds, both of which have yet to launch.** Three DFIs have backed two domestic funds—one for USD 20 million and the other for USD 10 million. Neither fund has yet deployed capital, but one is expected to close its first deal soon. Additionally, at least one bilateral donor and one DFI have assessed the possibility of anchoring sizable equity funds for Nepal, but the limited track record of the existing funds and the low level of experience of these

funds have been the deterrent factors.

**DFIs and donor agencies play an active role in promoting and advocating pro-investment policy changes on behalf of the investment community.** DFIs and donors, in collaboration with fund managers, have been working closely with regulators to address gaps and constraints in regulatory frameworks. Regulators perceive DFIs and donor agencies as knowledgeable and credible sources, and have addressed some concerns raised by these parties, including a recent change to blacklisting laws from which foreigners are now exempt (regulations will be discussed further in the section titled “Challenges facing impact investors in Nepal”).

**Diversified financial institutions and banks have been fairly inactive as impact investors.** SME lending from commercial banks is limited as the 117 domestic banks and 90 non-bank financial institutions (NBFIs) have been reported to shy away from small deals and prefer to finance the less-risky, well-collateralized, and diversified business houses. Further, there has been some effort to promote increased lending to SMEs by financial institutions through government mandates and DFI guarantees, but given the large unbanked population in Nepal, it is still difficult to reach SME owners with formal financial services. Only a small amount of capital—largely debt provided or guaranteed by DFIs but on-lent through the commercial banks—is being channeled through institutional investors.

**Domestic family offices and HNWI are operating largely informally—without formal fund structures or stringent timelines.** HNWIs, as well as the families of the leading business houses, are often considered to be the sources of seed capital. This happens informally and through networks that are not easy to access. There is one group of young investors that is starting to engage more formally as angel investors, but this has not been institutionalized. As in other countries, friends and family members also serve as a source of capital, particularly through remittance income. International HNWIs are also slowly engaging in Nepal, particularly through one asset management firm that matches these investors with enterprises. The asset manager works to identify potential investees, determines capital needs (as well as business development support needs), and approaches an existing network of investors outside Nepal to secure the needed capital.

FIGURE 10: TYPES OF IMPACT INVESTORS AND IMPACT-RELATED INVESTORS ACTIVE IN NEPAL

TYPE OF INVESTOR	ESTIMATED NUMBER	DETAILS OF INVESTORS IN NEPAL
Funds and fund managers	7 (6 impact investors)	Small local funds are slowly emerging and have been critical in shaping the market, given the limited number of impact and commercial investors in the country, but many have been put on hold, shut, or delayed due to difficulties in raising capital and management issues.
DFIs	2 (2 additional ones are anchoring funds)	DFIs are making direct investments, anchoring two funds, providing guarantees and loans to banks to promote SME lending, and advocating regulatory changes on behalf of the investment community.
HNWIs/Family offices	Likely many informal ones	Friends and family are a significant source of seed capital, and HNWIs are starting to engage informally.
Diversified financial institutions/banks	8 providing loans with DFI backing	The large unbanked population implies that many SME owners cannot be reached through formal financial institutions; therefore, bank lending is limited, but eight banks are providing SME loans with funding from DFIs.

## Key trends in impact investing in Nepal

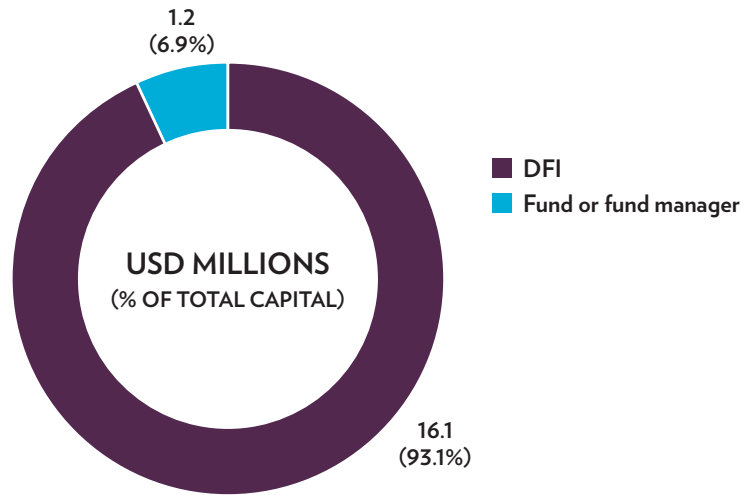
The following section examines the trends among impact investors. The figures quoted in this section refer only to this set of investors, who have collectively deployed about USD 17.3 million to date. The activities of impact-related investors will be discussed in the section “Beyond the impact investing market.” Despite the small amount of capital deployed in Nepal, we see trends emerging around features such as instrument, growth stage, sector, deal size, and return expectations.

### INVESTOR MIX

As discussed, two DFIs are responsible for 93% of impact capital currently deployed, or USD 16 million. The remaining USD 1.2 million has been deployed by two small funds.



FIGURE 11: IMPACT CAPITAL DEPLOYED BY INVESTOR TYPE



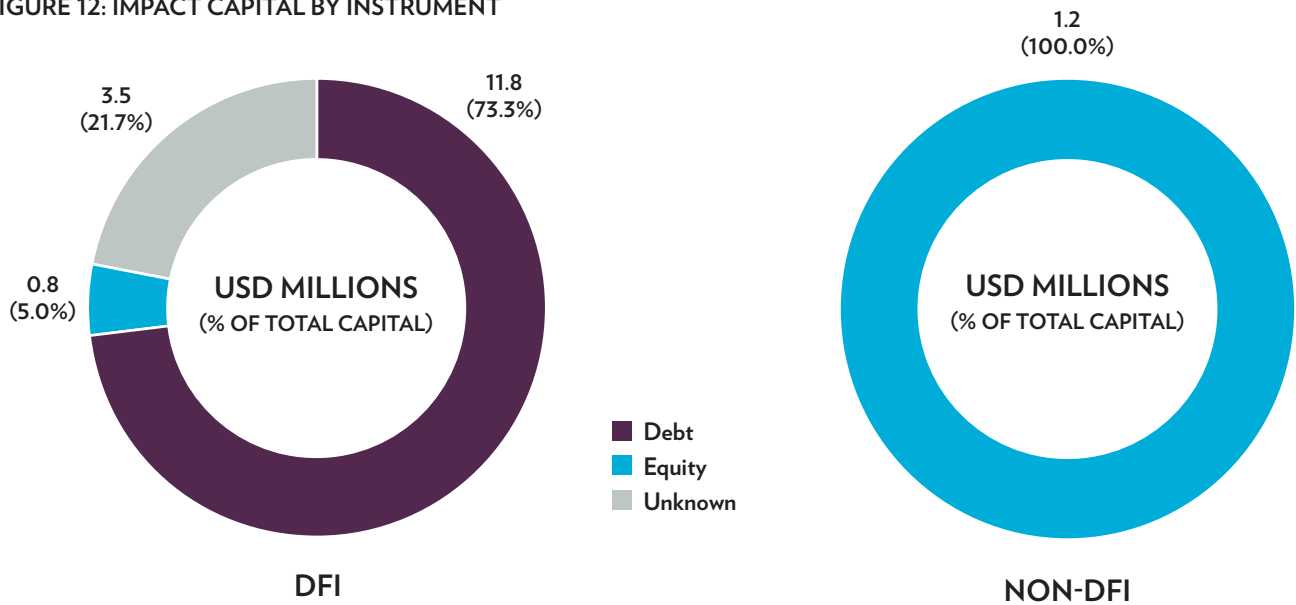
Sources: Stakeholder interviews; Investor websites; Dalberg analysis

## INSTRUMENT

**Debt is the preferred instrument for most of the overall impact capital in Nepal.**

DFIs are responsible for these trends as they are testing market viability through these relatively low-risk instruments. DFI debt investments account for at least 73% of capital deployed by impact investors, whereas equity is about 5% (Figure 12).

FIGURE 12: IMPACT CAPITAL BY INSTRUMENT



Sources: Stakeholder interviews; Investor websites; Dalberg analysis

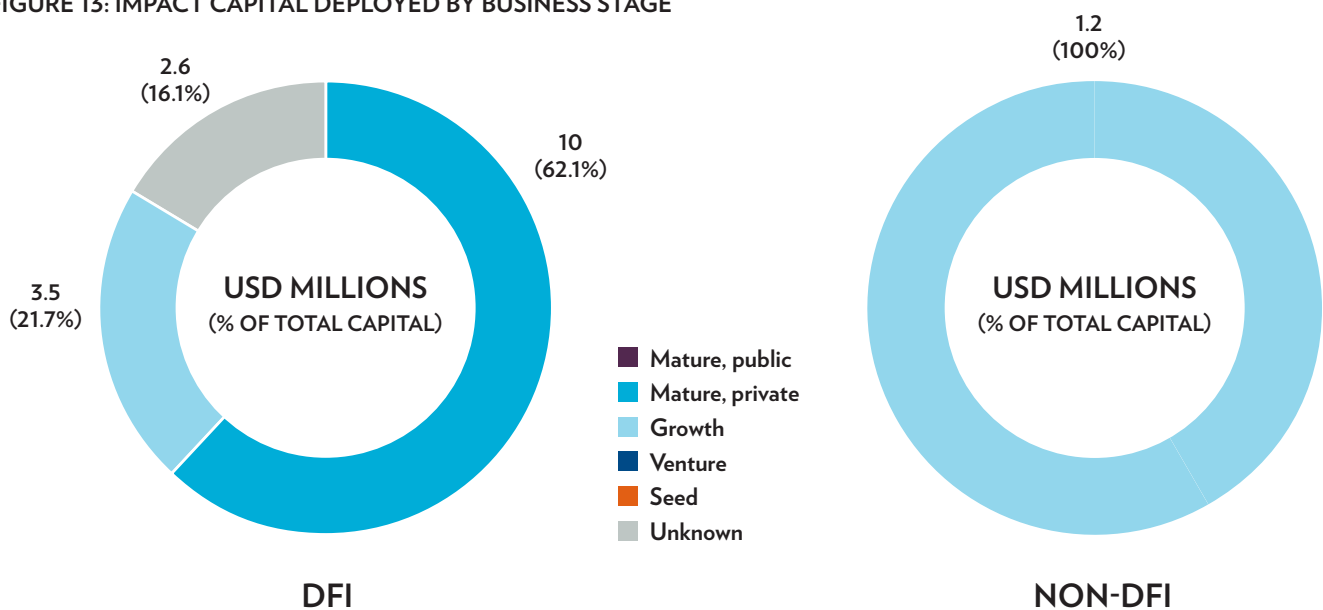
**Regulatory uncertainty around equity makes debt preferable.** Even among investors that have not yet deployed capital, debt is identified as the most feasible and least risky instrument. As a new instrument, the regulatory rules and processes around equity have not yet been fully defined in Nepal. Equity deals must get the approval of the country’s central bank, but the process for approval is long and not well-defined, leaving investors uncertain about what to expect. In addition, domestic investors can be blacklisted from financial markets or services if they provide equity to a company that fails (foreign investors have recently been exempted from these regulations).

**However, equity is being tested in small amounts, particularly by investors that are not legally allowed to provide debt.** While regulations around equity are stifling for investors, debt is outright prohibited for certain investors. In particular, in order to provide debt, an investor must be registered as a bank in its country of origin. For small funds, this is unfeasible, so they are testing the market through equity investments.

### GROWTH STAGE AND DEAL SIZE

**Most of the currently deployed impact capital has been invested in mature companies; this is strongly driven by one large investment by a DFI.** As is the case in the other countries considered in this study, DFIs prefer to make investments larger than USD 1 million, but only a small number of companies can absorb capital of this amount in Nepal—and these are primarily mature. As such, given the small amount of capital deployed and only around six deals made, the DFI investments drive an observed preference for mature companies.

FIGURE 13: IMPACT CAPITAL DEPLOYED BY BUSINESS STAGE



Sources: Stakeholder interviews; Investor websites; Dalberg analysis

**All known investments from non-DFI investors are in growth stage companies, as the capital requirements for these companies match the small ticket size of funds that are currently active.** For these non-DFI investors, ticket size limitations of less than USD 1 million are driving their preference for growth-stage companies. These investments have been less than USD 200,000 in size.

**Seed capital represents a funding gap among formal impact investment channels but is addressed by informal networks such as friends and family.** No seed capital has been provided by formal impact investors, and it is difficult for entrepreneurs to secure seed funding from commercial banks, due to high collateral requirements and general reluctance on the part of banks to fund early-stage ventures. As a result, entrepreneurs access seed capital through informal channels such as self-financing, friends, and family. Nepal's significant remittance inflows are likely driving much of this informal lending by friends and family.

**All four of the known non-DFI deals in Nepal are less than USD 1 million in value; the two known DFI investments are significantly larger.** As a result of two larger deals made by DFIs, the larger of which is USD 10 million, the overall average deal size across all known deals is approximately USD 2.4 million. Specific portfolio information was not available for one DFI; hence, the number of deals made is unknown.

**We see small deal sizes as investors are wary of the market, small investors are looking to diversify their portfolios, and only a limited number of companies are capable of absorbing large capital infusions.** As discussed previously, a limited number of investment-ready companies can absorb large amounts of capital (more than USD 1 million). DFIs, while able to deploy larger ticket sizes, are still new to the market. Smaller funds are looking to diversify their portfolios to minimize risks and are therefore, deploying smaller ticket sizes to allow for a greater number of deals. These funds have only made deals under USD 1 million.

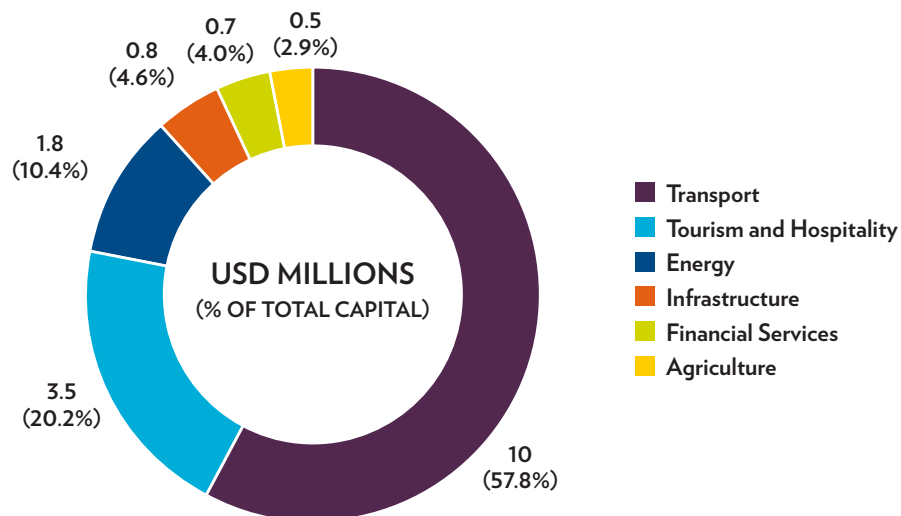
**Deal size trends are likely to shift as two large funds begin to deploy capital.**

While small ticket sizes have been the norm to date, two large funds are entering the impact investing market with expectations of deploying ticket sizes greater than USD 1 million, and focusing on renewable energy, tourism, education, information and communication technology (ICT), healthcare, and agriculture.

## SECTOR

**Transport and tourism and hospitality are two sectors that are currently receiving the largest portion of capital, but these preferences simply reflect two DFI investments.** Collectively, these sectors have absorbed 78% of capital.

FIGURE 14: IMPACT INVESTMENTS BY SECTOR (BOTH DFI AND NON-DFI INVESTORS)



Sources: Stakeholder interviews; Investor websites; Dalberg analysis

**In general, sector selection has been fairly opportunistic rather than strategic, as investors are focused on finding investable companies irrespective of sector.**

Faced with a dearth of investment-ready enterprises, investors are reluctant to restrict their portfolio to certain sectors. This has led to more capital flowing to sectors with investable companies. To date, these sectors are tourism and hospitality (there has been an investment in a hotel and interest in a restaurant, driven by the large number of foreign tourists visiting the country) and transport (there have been two investments in an airline).

**Additionally, sector selection is often tied to ticket size.** Investors who need to deploy large amounts of capital in individual transactions typically look for deals in sectors where enterprises can absorb large investments, including energy (particularly hydropower), and tourism and hospitality. While deal flow has been fairly limited, investors looking to make larger investments are expressing interest in these sectors (as discussed below). Agriculture in Nepal, in contrast, is still highly subsistence-based with little commercialization. Most investable opportunities in this sector are small in size and thus, do not appeal to DFIs or larger funds moving into the market. Instead, we see small funds investing in agriculture opportunities, with ticket sizes of USD 200,000 or less.

**Although investments to date have been opportunistic with respect to sector, for the future investors are particularly excited about the potential of investing in hydropower, and tourism and hospitality.** Historically, both these sectors have been high-growth sectors, and these trends are expected to continue. In addition, there have been a number of large hydropower projects that have brought on foreign investors, and IPO exits are more feasible, making it possible to list during construction to raise more capital. However, investors are growing wary of the hydropower sector, as regulations may tighten due to Indian investors looking to enter

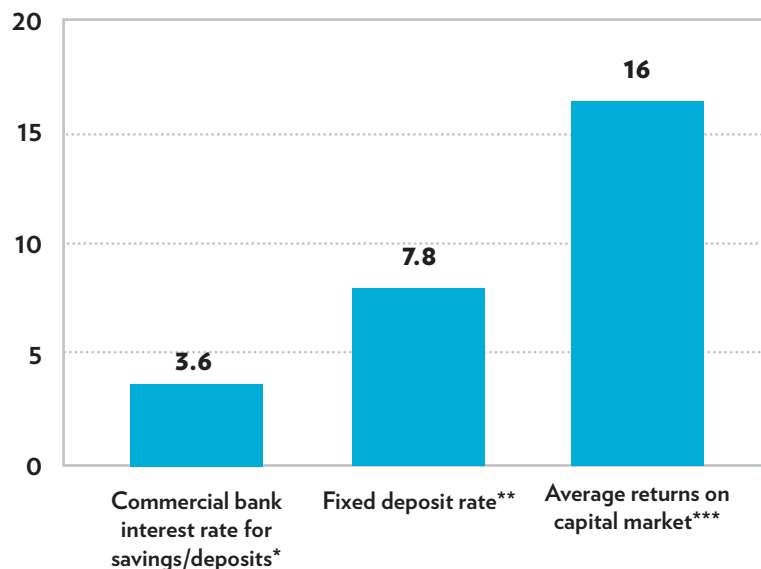
the market. Tourism and hospitality has also historically been a strong sector, and many investors are looking to invest in large hotel chains to capitalize on the growing number of foreign tourists visiting the country.

**Outside of hydropower and tourism, sectors such as healthcare and education are growing in appeal due to remittance-funded spending for private services in these sectors.** As remittance inflows continue to grow, provision of basic services is moving increasingly toward the private sector. Many families benefitting from remittance income are sending their children to affordable private schools and using private healthcare facilities, rather than the free public alternatives. Recognizing this trend, investors are increasingly interested in the for-profit entities coming into the market to address gaps in basic services.

## Return expectations and exit possibilities

**Return expectations range from 17% to 35% for equity investors, but with little market activity to date, these expectations are untested.** Equity investors benchmark expectations against a high cost of capital (12%–13%) and the less-risky return expectations of the capital markets (16%–18%). Given the lack of exit activity among impact investors, return expectations are being calculated against returns on other asset classes (Figure 15).

FIGURE 15: APPROXIMATE RETURNS OF OTHER ASSET CLASSES (% ANNUAL)



Source: World Development Indicators, The World Bank; Nepal Rastra Bank; Stakeholder Interviews. Notes: \*Interest rates have historically been volatile, making both depositors and investors wary. \*\*Rate on 1-year deposits; lower rate offered used to calculate average, as of 2010. \*\*\*Market returns at 16%–18%.

**Exits have been limited, among both impact investors and commercial investors.**

Given the nascent commercial and impact investment markets, few investors have exited deals. The exceptions are hydropower projects, which have had a few exits through IPOs and, in turn, are driving greater interest in the sector. Interestingly, regulations allow for hydropower projects to be listed even before the project begins.

**While equity investors would prefer exits via IPOs, it is more likely that exits will happen through secondary sales, trade sales, or owner buybacks.** IPO is preferred as investors believe that this exit option will yield the strongest returns. However, for now, the capital market is fairly small and not very vibrant. Additionally, the mandatory three-year post-IPO lock-in period (for investors holding equity stakes pre-IPO) is a key challenge that deters investors from making equity investments in the first place. Investors are hoping that IPO exits will be a feasible option by the time they are ready to exit as the capital market grows, but expect other exit mechanisms to be more likely. In particular, investors look at the large potential market in India as an exit option for both secondary sales to larger Indian funds and trade sales/acquisitions by Indian companies looking to expand.

## Beyond the impact investing market

**In addition to the eight impact investors, there is a peripheral group of impact-related investors that currently have investments worth USD 13.6 million.** These investors include one small local fund making small ticket investments of between USD 2,000 and USD 8,000. There are also eight commercial banks using DFI capital to make SME loans. While this is a common activity of DFIs in the other countries under study, it has been limited by comparison in Nepal as DFIs are just entering the market and banks do not have the potential to reach many SMEs.

**Debt is the preferred instrument among these investors, reflecting the large share of commercial bank lending to SMEs in this ring.** Indeed, apart from only one USD 5,000 equity investment that has been made by a single investor, all investments in activity peripheral to impact investing have been deployed as debt.

**While little is known about the individual portfolios of the commercial banks, it is likely that there is wide diversity in the sector, deal sizes are small, and investees are in the growth stage or are mature companies.** Sector selection, ticket size, and growth stage preferences differ by lender. However, most lenders are sector agnostic; they look for investments that are financially viable in any sector. Therefore, there is likely to be some diversity in the sectors absorbing capital. Given that the loans are targeting SMEs, ticket sizes are small. Banks require an operating history, so it is likely that no seed (and minimal VC) funding is available. The other investor in this ring has also been making small deals and is opportunistic with respect to sector selection; however, this investor has only invested in venture stage companies as their capital needs are small (and match the fund's desired ticket size) and the fund manager has experience with companies in early growth stages.

## Challenges facing impact investors in Nepal

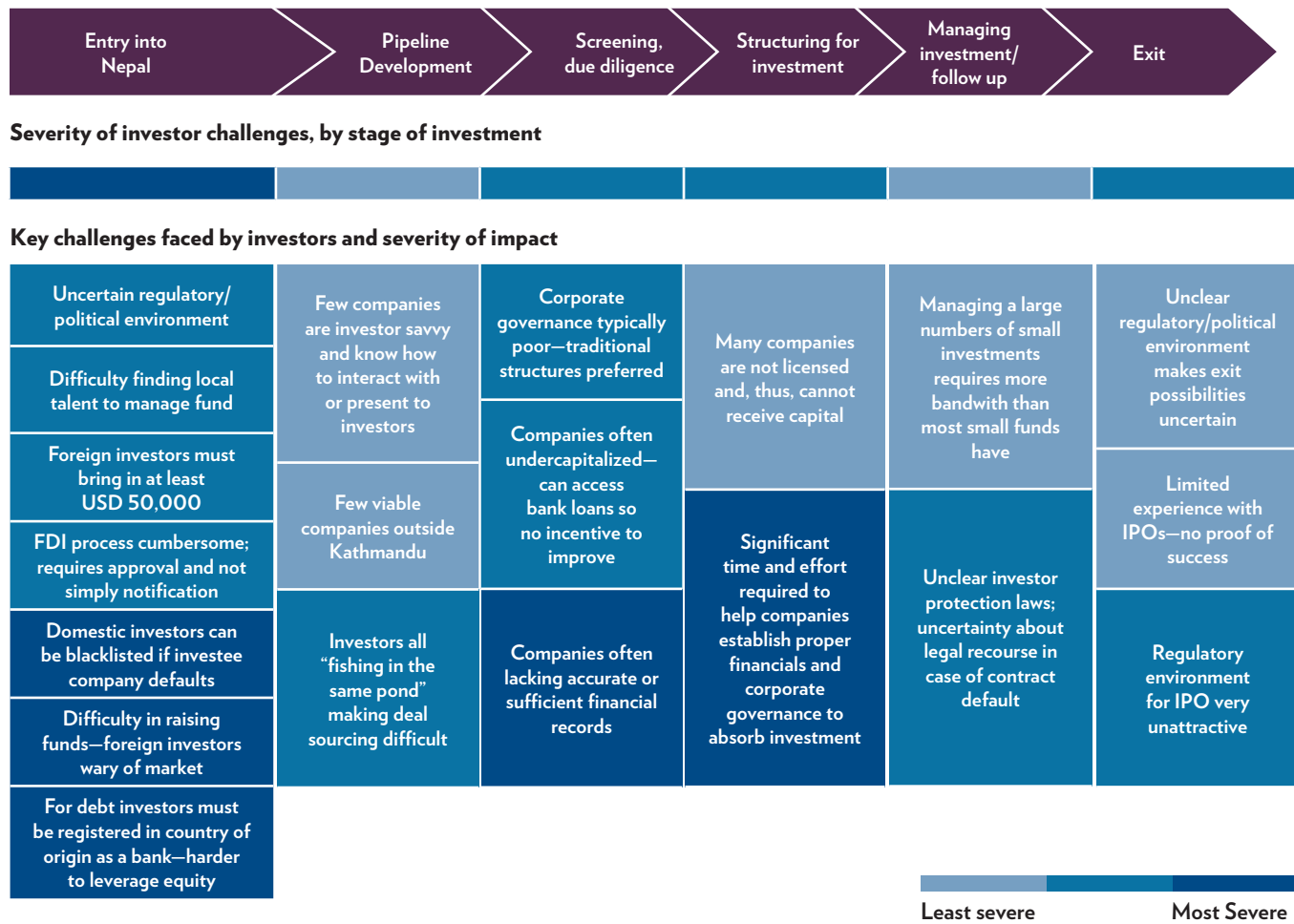
Looking across the investment cycle, investors struggle to get an initial foothold in Nepal due to cumbersome regulations (discussed further in the section titled “Enabling impact investing: the ecosystem”) as well as challenges in converting identified opportunities into investable deals (Figure 16). In the early stages of entering the market, investors face particular constraints navigating regulatory processes (particularly those related to registration and approvals) and identifying talented fund managers (since there is little history of PE/VC in Nepal, there are few experienced managers). Foreign investors face a cumbersome FDI process, which requires a minimum investment of USD 50,000 and pre-investment approval by certain authorities (rather than post-investment notification as in other markets).

Domestic investors, while not facing the same challenges, are subject to a “blacklisting” regulation that states that equity investors in a company that defaults or fails altogether are blacklisted in the financial markets, a threat that significantly lowers the investors’ risk appetite. Further, fund managers find it difficult to raise funds from both foreign and domestic investors who are uncertain of the potential in Nepal as illustrated in Figure 16.

**In addition to restrictive or deterrent regulatory elements, the uncertainty and unpredictability of the application of regulations is additionally a deterrent.**

For example, investors express that regulatory restrictions related to IPO exits are a barrier to investments—both in their official form and in the uncertainty of their enforcement. With a limited history of IPOs in the market, investors have no evidence of the viability of this exit option. Therefore, while defined on paper, there is no certainty that the regulatory process will be followed in practice. Furthermore, the regulations require a binding three-year lock-in period for investors following a listing and the premium valuation of shares is not allowed; instead, shares can only be listed at the present value.

FIGURE 16: CHALLENGES FACED BY INVESTORS AND ASSET MANAGERS ACROSS THE INVESTMENT CYCLE



Source: Stakeholder interviews; Dalberg analysis

**In terms of pipeline development, while never an easy task, the small size of Nepal’s market in this case presents some advantages.** The small market is made even smaller by the fact that most of the economic activity is concentrated in the Kathmandu Valley, and therefore most of the investible opportunities are concentrated there as well. On the flip side, this does at least make the identification of enterprises easier. While there is some level of “fishing in the same pond,” pipeline identification is possible through networking and relationship building as in most markets, and through alternative strategies such as working with commercial banks and other network points for enterprises.

**However, the real challenge for investors in Nepal is getting identified enterprises to the point where the execution of a deal is possible.** Above and beyond the standard due diligence, extensive and time-intensive work is needed to develop financial records and projections, business plans, governance structures, etc., as part of the deal-structuring phase. This can take months to achieve and requires significant hands-on investor engagement.



**FIGURE 17: FUNDRAISING CHALLENGES FOR FUNDS AND FUND MANAGERS**

<p>Difficulty raising funds and long fundraising timelines</p>		<ul style="list-style-type: none"> <li>• One fund took approximately 2.5 years to raise USD 20 million and has been primarily funded by DFI/IFIs</li> <li>• One fund raised capital from a DFI, but was unable to raise any additional capital</li> <li>• The remaining funds have not raised capital, but are/were either self funded, funded by winnings from a business competition or pair HNWLs with investable businesses to facilitate investments from HNWLs to business</li> </ul>
<p>Funds put on hold/closed</p>		<ul style="list-style-type: none"> <li>• Two funds seemingly closed after poor performance and one fund was put on hold due to management issues</li> <li>• One fund has not yet deployed any capital, but has deals in the pipeline. Many investors (including DFI/IFIs) waiting to see how this fund performs before releasing or committing capital</li> <li>• DFI/IFIs have put investments on hold</li> </ul>
<p>Challenges with foreign capital investments</p>		<ul style="list-style-type: none"> <li>• Overseas funds are restricted to equity deals, because regulations require that debt providers be registered in their country of origin as a bank</li> <li>• The Government of Nepal is considering an increase in FDI minimum from USD 50,000 to USD 200,000</li> <li>• Bringing in foreign capital is time consuming, difficult, and may require bribes be paid</li> </ul>



Source: Stakeholder interviews; Dalberg analysis

## Looking forward

Apart from the roughly USD 54 million capital that has been raised or committed to be deployed in the next 2-3 years, there are a few investors looking to raise additional capital for Nepal. While the size of these anticipated increases is much smaller than in other markets, these increases still represent a significant volume when compared to existing deployment. The investors will be a combination of DFIs and bilateral donors who are exploring the use of investment instruments to supplement their traditional grant-based financing. In fact, a few donors have expressed interest in anchoring investment funds or making direct investments. Finally, there is a small angel fund under consideration by existing Nepali investors that would meet a vital need for seed funding provided alongside technical assistance and mentorship.

In addition, a recently announced government program will provide USD 5 million to start-ups. No details are available on the program as yet. It is expected to take a year or more for the fund to open.

# NEEDS AND OPPORTUNITIES: THE DEMAND SIDE

## Overview of social enterprise ecosystem in Nepal

Like impact investing, the concept of impact enterprise, as defined by this report,<sup>18</sup> is relatively new in Nepal, and very few enterprises have been started with an impact intention. Stakeholders suggest that a large proportion of enterprises in Nepal are focused exclusively on financial returns, but there has been a recent shift toward operating socially minded businesses. The shift is being driven by investors and consumers who are interested in supporting socially conscious companies and buying environmentally friendly products.

As a result of both the small size and the nascent status of the impact enterprise landscape as well as the broader concerns related to the market, we see very little impact capital directed into impact enterprises. Rather, investors deploy capital into SMEs or enterprises operating in sectors where, irrespective of the business model itself, the investors perceive an opportunity to broadly meet their dual social and financial mandates. In Nepal, these sectors have been hydropower—given the limited access to energy and large, untapped hydro potential in the country—and tourism, which is expected to generate significant economic growth.

Given the agricultural base of the economy, there are a large number of agricultural and agro-processing enterprises that seek to develop more inclusive supply chains. While for many entrepreneurs in the sector, “impact” was often not a core consideration in developing their businesses and business models, increasing awareness implies there may be a shift to explicitly incorporate social and environmental impact into the model once the enterprise is established.

While potentially an interesting target for impact capital, investors perceive two ongoing challenges: i) most enterprises are small scale as agriculture is mostly for subsistence and commercialization is still limited, and ii) while there are many enterprises in the sector, most are unused to external capital and the vast majority are outside the Kathmandu valley, making access and identification by city-based investors difficult.

Secondly, education and, to a lesser extent healthcare, are also attracting entrepreneur attention, driven by the potential market arising from remittance-fuelled disposable income. Early entrepreneurs in education have focused on lucrative private coaching centers and college/university prep centers, but a growing number are exploring the potential of low-income private schools, successfully drawing students out of the public system as families prioritize quality education with their increased incomes. While a similar trend could be possible in healthcare—as

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<sup>18</sup> For the purposes of this study, we define impact enterprises as those that have articulated a core objective to generate a positive social or environmental impact (as a part of their operating model rather than an ancillary activity), and seek to increase their financial viability and sustainability.

remittances increase incomes, populations become more discerning and willing to pay for private care—the regulations in the sector create relatively high barriers to entry. Therefore, impact enterprise activity in the sector may be slower to take off.

**Energy is the third area that is increasingly seen as a growth opportunity for impact enterprises and therefore, for investors as well.** Nepal offers massive untapped potential in the sectors of hydro and wind energy, and as the current energy demands are not being met, there is notable scope for innovative enterprise models to meet household needs. While experimentation and entrepreneurship in the sector are still limited, and the focus remains on relatively large-scale hydro plant development, there is potentially an opportunity for small-scale enterprise activity in the sector as well.

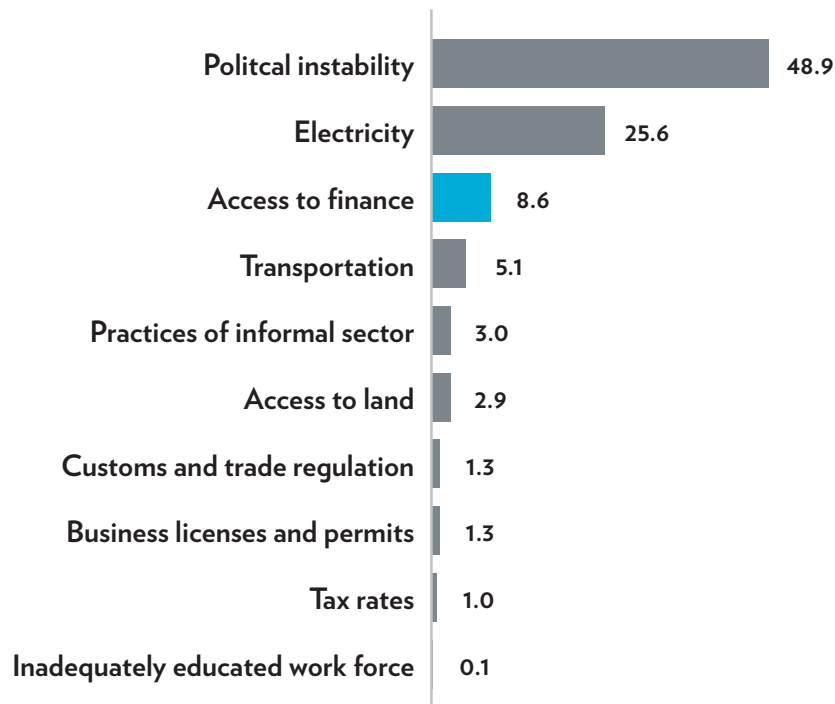
**Ethically sourced handicrafts are a growing market, largely driven by foreign tourists.** Handicraft stores in Kathmandu valley and other tourist spots are selling woven products, jewelry, and cosmetic and bath products produced using ethically sourced inputs. These retail stores often source directly from local women's cooperatives that manufacture the products. The market is largely driven by foreign tourists.

**That said, while opportunities are certainly visible in the market, the low level of familiarity with the impact enterprise concept means that thus far, there has been little innovation in the space.** Some investors believe that once impact-oriented funds become more active and start to target and develop viable impact enterprises, the awareness and attractiveness of the model will grow; entrepreneurs that may have been operating with dual social and economic objectives without explicitly defining as such may start to rearticulate their models and new approaches may be developed.

## Constraints to enterprise growth

**As shown in Figure 18, access to finance is the third biggest constraint to growth in Nepal, preceded only by political instability and access to electricity.** Power access is particularly important for enterprises in manufacturing industries where the key issues are related to reliability and consistency, given the context of heavy load shedding in Nepal, rather than connectivity or access itself.

**FIGURE 18: ENTERPRISE CHALLENGES (PERCENTAGE OF RESPONDENTS IDENTIFYING A CERTAIN CHALLENGE AS THE LARGEST CONSTRAINT TO BUSINESS)**



Sources: IFC Enterprise Survey of 482 enterprises in Nepal; Stakeholder interviews; Dalberg analysis

**The access to finance constraint is driven by multiple sub-factors (Figure 18).**

For business managers, access to capital (rather than its availability) is often the more pressing issue. In particular, many enterprises do not know where to look or how to identify sources. Often, the capital available is not appropriate for the needs of business managers, and the process of obtaining capital also prevents access. For instance, the low level of innovation in bank products means a poor fit for enterprise needs: no bridge loans or project finance products are available, and working capital loans are only given against stock (which may not exist in the early stages).

**Like investors, entrepreneurs also face certain challenges while raising finance in the capital markets as they are similarly dissuaded by the regulatory conditions.**

As discussed previously, regulations in Nepal require a three-year lock-in period for investors and prohibit the premium valuation of IPOs. As such, business managers have little incentive to list shares on the public market.

**As expected, we see that the extent and manifestation of these challenges vary by enterprise growth stage.** Seed stage enterprises can often, although not easily, access capital through microfinance or informal channels. Therefore, it is after the initial injection and before the company is fully profitable or with stable revenues that the greatest constraints are felt.

FIGURE 19: SEVERITY OF ACCESS TO FINANCE CHALLENGES FOR BUSINESS MANAGERS BY ENTERPRISE GROWTH STAGE



**Severity of access to finance challenge, by stage of growth**



**Key challenges faced and severity of impact**

**Identifying sources of capital**

Limited formal sources of capital for early stage; most seed funding from friends and family	For large loans, banks prefer only to loan to companies with whom they are familiar or have a lending history	
Few domestic investors take equity stakes in private companies; they either invest equity in enterprises within their own networks (which are easy to vet) or they invest in public equity markets		
Many entrepreneurs are wary of banks due to belief that bank employees may steal business idea	International investors not interested in or cannot enter Nepal market	Small capital market with mostly banks listed
Outside of banks, there are a minimal number of capital sources present in the country		
Banks do not reach a large portion of the population		

**Appropriateness of capital**

Low levels of understanding among business managers of non-debt instruments and appropriateness of instrument given needs/stage (e.g., debt in early stages can be crippling due to interest repayment)		Regulations inappropriate—act as a deterrent or disincentive (e.g. 3-5 year lock-in period, no premium valuation)
	Uncertainty about legal recourse available if issues arise with equity investor	
Tenure of bank loans not appropriate—in early stages need long term loans with long grace periods before company is revenue positive		High levels of volatility in interest rates can be crippling and reduce ability to repay
Low levels of innovation in bank products means poor fit for enterprise needs—e.g. no bridge loans or project finance products, working capital loans only given against stock which doesn't exist in the early stages, etc.		

**Accessing capital**

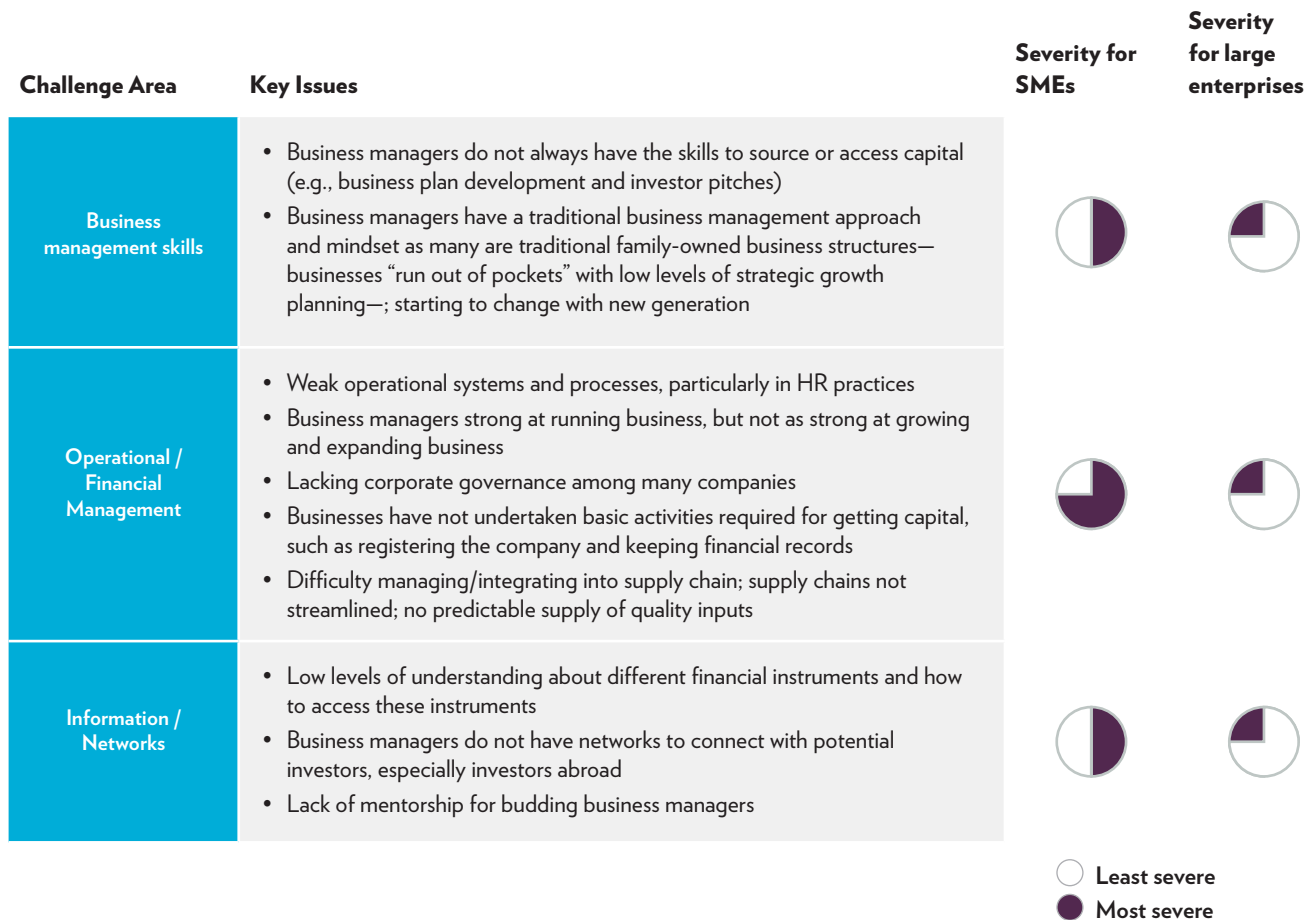
Complicated process of applying for capital and negotiating terms of investment, due to lack of investment-related experience		Uncertainty about IPO process and perceptions of restrictive nature
Difficult to secure reliable third party valuation; enterprises themselves don't understand or have the capability		
Companies have not kept accurate financial records (by design to avoid taxes or by default due to lack of knowledge) and investors require 1+ years of operating records		Owner can only sell to other owner—limits ability to exit through IPO
Collateral requirements are high, too high for new/young enterprises; entrepreneurs often take personal loans or use unregulated financial institutions, both of which have higher interest rates		
Working with foreign investors is more difficult due to cultural mindset—perceptions of how things should work based in home country are different		

Source: Stakeholder interviews; Dalberg analysis



In addition to limited access to finance, enterprises struggle to grow due to lack of business and management skills—a gap identified by entrepreneurs, investors, and ecosystem players. In particular, for SMEs, the low levels of operational and financial management skills are a significant constraint to growth, particularly around financial record keeping and planning, HR management, and supply chain management.

FIGURE 20: KEY CONSTRAINTS FACED BY ENTERPRISES OF DIFFERENT SIZES



Source: Stakeholder interviews; Dalberg analysis

# ENABLING IMPACT INVESTING: THE ECOSYSTEM

The two broad dimensions of the ecosystem to consider are the macro investment climate (including considerations such as ease of doing business, political stability, macroeconomic governance, infrastructure strength and reliability, and the regulatory framework) and the specialized support available for investors and enterprises for navigating the investment landscape (such as deal sourcing and matchmaking, and enterprise development).

## The macro investment climate

**The macro climate for investors has been improving slowly along certain dimensions, but in general, it remains fairly unattractive.** While ranking fairly highly in our study country set (lower than Sri Lanka and India but higher than the rest), overall, Nepal ranks 105 out of 189 countries in the World Bank “Doing Business” rankings. Nepal scores relatively high on protecting investors with a ranking of 80 and the ease of starting a business rank improved from 103 to 97 between 2013 and 2014.

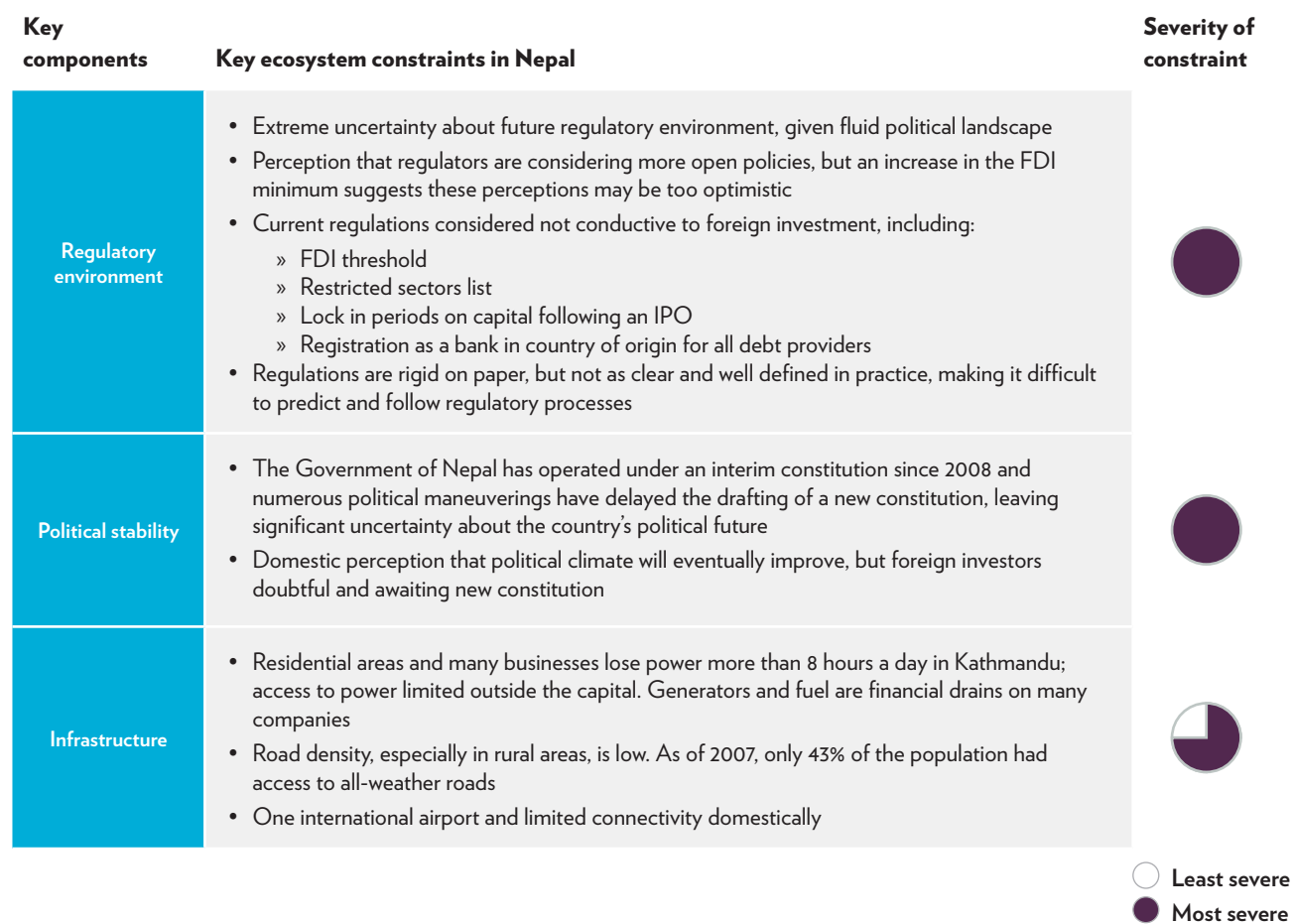
**Investors and entrepreneurs are optimistic that shifting political conditions, and a new constitution (currently under negotiation) will open markets and lead to more liberal policies and regulations.** However, delays in the political process to date leave them uncertain of when the changes will come and exactly how positive these changes will be. In the meantime, a variety of regulations reduce the appeal for investors or prevent entry altogether. Some of these regulations have been discussed previously and are highlighted below.

- ✓ Foreign investors must bring at least USD 50,000 for investment, and the government is considering raising this threshold to USD 200,000.
- ✓ Foreign investors must gain approval from the Department of Industries for all equity investments. For new equity investors, the process requires additional registration and approvals.
- ✓ A foreign investor providing debt must be registered with the appropriate officials as a bank in their country of origin, and the loan must also be approved by the Department of Industries.
- ✓ Foreign investors are restricted from investing in 21 sectors under the Foreign Investment and Technology Transfer Act of 1992. However, the current list is under review and a new policy seeks to reduce the number of sectors restricted to foreign investment from 21 to seven. Sectors that are likely to remain restricted under the amended framework include real estate and housing (excluding construction), hotels that have a ranking of less than three stars, multi-brand retail businesses with investments of less than USD 50,000, cottage industries, arms and ammunition, and coins and currency.

- ✓ Domestic investors can be blacklisted from financial markets if they hold equity in a company that fails. Foreign investors were recently exempted from this regulation.
- ✓ The Securities Registration and Issue Regulations Act requires that pre-IPO investors are locked in for a period of three years following a public listing.
- ✓ Upon public listing, no premium valuation of shares is allowed.

**Perceptions of political and policy instability are compounded by the weak infrastructure—particularly, power and road infrastructure.** Although nearly 80% of the population has access to electricity, power is unreliable, with residential and business areas losing power for up to eight hours a day. Many businesses are forced to use generators, which are a financial drain. Meanwhile, poor road conditions make it difficult to access areas outside Kathmandu—disrupting supply chains, increasing the cost of travel and shipping, and making it difficult for investors to scope for companies outside the Kathmandu valley.

**FIGURE 21: SEVERITY OF INVESTMENT CLIMATE CONSTRAINTS IN NEPAL**



Source: Stakeholder interviews; Ministry of Industry “Invest Nepal” and policy documentation; Nepali news reports; Dalberg analysis



The general perception is that the new government and the heads of key bureaucratic divisions are pro-private sector and will institute business-friendly reforms. However, the key question for investors and entrepreneurs is related to the pace of such reform, and the perception is that although positive, the change will be slow.

There are three institutions leading the efforts to improve the investment climate (in partnership with donors and DFIs): the Nepal Investment Board, Nepal Rastra Bank, and the Securities Board of Nepal. While investors seem to believe that all three regulatory bodies are pro-private sector growth and thus, investment-friendly, there are varying degrees of belief in these bodies' ability to address the existing gaps in policy (Figure 22).

FIGURE 22: ROLE, MANDATES, AND PERCEPTIONS OF THE THREE KEY REGULATORS



<p>Nepal Investment Board</p>	<ul style="list-style-type: none"> <li>Established under the Investment Board Nepal Act in 2011</li> <li>Promotes economic development by creating and ensuring an investment-friendly climate</li> <li>Functions include mobilizing and overseeing investments, setting investment priority areas, selecting investment projects</li> </ul>	<ul style="list-style-type: none"> <li>Perception that Nepal Investment Board is supportive of private sector development and improvements to investment climate</li> <li>Able to interface with foreign investors</li> </ul>
<p>Nepal Rastra Bank</p>	<ul style="list-style-type: none"> <li>Founded in 1956 under the Nepal Rastra Bank Act</li> <li>Monetary, regulatory and supervisory authority of banks and financial institutions</li> <li>Functions include regulating and overseeing banks, monitoring economic situation, promoting financial services and setting monetary policy</li> </ul>	<ul style="list-style-type: none"> <li>Perception that bank is aware of policy gaps and willing to address these gaps</li> <li>Uncertainty about the future direction of Bank policy, given shifting political climate and new constitution</li> <li>Process is expected to take time (One year to sign new constitution)</li> <li>Perception that there are very low levels of understanding about new financial instruments, leading to difficulty in regulating instruments they don't understand</li> <li>Concern about bureaucrats' ability to work with foreign investors</li> </ul>
<p>Securities Board of Nepal (SEBON)</p>	<ul style="list-style-type: none"> <li>Set up in 1993 under the Securities Act</li> <li>Registers securities; regulates sale, transfer and exchange of securities; supervises and monitors stock exchange; supervises investment funds and grants permission for their activities</li> </ul>	<ul style="list-style-type: none"> <li>Appear supportive of regulatory changes that promote investment and private sector development</li> <li>Concern about bureaucrats' ability to work with foreign investors</li> </ul>

Source: Stakeholder interviews; Dalberg analysis

## Support for investors and enterprises

There are a growing number of service providers for investors and enterprises, but this support is not sufficient or advanced enough. Little is known about the changing regulatory environment, and there is no support for investors navigating the regulations. No “one-stop shop” exists to support investors with navigating the process of registering.

FIGURE 23: CONSTRAINTS TO INVESTOR AND ENTERPRISE SUPPORT IN NEPAL

	Key components	Key ecosystem constraints in Nepal	Severity of constraint
Investor and Enterprise support	Investor support	<ul style="list-style-type: none"> <li>• Little is known about the changing regulatory environment and there is no support for investors navigating the regulations</li> <li>• DFI/IFIs and large funds advocating to regulators/policymakers on behalf of investors</li> <li>• No local providers of investor support, but many fund managers are expats or have worked/been schooled abroad and have a strong grasp of the financial sector</li> <li>• No “one stop shop” for investors to register—e.g. Department of Industry approves FDIs, Central Bank approval, etc.—and no assistance provided to navigate process</li> </ul>	
	Enterprise support	<ul style="list-style-type: none"> <li>• In addition to access to finance challenges, entrepreneurs face a range of other constraints to growth including their own business mindset, skills and knowledge, as well as access to information and networks</li> <li>• Given the small market size in Nepal, there are quite a few providers of business support services, but these providers are typically small and new to the space</li> <li>• Key areas of need include:               <ul style="list-style-type: none"> <li>» Aggregation/networking/knowledge sharing amongst entrepreneurs</li> <li>» Training in key business management functions—both strategic and operational</li> </ul> </li> </ul>	

○ Least severe  
● Most severe

Source: Stakeholder interviews; Dalberg analysis

While there has been some history of donor programs (including some run by Gesellschaft für Internationale Zusammenarbeit (GIZ) and Stichting Nederlandse Vrijwilligers (SNV)), private players are only just starting to enter the enterprise development or support landscape and very few are well known or easily accessible. Given the current focus on improving the investment climate and regulatory environment, there has been a heavy emphasis on institutional capacity building and policy advocacy. As a result, enterprise development support has not been emphasized as heavily, although there is recognition now of the severe need in this area with the emergence of private providers.

FIGURE 24: EMERGING PLAYERS IN ENTERPRISE SUPPORT LANDSCAPE IN NEPAL

**Incubators/Accelerators**



**Advisory Services**



**Credit Rating Services**



**TA Providers**



\* Has not yet started but is in final fundraising and should host first cycle this year

Sources: Stakeholder interviews; Dalberg analysis

While the ecosystem seems to be evolving and growing, it is not yet sufficient to address the needs of entrepreneurs and investors in the market. Investors hope that a new constitution will bring about regulatory structure and certainty, kick-starting the investment market and enabling continued growth.

# AREAS FOR FURTHER RESEARCH

As Nepal represents a still-maturing impact investing landscape, there exists scope for additional research to highlight key opportunities in the country. First, in addition to determining what innovations in financial products are optimal for a nascent enterprise and investing market, further insight on what will make the market more attractive overall, would be beneficial. Investors from abroad are not yet very interested in the Nepal market, given the country's small population, small GDP, and a very small number of companies that can actually absorb capital. Furthermore, exposure to financial services and investor experience in Nepal is limited. Given a very young and not fully supportive overall ecosystem for impact investing, further research can highlight how to catalyze impact enterprise growth, increase investor knowledge and experience in-country, and pinpoint areas of interest for foreign investors.

Second, most of what is known about the impact investing market in Nepal reflects what is happening in Kathmandu only and not the activity outside this region. A greater understanding of what is happening in the surrounding areas would be helpful to the investors.

Third, further study in specific sectors of interest, including tourism and hydropower, to estimate the financial performance and impact of historical activities, will provide lessons that will guide the market growth.

Lastly, specific research on the effect of remittances from abroad on the private uptake of traditionally public services would be interesting. For example, there are several start-up enterprises that provide basic services, such as water, sanitation, healthcare, and education. Families in Nepal can, to a large extent, consume these services because of their remittance income, which is a significantly high percentage of the country's GDP. If foreign nationals further develop an interest in investing in small enterprises, remittances may begin to fuel investments in growing start-ups in Nepal, as a trend.

# ANNEXES

## Annex 1—Interview participants

### FUND MANAGERS

- Bidhya Sigdel and Shabda Gyawali, *Dolma Development Fund*
- Willem Grimminck and Niraj Khanal, *One to Watch*
- Saurya SJB Rana, *Tara Management Pvt. Ltd*

### DEVELOPMENT FINANCE INSTITUTION (DFI)/ INTERNATIONAL FINANCIAL INSTITUTION (IFI)

- Navin Dahal, *DFID*
- Deep Karki, Valentino Bagatsing, and Santosh Pokare, *IFC*

### ECOSYSTEM PLAYER

- Vidhan Rana and Sanam Chitrakar, *Biruwa Ventures*
- Suman Rayamajhi, *Eos Advisors*
- Prabhat Shrestha and Robin Sitoula, *Lead International*
- Radesh Pant, *Nepal Investment Board*
- Willem Grimminck, *Rock Start*
- Saurabh Rijal, *Saadhya*
- Niraj Giri and Mukti N. Shrestha, *Securities Board of Nepal*

### ENTERPRISES

- Kumud Sing , *Alpine Coffee Estate*
- Bhuwan K.C., *Ecoprise*
- Samir Newa, *The Organic Village*
- Anand Bagaria, *Pro Bio-Tech Industries and Nimbus International Co.*

## Annex 2—Survey respondents

### FUND OR FUND MANAGER

- Willem Grimminck and Niraj Khanal, *One to Watch*

### ECOSYSTEM PLAYER

- *Solutions Consultant Pvt. Ltd.*

### ENTERPRISES

- Kumud Sing, *Alpine Coffee Estate*
- Bhuwan K.C., *Ecoprise*
- *Health at Home Pvt. Ltd.*
- Anand Bagaria, *Pro Biotec/NIMBUS*
- *Shree Krishna Livestock Devt. Farm*
- *WindPower Nepal*