

FIELD Report No. 3

Delivering Microfinance and Social Services in Conditions of Fragility in Nepal

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Acronyms

CBB	Chhemek Bikas Bank
CBO	community-based organization
IG	income generation
MADE	Multidimensional Agriculture Development
MFI	microfinance institution
MUM	Mahila Upakar Manch
NGO	non-governmental organization
NRB	Nepal Rastra Bank
NUB	Nirdhan Utthan Bank
OCDL	Oppressed Community Development Center
PVO	private voluntary organization
SAC	Social Awareness Concerned Forum
SC	Save the Children
VDRC	Vijay Development Resource Center
YCL	Young Communist League

Executive Summary

Natural disasters, civil conflicts and the HIV/AIDS pandemic are forcing an increasing number of people to live in conditions of fragility, complicating the delivery of basic public services. Despite the obstacles posed by these fragile conditions, relief and development organizations as well as national governments have been able to increase their outreach to affected populations by developing new approaches and strategies. This case study documents the strategies used by microfinance institutions (MFI), non-governmental organizations (NGOs) and private businesses to deliver financial and non-financial goods and services (e.g., business development services; health and education services; basic consumer goods; sanitation services) to populations affected by the Maoist insurgency in Nepal.

The case study is based on interviews with several of these service providers and with beneficiaries from two districts of Nepal. It discusses restrictions on the operations of service providers imposed by both the Maoist rebels and the Nepalese government security forces, the direct impact of the conflict on them and their beneficiaries and the coping mechanisms and strategies they developed in response to the conflict.

Based on this experience, the case study draws several lessons for wider use by relief and development organizations, local governments, donors and local NGOs and community organizations. These lessons include the benefits of engaging communities and direct beneficiaries in project activities, the need for innovative design and delivery of services under conditions of fragility, the value of partnering with the private sector and using local NGOs and community organizations to deliver services and defining an appropriate role for government agencies when they themselves are a party to an ongoing conflict.

Background

Relief and development organizations, as well as governments around the world, increasingly face fragile environments as they expand the outreach of basic services, such as health, education, water and sanitation, public safety and livelihood and enterprise promotion. This situation has been amplified by recent natural disasters, such as the Aceh tsunami in 2005, Hurricane Katrina in 2006 on the southern coast of the United States, the 2007 earthquake in Pakistan, the worldwide HIV/AIDS pandemic and the prolonged civil unrest that has crippled over 40 countries today.¹ Conditions of fragility can be identified as those prevalent in countries, regions or communities that have experienced significant political conflict and lawlessness, are difficult to reach (either because they are slums or are extremely remote) and are affected by natural disasters, pandemics and/or severe starvation. Fragility scenarios can range from conditions of political and socioeconomic deterioration, active conflict and/or arrested development to post-conflict and early recovery conditions.

This case study aims to document the experience of NGOs, government agencies and the private sector in delivering microfinance, enterprise development and basic social services under conditions of fragility in Nepal. By analyzing their experience, the case develops lessons learned and better practices for the delivery of such services that can be disseminated on a wider basis.

Nepal plunged into a state of fragility when the Maoist insurgency started in 1996. Within a few years, Maoist forces took control of large swathes of rural Nepal, setting up a parallel administration. During the last ten years, the insurgency has dramatically affected the country's socioeconomic conditions at both the macro and micro level. The strict restrictions imposed by the conflicting parties (i.e., the Nepalese government and the Maoists), together with frequent strikes and road blocks, closed down transportation systems, markets, and educational and other institutions. Almost 15,000 people lost their lives and the infrastructure of the country sustained heavy losses.² Communities suffered due to interruptions in or the discontinuation of basic social services, such as health, education, sanitation, basic commodities and livelihood and enterprise promotion.

Although the Maoists signed a peace agreement in 2006 and subsequently joined the parliament and government, much of rural Nepal remains in a state of lawlessness.³ Since the Maoists agreed to participate in the government, splinter groups have emerged under different names as regional and ethnic forces. These groups have used terror tactics commonly employed by the Maoists and have contributed to anarchy and interruptions in the delivery of basic social services. To engage their young supporters, the Maoists created a group called the Young Communist League (YCL), which is presently being blamed for interfering in law and order. Overall, the situation in the country has improved significantly since the 2006 peace agreement, but Nepal still rates low on several factors of fragility (see table I).

During the Maoist insurgency, the ability of microfinance institutions (MFIs), non-governmental organizations (NGOs), community-based development organizations (CBOs), local governments and private businesses to deliver services to local communities was severely impaired. While the Maoists harassed these organizations as an extension of the state with which they were fighting, government

¹ This estimate is derived from www.globalsecurity.org (accessed July 2007).

² Laxmi Iyer and Quy-Toan Do, "High Hills, Deep Poverty: Explaining Civil War in Nepal," Harvard Business School Working Knowledge Paper, Harvard University, Cambridge, Massachusetts, 2007.

³ International Crisis Group (ICG), "Nepal's Peace Agreement: Making it Work," Crisis Group Asia Report No. 126, 2006.

security forces also interfered in their operations in the name of maintaining law and order. Faced with an extremely difficult working environment, these organizations used several coping mechanisms and invented new and better ways of delivering their services. Accordingly, many organizations were able to survive; some even grew and expanded their outreach. In view of growing conditions of fragility around the globe, it is important to document and disseminate the lessons learned by these organizations in Nepal.

Table I: Current Situation of Fragility

	Deterioration	Post-conflict	Early Recovery
Security of life and property		X	
Law and order	X		
Economic disruption	X		
Discontinuation of public services		X	
Capacity of the government			X
Political ambiguity		X	

Source: Based on interviews with MFIs, NGOs, businesses, beneficiaries and opinion leaders in Nepal, 2007.

Objectives and Methodology

Objectives

Based primarily on the experience of several MFIs, NGOs, CBOs and local government units that operated under the Maoist insurgency in Nepal, this case study explores options for continuing to deliver and even expand microfinance, enterprise development and social services in politically unstable areas. Specifically, the case study:

- assesses the impact of the insurgency on the delivery of essential services in Nepal;
- analyzes the experience of service providers in coping with fragile conditions resulting from the Maoist insurgency; and
- documents lessons and explores ways of ensuring and enhancing the delivery of basic services in politically fragile areas.

Methodology

Information for this case study was collected from primary as well as secondary sources. Primary information was collected through detailed interviews with MFIs, NGOs, government units and private businesses (as service providers), as well as with community members (as service recipients). Because the case study aimed to develop lessons learned, rather than quantify the impact and coping measures of service providers, only two districts of Nepal were selected for interviews. One district was severely affected by the insurgency, the other was moderately affected. In each district, two MFIs (one branch of Nirdhan Utthan Bank and one independent MFI), two NGOs, five businessmen, two government units and about 30 beneficiaries were interviewed.

Site visits and focus groups were also conducted to corroborate and validate the information gathered in interviews. To ensure consistency, the reference period was established as the time period from the beginning of the insurgency until the peace agreement; respondents were accordingly asked to share their experience of this period. The survey covered four essential services (microfinance, non-financial enterprise development services, social services and the supply of essential consumer goods) that the aforementioned providers struggled to deliver to local communities. While the sample size is a major limitation of this study, the research findings shed ample light on how the delivery of essential services can be ensured in politically fragile environments.

Delivery of Microfinance Services during the Insurgency

Although 19 commercial banks, 29 development banks, 63 finance corporations and 11 rural microfinance banks are engaged in microfinance in some manner in Nepal,⁴ there are only about 25 credible dedicated microfinance institutions in the country. Most, if not all, of these institutions were seriously affected by the insurgency.⁵ This case study interviewed two branches of the Nirdhan Utthan Bank (NUB), one in the Banke and one in the Bharatpur district, as well as the Chhemek Bikas Bank in the Bharatpur district and the Mahila Upakar Manch in the Banke district.

NUB is one of the largest MFIs in the country and delivers only microfinance services, while CBB and MUM deliver microfinance services along with other social services, such as livelihood and vocational training, legal awareness campaigns, health and sanitation programs, social and economic empowerment programs for deprived and vulnerable women, as well as campaigning against domestic violence. All three institutions have received licenses from the Nepal Rastra Bank, the central bank of Nepal, to undertake microcredit activities (see table 2 below).

Table 2: Brief Profile of MFIs Interview

	Nirdhan Utthan Bank	Chhemek Bikas Bank	Mahila Upakar Manch
Operations started	1993	2002	1992
Number of clients	Over 75,000	2,523	3,500
Coverage	8 districts	1 district	1 district
Services	Credit	Credit plus	Credit plus

Source: Records provided by NUB, CBB and MUM, 2007.

What did the Maoists do?

Large and small MFIs alike reported that the Maoists terrorized and intimidated them to keep them from doing business. They labeled the MFIs as agents of capitalism that exploited the poor. In their minds, MFI activities were designed to provide nominal, temporary benefits to the poor, which would never take them out of chronic poverty. Initially, the Maoists also saw MFIs as a security risk, believing that they employed government informants working in the guise of MFI staff. As a result, the Maoists used a number of terror tactics to discourage MFIs from operating in areas under their control, such as:

- coercing clients to default on their loans;
- vandalizing offices and looting documents (e.g., minute books and passbooks) and property;
- levying a 5 to 40 percent war tax (or donation) on staff salaries, as well as a fixed amount on project revenues;
- attempting to stop programs supported by countries that were supplying weapons to the Nepalese government (e.g., the USA, Belgium, India);

⁴ Website of “Private Sector Promotion: Rural Finance Nepal,” www.microfinance.org.np/microfinance.html (accessed July 2007).

⁵ Armen Hofmann and Helmut Grossmann, “Rural Finance in Conflict Environments: Experience from Nepal’s Small Farmer Cooperatives,” GTZ, Eschborn, Germany, 2005.

- requiring all residents to register with their “people’s government” and follow their rules; and
- abducting staff.

In addition to the interference described above, the Maoists imposed travel bans, blockades and market closures that were designed to spread terror and demonstrate the ineffectiveness of the national government. These tactics had an adverse impact on the general economy, business and livelihood opportunities for the poor, as well as on the operations of MFIs. Material deliveries, trainings and project staff visits were all constrained, resulting in delays in program implementation.

What did government security forces do?

Similar to the Maoists, state security forces on several occasions also harassed MFIs, impeding their business. For example, the government frequently ordered MFIs to close rural outlets and move to the cities and, in a few cases, they accused MFI staff of supporting the Maoists and threatened to physically harm them. While the activities of the security forces were based purely on security concerns, they nonetheless created severe obstacles for MFIs.

Impact of the conflict.

As a result of this difficult working environment, MFIs and their beneficiaries suffered on a number of fronts. Growth and outreach were restricted, portfolio quality deteriorated, operations in remote areas were discontinued, operating costs increased by 5 to 20 percent and profitability and sustainability declined. Beneficiaries suffered from reduced access to financial services, as well as deteriorating economic conditions that limited microenterprise opportunities. Initially, several MFIs took a “wait-and-see” approach, hoping that the conflict would soon be resolved. As it not only lingered, but became more widespread and severe however, the MFIs came up with a number of coping mechanisms at the operational and strategic levels.

Coping mechanisms.

While the microfinance industry took root in Nepal over the last 15 years, the country’s political landscape remained volatile. This period alternated between pre-conflict, active conflict and post-conflict conditions.⁶ However, MFIs hardly ever designed their products and operations with conflict in mind, even though almost every aspect of MFI operations were impacted by the ongoing political instability. This inattention to product and operational safeguards was partly due to the expectation that the conflict would neither linger nor intensify, and partly due to the MFIs’ lack of experience in delivering microfinance services in a conflict situation.

As a result, when the insurgency intensified, the MFIs were left with the sole option of adapting their products and operations to survive and grow. Internal adaptations aimed to increase flexibility and decentralization so as to reduce business risk, while external adaptations aimed to improve the general working environment in which they operated. The coping mechanisms invented and successfully used by the MFIs included product and service modifications, cultivating staff morale and implementing codes of conduct, conducting public relations, promoting transparency, partnering with other institutions and engaging in community mobilization, all of which are discussed below.

⁶ A “people’s movement” overthrew one-party rule in 1990 and established a constitutional monarchy. In 1996, the Maoists started a so-called “people’s war” that subsequently intensified. The year 2001 witnessed an unimaginable palace massacre. The new king suspended parliament and took direct control of the government in 2002. Another people’s movement re-established parliamentary democracy in 2006, paving way for the peace process that led to the inclusion of the Maoist party in the government.

1. ***Modifications of products and procedures.*** The first set of modifications made by MFIs in response to the political crisis focused on increasing their institutional flexibility and adaptability. These modifications touched on product features, delivery procedures, staff recruitment and training, client monitoring systems and information management, including:
 - keeping money directly in the control of clients as much as possible by disbursing all cash collected in center meetings to new borrowers at the same meeting;
 - arranging for the strict security of funds through various mechanisms, including timely deposits in better-guarded commercial banks, insuring fund transfers, etc.;
 - modifying the standard loan period from 12 months to shorter periods of 3, 6 or 9 months;
 - permitting loan rescheduling in case of emergencies beyond the control of a client;
 - encouraging clients to repay loan installments at branch offices (which had better security) rather than at center meetings by giving them a 2 percent discount on interest repayments;
 - reducing the interest rate charged on loans from 25 to 20 percent in response to requests made by beneficiaries and the findings from market studies;
 - decentralizing management decisions by empowering branches to determine when to stop and restart operations, as well as when to close during periods of severe unrest;
 - implementing new client monitoring systems that emphasized prompt follow-up in the case of non-payment;
 - removing computers from branches in the areas most affected by the insurgency;
 - backing up all data on two different compact disks, one of which was kept at the branch and the other, at the branch manager's house;
 - recruiting local employees and improving the gender and ethnic diversity of MFI staff; and
 - introducing staff incentive schemes.

2. ***Improving the morale of staff and clients; implementing codes of conduct.*** To help staff make the difficult choices required to modify products and procedures, the MFIs felt it was necessary to strengthen their morale and behavior. In addition, they felt that their staff and clients were their greatest assets and allies during the crisis. To unleash the potential support of clients and staff, MFIs thus implemented several morale-boosting and confidence-building activities via a comprehensive internal communications strategy. These activities included:
 - introducing an internal code of conduct or adapting the code of conduct developed by the Association of International NGOs in Nepal (see annex 2);
 - reaching out to clients to remind them of the value of the MFI services they received;
 - organizing workshops and exchange visits for center chiefs to provide them a broader understanding of MFI operations;
 - reaching out to client families, particularly husbands and fathers-in-law, to discuss MFI services and benefits and to answer their questions about MFI programs;
 - promptly following up with clients who were victimized by the insurgency, both to develop a loan repayment strategy and help rebuild their morale;
 - organizing senior management visits to branches affected by the insurgency, particularly those that were vandalized; and
 - organizing training programs for staff on negotiation, presentation and articulation skills.

3. ***Conducting public relations, communications and transparency efforts.*** While the above strategies described above allowed MFIs to reduce their operational and financial risks to some extent, the institutions recognized that their ability to minimize risks was limited and could not

ensure MFI survival and growth. It was therefore necessary to reach out to clients with a clearer message in a convincing manner in order to ensure external support and improve the sociopolitical context in which these institutions operated. To this end, MFIs developed a far-reaching public relations and communications strategy that included such elements as:

- building relationships with civil society organizations and ensuring their public support by involving them in negotiations with the insurgents (e.g., in cases of abductions, asset seizures, etc.);
- opening a dialogue and building relationships with local opinion leaders (which often included Maoist leaders) and explaining the positive impact of microfinance programs, as well as engaging them in its activities;
- launching massive public campaigns to make communities aware of MFI goals, activities and contributions to local society;
- conducting public relations campaigns to encourage communities to take ownership and responsibility for microfinance programs;
- increasing transparency through “public audit” meetings, including presentations on the community benefits of MFI programs, followed by open discussions and question-and-answer sessions; and
- developing better relations with the media by using newspapers, radio, TV and pamphlets to increase public awareness and support.

Box 1. The Kapali Group convinces the Maoists to let them to work with an MFI

Kapali is a self-reliance microfinance group organized by Nirdhan Utthan Bank in western Nepal. At the height of the insurgency, the Maoist rebels seized all its documents and forced Nirdhan to close the program. This act angered local members of the group, who decided to fight for their rights themselves. They called a meeting of members, NUB staff and local Maoist leaders, including the area commander, and explained how they had been benefiting from the program. They then asked the Maoists to provide an alternative if they closed down NUB. At the end of the meeting, the Maoists agreed to allow the bank to operate and, after two months of suspension, the program started again.

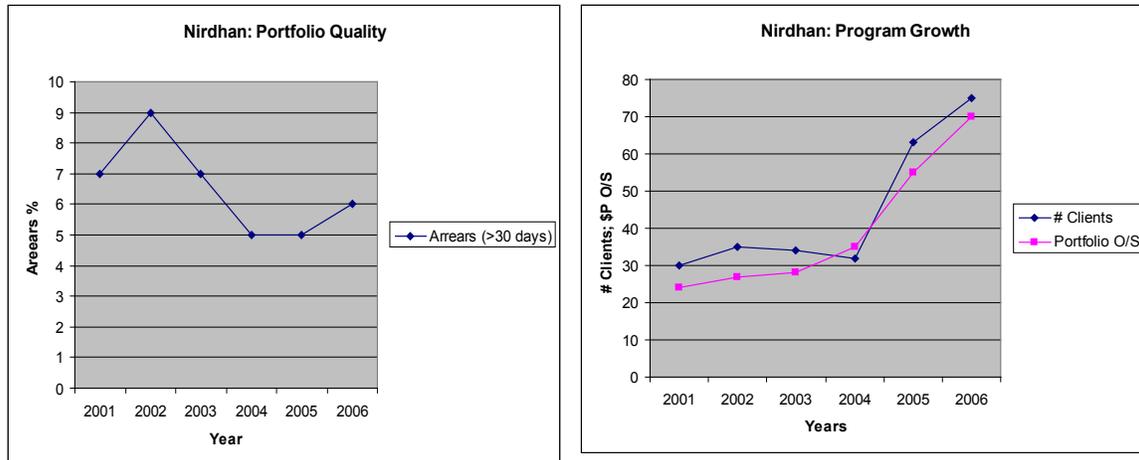
Source: Field interviews, Nepal, 2007.

Certain MFIs tried to solicit support from other political parties and made public the support that they received from the national government, actions that angered the Maoist insurgents. The institutions then realized that the best policy was to maintain neutrality among the parties to the conflict. The more they could assure the insurgents and the security forces that they did not support either one, the easier it was to operate.

4. **Leveraging community relationships and partnering with the private sector.** MFIs recognized that among the influential groups from which they could solicit support, the most influential were the beneficiary communities themselves. There were occasions, for example, where both the Maoists and the security forces acceded to their requests. Through many years of work on the ground, the MFIs had built cordial relationships with these communities. As illustrated in box 1, the institutions seized the opportunity to improve their working environment by leveraging these strong relationships. MFIs, for example, educated and encouraged their beneficiary communities to explain the benefits of microfinance and conduct negotiations with the conflicting parties. MFIs also looked

for partnership opportunities with the private sector to reduce operational risks. For example, some institutions partnered with commercial banks, while others partnered with insurance agencies, to reduce risks of fund transfers, looting and fraud.

Figure 1. Nirdhan’s Performance after Implementing Coping Mechanisms



Source: Nirdhan portfolio reports, 2001–2006.

Using such innovative measures, MFIs were able to increase their outreach, reduce loan delinquency and improve their sustainability. Figure I shows the improvements made by Nirdhan on both portfolio quality and growth (the graph covers a period during which Nirdhan was most impacted by the insurgency).

Several MFI innovations, such as implementing a staff code of conduct and improving information systems and transparency, remained relevant and useful even after the crisis. In most cases, these mechanisms were developed out of desperation through trial and error, rather than through systematic analysis and planning. Nonetheless, they proved useful in the long run.

Delivery of Enterprise Development & Social Services During the Insurgency

In addition to microfinance institutions, two NGOs that focused on livelihood and enterprise development services, and two that focused on social services (e.g., health, education and sanitation) were interviewed for this study. The goal of these interviews was to understand the obstacles they faced as a result of the insurgency and the coping strategies they adopted to deal with them. The Maoists had philosophical objections to microfinance, probably due to the market rate of interest charged by MFIs. In the case of NGOs, however, regardless of whether they provided business or social services, they were less opposed, although they frequently described NGO services as “imperialist activities designed to engage the poor in trivial activities.” The Maoists, were above, all interested in ensuring that NGOs did not represent government programs and that their staff did not work as government informants. They also sought to extort money from NGO programs and use them as a forum to promote their political agenda.

Among the income-generation (IG) and/or enterprise development NGOs operating in the two selected districts, Vijaya Development Resource Center (VDRC) and Multi-Dimensional Agriculture Development (MADE) were interviewed. Both NGOs delivered services related to water and sanitation, health, child labor, social mobilization and the environment, along with IG and livelihood services. Social Awareness Concerned Forum (SAC) and Oppressed Community Development Center (OCDC) were selected for interviews because of their focus on social services such as education, health and sanitation.

Table 3. Profile of NGOs Interviewed

	VDRC	MADE	SAC	OCDC
In operation since	1988	1996	2005	1998
Coverage	Nationwide	15 districts	3 districts	8 Districts
Services	Multisector with IG focus	Multisector with IG focus	Social services-focused	Education, human rights-focused
Sources of funds/ partners	National & international donors	National & international donors	PLAN, ITDG, Practical Action	World Education, PLAN

Source: Records provided by VDRC, MADE, SAC and OCDC, Nepal, 2007.

What did the Maoists do? While the extortion and harassment techniques used by the Maoists differed slightly from place to place due to the different views and general exposure of their local leadership, the general treatment of NGOs was similar across the board. In fact, actions directed at NGOs that delivered social and income-generation services were not very different from those directed at MFIs and included:

- requiring them to hire their cadres and nominate them for community or user-group leadership positions;

- using programs as a platform to broadcast their political ideology and program assets (e.g., vehicles) for personal and/or Maoist party purposes;
- in a few cases, forcefully closing down programs;
- levying a war tax and forced donations (10 to 40 percent of staff salary, plus a fixed amount per project);
- requiring NGOs to register with them and follow their rules (see box 2); and
- abducting NGO staff.

Although the Maoists considered NGOs to be the disguised apparatus of the rich, who used them to sustain feudalism, interviewees suggested that the rebels did not have much objection to programs related to health, education, drinking water and sanitation, or to livelihood and income generation. They also encouraged infrastructure projects, such as rural roads and electrification. They did not, however, like awareness-building programs, as they perceived such programs to conflict with their political ideology.

Other activities of the Maoists also affected business development and social service NGOs, just as they affected MFIs. Frequent “*Bandhs*,” travel bans, blockades, etc., limited the ability of all of these institutions to implement and monitor their programs.

What did government security forces do? The state security forces also created obstacles to NGO operations. In particular, they restricted the movement of construction materials and supplies to hilly areas under Maoist control. They also harassed project staff by asking for documents and requiring approvals before permitting them to move materials and supplies. As illustrated in box 3, certain cases have been documented in which security forces tortured NGO staff alleged to be aligned with the rebels.

Box 2. Rules Imposed on NGOs by Maoist Forces

1. Each and every development agency should register with the “people’s government” before starting operations and pay a registration fee of Rs 1000.
2. NGOs and development agencies should pay taxes to the “people’s government.”
3. Biographical data on all project staff must be submitted to the “people’s government.”
4. The “people’s government” will issue permits to implement projects. Such permits will be issued only in priority areas identified by this government.
5. Staff deployed by NGOs must be morally sound and strong in character.

Source: Field interviews and records provided by VDRC, MADE, SAC and ODCD, Nepal, 2007.

Box 3. ODCD Chairman Arrested and Tortured by Government Security Forces

Dil Bahadur Pariyar, the chairman of ODCD, was arrested in 2002 by security forces, together with 9 other farmers from his village. The men were hurled into a truck and taken to an army barrack, where they were severely tortured. The army suspected them of supporting the insurgents, but rather than interrogating them and corroborating this suspicion, it tried to force them to confess. One of the victims was the vice-chairman of the government's own apparatus—the Village Development Committee. Although Dil Bahadur was released after 24 hours of severe beating, 3 people taken that evening remain missing.

Source: Field interviews, Nepal, 2007.

Impact of the conflict. As the conflict intensified, NGO staff, programs and beneficiaries suffered in a number of ways. It was reported that communities did not want to interact with outsiders out of fear of being labeled either a rebel or a government informant. This trend reduced the participation of community members in development works by about 20 percent. Project targets and coverage accordingly shrunk, implementation was delayed, certain projects were only partially completed and others were discontinued altogether. In addition, certain projects had to be pulled out of remote areas in which the insurgency was raging and implemented elsewhere. Several NGOs reported that their overall annual achievement declined to about 65 percent of planned targets and that project costs went up by 15 percent.⁷

Coping mechanisms. NGOs designed coping mechanisms by taking into account the motives and modus operandi of both the Maoists and government security forces. The insurgents wanted to take advantage of the NGOs to enrich their war coffers and secure jobs and leadership positions for their cadres. They also wanted to eliminate the presence of the government in areas under Maoist control and establish their own rule. In addition, the Maoists thought that tiny development initiatives would only engage people in trivial activities, not transform their lives. The security forces were similarly suspicious that local NGOs, especially local staff, would cooperate with the Maoists. Because they were focused on defeating the Maoists by the use of force, these forces were not concerned about how their actions would hurt the communities in question. The NGOs used the following measures to address the concerns of the conflicting parties, as well as to establish their credibility and improve operational flexibility.

1. **Implementing public relations and transparency.** The NGOs quickly realized that they could not operate in the villages dominated by the Maoists without opening channels of communication with them and seeking public support from civil society, human rights groups and beneficiary communities. It was necessary to make the rebels and the communities understand the development value of NGO activities and earn their trust by fully disclosing their goals and funding sources. To achieve these aims, the NGOs developed a public relations and transparency strategy that featured the following elements:

- informing the conflicting parties and the community at large about NGO projects, budgets, expenses and outputs via local newspapers and/or public displays;
- organizing public audits of their programs;

⁷ These are average figures reported by the NGOs interviewed for this study.

- eliciting support from rebels by stressing ethical and community concerns;
- interacting with local leaders of rebel and government security forces, promptly answering their queries and supplying them program reports, as requested; and
- engaging civil society organizations and media by soliciting their support for NGO programs.

Putting the community in charge. It was noted that when NGO programs responded better to beneficiary needs and the communities supported them, the parties to the conflict were less likely to intervene in the programs.

Although the Maoists used terror tactics to increase their influence, they had political ambitions and thus did not want to alienate rural communities. Hence, the response of NGOs was to keep the communities front and center in their programs. The strategy employed by these institutions included the following elements:

- recruiting local staff under an inclusive hiring policy and selecting program beneficiaries so as to increase the participation of ethnic minorities and women;
- supplementing principal program activities with smaller projects (e.g., child-care centers, non-formal education, sanitation, etc.), as demanded by a community, even if such projects were less relevant to the annual plans of the NGOs;
- putting greater emphasis on programs that delivered “tangible” benefits, as opposed to awareness-raising activities, in response to the preference of local community members;
- engaging community members from project design through implementation to monitoring and evaluation, thus building community consensus before implementing any project;
- engaging existing local beneficiary institutions, such as youth clubs, village committees and women’s solidarity groups in program implementation;
- preparing communities to convince the rebels and security forces to allow them to participate in NGO projects; and
- inculcating a sense of program ownership in local communities.

One of the key elements of the NGOs’ community mobilization strategy was to emphasize ethnic and gender balance. Support from all sections of the community was needed to successfully implement programs, hence an all-inclusive policy was essential. If any section of the community felt excluded and complained to the Maoists, the program would be forced to shut down. In addition, the NGOs realized that social divisions, whether based on gender or

Box 4. Local Youth Club Successfully Implements an NGO Income-Generation Program

SAC/Nepal wanted to implement an income-generation program for households in Kohalpur headed by single women whose male heads had been killed in the conflict. Since the area was deeply affected by the conflict and both the Maoists and the security forces would likely have intervened in the program, thus making it impossible to implement, SAC/Nepal decided to engage a local youth club for the project. The youth club was able to implement the program undisturbed by either of the warring parties.

Source: Field interviews, Nepal, 2007.

ethnicity, could easily trigger frictions in a conflicting society and lead to service delivery disruptions.

2. **Maintaining neutrality.** One of the reasons both parties to the conflict intimidated and harassed NGOs was because they suspected them of working for, or at least supporting, their opponent. They thus asked the NGOs for detailed information, required advance permits to permit the movement of project materials and interrogated project staff with often irrelevant questions. The NGOs handled this situation by:
 - making clear through publications, dialogue, etc., that they were not-for-profit and purely non-political programs; and
 - instructing staff not to provide any information to the conflicting parties about one another, despite intimidation or incentives to do so.

3. **Implementing staff codes of conduct and staff support programs.** As the conflict intensified, soldiers disguised themselves as Maoists and extracted information from villagers and the Maoists used similar tactics. These tactics led villagers to avoid interacting with strangers. Mutual trust and respect among people eroded. Under these circumstances, it was imperative that NGO staff became highly sensitive to the language they used when speaking with villagers. Since one small mistake by an NGO staff member could sow mistrust and lead to disastrous consequences, the NGOs either developed their own codes of conduct (see box 5) or adapted the code of conduct that was developed by international NGOs working in Nepal. In addition to codes of conduct, simple lifestyle rules were emphasized, such as moderate dress, the use of bicycles rather than motorbikes, and financial discipline.

Working in such a tense environment was very stressful for NGO staff. One small misstep could result in being abducted, beaten up, or fined. As a result, NGOs implemented a number of morale-boosting activities for staff, including training in communication and negotiation skills, staff security plans and direct assistance in cases where staffs were personally harmed.

Both MFIs and NGOs leveraged cordial relationships with communities to protect their interests, but in different ways. The MFIs prepared communities to explain to the conflicting parties how important MFI programs were for them and why it was necessary to allow MFIs to continue their programs. NGOs, on the other hand, identified communities as their main stakeholders and included them in the design and implementation of their projects. Government units delivering social services had the hardest time achieving their targets because the Maoists were totally opposed to the government's presence in areas under Maoist control. Interviews with two such government units (the District Health Office and the District Education Office, both from Bako) revealed that even

Box 5. Key Features of the Internal Code of Conduct Used by NGOs in Nepal

1. Be neutral with respect to conflicting parties and other political forces.
2. Be inclusive when selecting target beneficiaries and/or staff.
3. Ensure that staff attire and lifestyle is simple and austere and reflects the lifestyle of beneficiaries.
4. Avoid smoking and drinking in public.
5. Encourage amiable relations with community members, rebel cadres and others.
6. Make decisions in the interest of beneficiaries and community consensus.
7. Maintain up-to-date knowledge on the project, its objectives and implementation procedures.

Source: Field interviews and records provided by VDRC, MADE, SAC and ODCD, Nepal, 2007.

national government officers at the district level paid the Maoists for security and that they maintained regular communication with the rebels. These tactics were the only way to achieve anything in areas under Maoist control.

Delivery of Essential Commodities During the Insurgency

Interviews with ten shopkeepers (five from each district) and 60 community members (30 from each district) revealed that a regular supply of consumer commodities was also interrupted during the insurgency. Both the Maoists and the security forces were responsible for these interruptions. Although the Maoists did not ban the supply of any commodity, their disruptive activities (e.g., blockades, intimidation of private business owners, extortion and armed invasion of towns) did cut off or reduce the supply of essential consumer products, including life-saving drugs. Larger businesses were particularly targeted by the Maoists for extortion and intimidation.

In response to this harassment, the business sector, along with private boarding schools, came up with several coping strategies. These strategies included paying for protection, increasing wages and improving working conditions, outsourcing work to local people and small businesses, laying off excess workers through voluntary retirement schemes, engaging in negotiations with a Maoist-affiliated workers' union and getting involved in peace building.⁸

The Nepalese security forces, however, banned the bulk supply of certain commodities to hilly regions of the country, especially commodities that could be used by the insurgents. Such items included pressure cookers, sanitation fittings (e.g., pipe sockets), green combat shoes, backpacks, instant noodles, biscuits, cell phones and matches. The supply of food to districts that had a perpetual food deficit via market channels was thus severely hindered due to both fear of the Maoists and the restrictions imposed by district administrations.⁹

Private businesses such as kitchenware and utensil shops, hardware stores, shoe suppliers and grocery stores lost as much as 40 percent of their sales due to these bans. People who defied the ban were typically arrested and beaten up by the security forces. Under pressure from communities and private businesses, however, the government put a system into place that permitted the supply of these items to hilly regions only after approval by the local administration.

⁸ Ameet Dhakal and Jhalak Subedi, *Local Business, Local Peace: The Peacebuilding Potential of the Domestic Private Sector* (London: Peacebuilding NGO International Alert, UK, 2006).

⁹ Shiva Sharma and Ram Krishna Sharma, "A Study on Conflict-induced Food Insecurity in Nepal," report prepared for the World Food Program, National Labor Academy, Nepal, 2002.

Conclusions and Lessons Learned

The survey suggests that the delivery of basic services (e.g., primary education, income generation, microfinance, drinking water, sanitation, primary health and public safety) can be severely interrupted by prolonged political conflict or civil war. However, service providers can maintain delivery of these services, albeit occasionally at a reduced level, by developing specific coping strategies. Based on the decade-long experience of Nepal, this case study suggests that local actors can ensure regular, and even expanded, supply of these services in conflict situations by combining different strategies and mobilizing a range of stakeholders, as detailed below.

1. Introduce practical innovations in services and delivery procedures. MFIs in Nepal went a long way toward modifying their products and services, as well as their operating procedures, to respond to the challenges posed by the insurgency. They also made improvements in their human resource management, including the promotion of gender and ethnic diversification, incentive systems and staff training. These changes, directed at the internal environment of the institutions, significantly reduced their risks, improved their flexibility and enabled them to grow once again. NGOs in the country, on the other hand, focused more on operating systems and human resource management, and less on changes to their products and services.

Both the MFIs and the NGOs took into account the basic interests and operating procedures of the conflicting parties. For example, the rebels wanted to minimize the presence of the Nepalese government in their areas, hence the service providers reduced their interaction with government agencies. Similarly, government security forces wanted to ensure that the NGOs did not assist the insurgents, hence the service providers enforced a policy of neutrality. The experience of the two types of institutions clearly shows that creative innovations in products, services and operating procedures should be a critical part of any strategy that seeks to ensure the smooth delivery of essential services under conditions of fragility. Other innovations that were not tried in Nepal, but have potential, include having social service providers use MFI delivery systems and using cell phone and mobile banking for financial services.

2. Mobilize the community. When the government's presence in rural Nepal broke down, the vacuum was immediately filled by the Maoists, not local community leaders, as would have been the case during a crisis created by a natural disaster. However, as the delivery of essential services started to decline, communities emerged as a local force and began to negotiate with the conflicting parties to prevent the interruption of services. Seeing the effectiveness of communities in minimizing political interference in service delivery, service providers (i.e., MFIs and NGOs) started to involve them more prominently in their activities.

MFIs leveraged their cordial relationships with communities, for example, to advocate for their programs. They also used communities in negotiations with the Maoists when MFI staff members were abducted or MFI assets were seized. NGOs in Nepal went even further—they recognized communities as the main stakeholders in their programs and engaged them in program implementation, starting from selection and design of activities to their implementation and monitoring. Active community participation in NGO programs was indeed a major factor in making it possible to deliver essential services in rural Nepal during the insurgency.

While community mobilization is a good approach in any community development effort, it proved even more useful in the conflict in Nepal. Because of their political goals, the conflicting parties did not want to irritate local communities, hence they would listen to genuine arguments and requests made by them.

It became clear that the Maoists placed high importance on public rapport, community relations and political credibility to serve their political goals. Government security forces, on the other hand, found it was not always easy to ignore reasonable requests made by the people whom they were supposed to protect. In fact, the Maoists as well as government security forces listened to local communities more than they listened to NGOs, MFIs or private businesses.

It should be noted that local communities may not be as effective if the parties to a conflict are apolitical and/or fanatical, as is the case in Afghanistan and Iraq. In such situations, it is not advisable to place great emphasis on community mobilization. It should also be noted that Nepal also has a long cultural history of self-help. Village roads, irrigation systems and educational institutions that have been successfully built and maintained by communities are well documented.¹⁰ In view of this tradition, one approach to ensuring the delivery of essential services during a crisis would be to support communities with financial resources and technical ideas and let them organize the delivery of services themselves. A program called “build your own village” presently being funded by the Government of Nepal is a good example of this type of approach.¹¹

3. Use local NGOs for program delivery. As the insurgency intensified, several international NGOs working in Nepal partnered with community-level NGOs to deliver services. These community-based organizations and their local staffs were savvier in dealing with local Maoist leaders. They proved not only flexible and adaptable, but also more knowledgeable about local needs and community priorities. Their only limitation was lack of international exposure and access to cutting-edge concepts, a shortcoming that was balanced by the expertise of international NGOs that partnered with them. Local NGOs, however, did not fair well with security forces because the latter usually saw locals as Maoist supporters. Nonetheless, these NGOs played a critical role in delivering essential services during the insurgency.

4. Work with the national government to create and improve an enabling environment for service delivery. From the accounts of respondents interviewed for this study it became clear that the Government of Nepal was not truly concerned by the interruption and/or discontinuation of basic public services. Government security forces clearly relied too heavily on the use of force to suppress the insurgency and did not have a strategy to deliver services and win the hearts and minds of the people. Villagers suffered not only at the hands of the Maoists, but also at the hands of government security forces. District-level government units did make efforts to deliver services according to their mandates, but became the first target of the insurgents.

Because of the nature of the conflict, direct government involvement in the delivery of basic services is not advised. In addition, government agencies do not have the same flexibility that NGOs, MFIs and the private sector have to operate in a war zone. However, if the Nepalese government had committed itself to ensuring the smooth delivery of public services to local communities, they could have assisted other players enormously by creating a more enabling environment through the adoption of the following measures:

- establishing a streamlined process for creating community-level NGOs;
- waving the need for permits, or otherwise making it easier and cheaper to form local NGOs;
- redirecting their resources to local NGOs and private businesses through grants and contracts so as to deliver essential services;

¹⁰ S.E. Howarth and M.P. Pant, “Community Managed Irrigation in Eastern Nepal,” *Irrigation and Drainage Systems* 1, no. 3 (October 1987) [Netherlands: Springer].

¹¹ Vijay Kunwar, “In Defense of the Finance Minister,” *Nepali Times*, July 25, 2003; and Dhawal Rana, “Think Nationally, Act Locally,” *Nepali Times*, December 26, 2002.

- facilitating linkages between MFIs, banks, the private sector, etc., in order to forge partnerships to deliver essential services; and
- assisting MFIs to introduce new services to address community health, education and sanitation needs (e.g., education loans, health insurance, housing and latrine loans, bio-gas loans, etc.).

5. Partner with the private sector and use market-based solutions. The study did not find examples of MFIs and NGOs that partnered with the private sector, except for larger businesses that outsourced work to smaller businesses and MFIs that utilized the services of insurance companies and commercial banks to reduce their cash flow risk. Nor did the study find good examples of existing private businesses that capitalized on new market opportunities created by interruptions in existing channels, networks and the flow of goods and services.

However, a number of entrepreneurial people from local communities in Nepal did create local-level NGOs to deliver essential services that national and international NGOs were having difficulty delivering. Although these NGOs were registered as not-for-profit entities, they were essentially acting on new market opportunities and doing business. New opportunities surfaced as a result of the conflict and a new breed of entrepreneurs emerged in the form of local NGOs that capitalized on these opportunities, leading to significant improvement in the delivery of these services.

Existing private businesses also took advantage of new opportunities, but mostly within their traditional business sub-sectors. These businesses were accordingly not as innovative nor as prone to take risks, but there is no reason why they could not be encouraged to enter service delivery businesses, provided these were profitable.

