

## **Nepal: Selected Issues and Statistical Appendix**

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NEPAL

**Selected Issues and Statistical Appendix**

Prepared by a staff team consisting of Wafa Abdelati, Joong Shik Lee (All APD),  
Petya Koeva (EU1), and Jesmin Rahman (PDR)

Approved by Asia and Pacific Department

August 21, 2002

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## OVERVIEW

**Deep-rooted and pervasive poverty is an overriding concern** of policy makers in Nepal. In the forthcoming Poverty Reduction Strategy Paper, the authorities argue that both growth enhancement (especially of agriculture) and better social service delivery to the poor are important goals of their reform efforts.

**The authorities have taken a number of initiatives to achieve these goals.** To enhance growth, the authorities stress that better availability of agricultural inputs is critical and that export promotion is also key to their strategy. To improve social service delivery, the authorities have embarked on fiscal decentralization and civil service reform. Finally, the authorities are promoting microfinance to help the poor gain access to credit as a key step towards poverty reduction.

**Chapters in this volume summarize staff work on these issues.** Many of these issues are structural but have substantial macro-financial relevance in the medium run.

**Chapter I reviews agricultural productivity in Nepal and examines its links at the regional and aggregate levels to the amounts of available inputs** such as chemical fertilizers, irrigation water, and improved seeds, as well as rainfall, rural credit and foreign aid. The chapter highlights factors that are statistically correlated with agricultural productivity and, as importantly, those that are not.

**Chapter II examines causes for the recent export slowdown.** While external reasons including the global economic slowdown and policy shifts of countries that import Nepalese goods are important factors, the analysis suggests that high costs associated with poor infrastructure and the landlocked location may be contributing significantly to deteriorating performance—especially when external demand is weak.

**Chapter III focuses on fiscal decentralization.** With well-managed decentralization, local governments can deliver services that better meet the needs of local residents. The chapter reviews available information on local governments and endorses the authorities' cautious devolution strategy since elements required for successful decentralization—e.g., administrative capacity and adequate monitoring at local levels—are not yet in place.

**Chapter IV describes the bottom-heavy civil service structure** and summarizes policies being implemented to reduce the overemployed lower grades as well as measures to improve performance incentives of higher level employees.

**Chapter V discusses microfinance.** Although efforts have been made for decades, microfinance in Nepal has limited coverage and targeting, and virtually no microfinancial institution is commercially sustainable. The chapter reviews the authorities' efforts so far, and discusses steps to improve Nepal's microfinance sector based on lessons learnt from recent experience in the rest of the world.

## I. THE DETERMINANTS OF AGRICULTURAL PRODUCTIVITY<sup>1</sup>

### A. Introduction

1. **Agriculture is the backbone of the Nepalese economy.** The share of agriculture as a percent of GDP is close to 40 percent, and about 80 percent of the working population is employed in the sector. The key crops are paddy, wheat and maize, accounting for more than one third of overall agricultural production.
2. **This paper analyzes the determinants of agricultural productivity in Nepal.**<sup>2</sup> In particular, the study examines the relationship between the productivity (yield) of three major crops (paddy, wheat, and maize) and agricultural inputs (chemical fertilizers, improved seeds, irrigation, agricultural credit and foreign aid disbursements, and rainfall).<sup>3</sup>
3. **The main findings of the paper can be summarized as follows:**
  - Weather remains an important determinant of agricultural productivity.
  - The use of chemical fertilizers has broadly contributed to the rise in paddy and wheat productivity; in contrast, maize productivity has been mostly unaffected.
  - The use of improved seeds has not been associated with higher yields of paddy and maize crops, although the yield of wheat crops has been positively affected.
  - Generally, the improved access to irrigation facilities has not been linked to higher crop productivity. Its beneficial effect is observed only in some regions.
  - Higher agricultural credit and foreign aid disbursements are associated with better crop productivity.

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<sup>1</sup> Prepared by Petya Koeva (EU1).

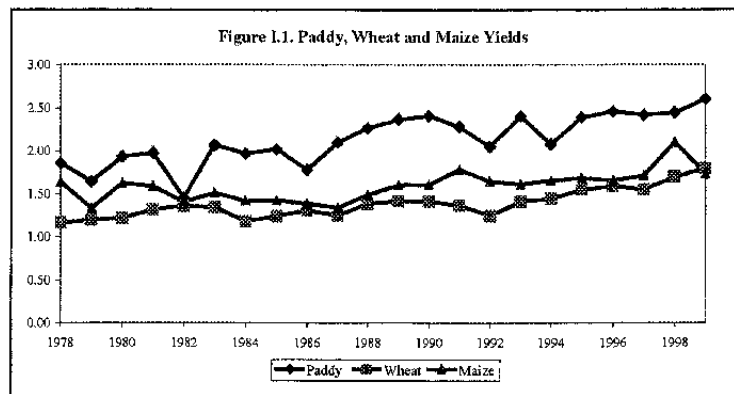
<sup>2</sup> Another important and interesting question, which is beyond the scope of this paper, is whether agricultural productivity in Nepal is low compared to other developing countries and (if so) what factors can explain these productivity differences. Although some data on crop yields across countries are available, answering the above question is difficult, since the crop yields may not be comparable across countries. For example, certain paddy varieties that are successfully used in other countries may not be viable in Nepal due to differences in local climate and topography.

<sup>3</sup> The crop yield is defined as output (in metric tons) divided by area (in hectares).

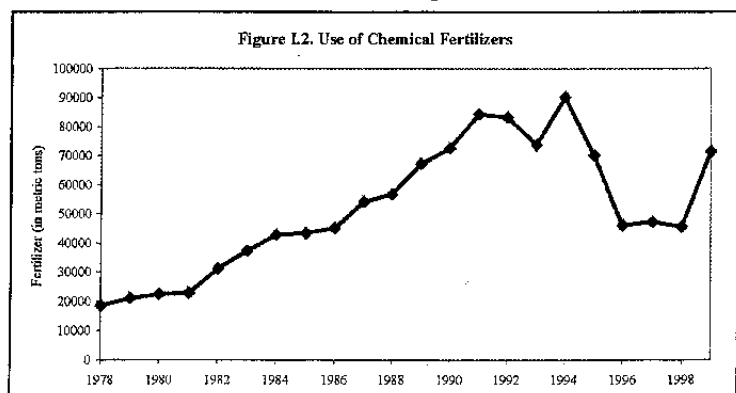
4. **The remaining part of the paper is organized as follows.** Section B describes the changes in crop productivity over time and presents some background information in the areas of fertilizer, improved seeds, irrigation and foreign aid policies. Section C introduces the data and variable definitions used in the analysis. Section D discusses the main findings of the paper. Section E concludes.

## B. Background

5. **The productivity of paddy, wheat, and maize crops generally increased, although slowly, during the past decades** (Figure I.1). Most pronounced was the increase in paddy yields—the mean yield between 1978/79 and 1988/89 was 1.91, i.e., over 0.50 metric tons per hectare less than the one between 1989/90 and 1999/2000. The productivity of wheat crops rose steadily in the 1990s, with mean yields during the two subperiods (1978/79–1988/89 and 1989/90–1999/2000) of 1.27 and 1.50 metric tons per hectare, respectively. The productivity of maize crops increased modestly during the sample period, as the maize yield in 1999/2000 was only 0.09 metric tons per hectare higher than in 1978/79.



6. **Following a continuous rise in the consumption of chemical fertilizers, the fertilizer market collapsed in the mid-1990s and was deregulated in late 1997.** The institutional distribution and sale of inorganic (chemical) fertilizers in Nepal started in the late 1960s.<sup>4</sup> The consumption of chemical fertilizers increased dramatically between 1978/79 and 1994/95, but dropped significantly in the next two years (Figure I.2). This collapse of consumption, as well as problems with the distribution and the efficient use of the fertilizers, prompted the deregulation of the market in November 1997, when the Agriculture Inputs Corporation (AIC) lost its monopoly over the imports and distribution of

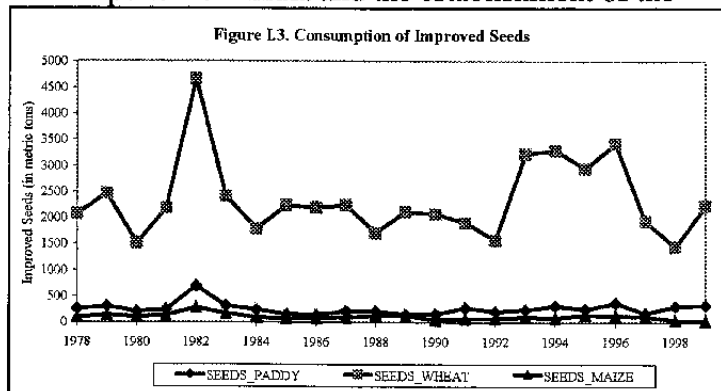


<sup>4</sup> Since the country does not produce any inorganic fertilizers, the agricultural community depends on their purchase from other countries imports, often financed by foreign grants.

fertilizers in Nepal. Under the new institutional setup, the Fertilizer Unit of the Ministry of Agriculture was given the mandate to oversee the distribution of chemical fertilizers and monitor their quality.

7. **The consumption of all types of improved seeds fluctuated during the past several decades.** The supply of improved seeds in the formal sector did not start until the 1970s, with the start of improved seed imports from India and the establishment of the

Hetauda Seed Processing Plant with the cooperation of the Food and Agriculture Organization of the United Nations (FAO). However, the consumption of wheat seeds, which comprises more than 80 percent of the total amount of improved seeds used each year, does not show an upward trend (Figure I.3). The consumption of maize and paddy seeds has also not



increased significantly during the period from 1978/79 to 1999/2000.

8. **The development and maintenance of irrigation facilities have proceeded for many decades, including with the support of foreign donors.**<sup>5</sup> After a period of limited progress, government investment in large-scale irrigation facilities rose between 1970 and 1975, as borrowing from international institutions increased. During this period, the focus was on the construction of new facilities, but not on their subsequent maintenance. To address the maintenance problem, a number of management-oriented projects were initiated in the 1980s, with the assistance of international organizations.<sup>6</sup> Most ongoing irrigation projects are multi-stage initiatives, which were started decades ago. The financing of each stage often comes from different sources, although the involvement of international institutions such as the World Bank and AsDB is prevalent.

<sup>5</sup> Most of the information presented in this section comes from the website of the Department of Irrigation (<http://www.doi.gov.np/doi>). Unfortunately, data on the *stock* of irrigation facilities are unavailable. Government publications contain information on the yearly *additions* to the total irrigated area. Since little is known about the composition of the irrigation stock and the depreciation rates of the different facilities, the construction of capital stock series is not attempted. Instead, the empirical analysis uses the additional irrigated facilities as an explanatory variable.

<sup>6</sup> Examples of such projects are: USAID Irrigation Management Project (1985), World Bank Irrigation Line of Credit (1988), AsDB Irrigation Sector Project (1988), UNDP/World Bank/AsDB Irrigation Sector Support Project (1989).

9. **The agricultural sector is one of the large recipients of foreign grants and loans in Nepal.** For example, approximately one fifth of the total foreign aid disbursements in recent years were designated to agriculture and irrigation.<sup>7</sup> In particular, foreign grants and loans frequently finance the development and maintenance of irrigation facilities, as well as the purchase of improved seeds.

### C. Data Source and Sample Description

10. **The data used in the empirical analysis were derived from various issues of the *Statistical Year Book of Nepal*.** The crop yields were computed using aggregate and regional data on the estimated area and production volume, reported in the yearbook. The annual series for the consumption of chemical fertilizers and improved seeds, agricultural credit and foreign aid disbursements, and annual rainfall were available in the same publication.<sup>8</sup> The descriptive statistics of the main variables are presented in the appendix.

11. **Two samples—aggregate and regional—were constructed and used in the empirical analysis.** The aggregate sample contains 22 observations, covering the period from 1978/79 until 1999/2000. The regional sample includes 110 observations, with 22 data points for each of the five development regions (Eastern, Central, Western, Mid-western, and Far-western).

### D. Results<sup>9</sup>

12. **This section presents the estimation results, obtained from different samples and model specifications (Tables I.1–I.4).** In particular, the discussion focuses on the effect of chemical fertilizers, improved seeds, irrigation, agricultural credit, foreign aid, rainfall, and regional factors on agricultural yields.

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<sup>7</sup> Unfortunately, the complete series for the disbursements to agriculture between 1978/79-1999/2000 are not available. The *Economic Survey FY 2000/01* contains this information only from 1984/85 onward. The *Statistical Year Book of Nepal* does not report the sectoral breakdown of foreign aid disbursements. Therefore, the empirical analysis uses the available data on total foreign aid disbursements.

<sup>8</sup> The annual rainfall data were reported by 21 meteorological stations across the country. After identifying the location of each station, the mean precipitation for each development region was computed and used in the empirical analysis.

<sup>9</sup> Details about the estimation and specification of the regression model can be found in the appendix.



Table I.1. The Determinants of Crop Yields  
(Aggregate data)

	Paddy			Wheat			Maize		
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
<i>Fertilizer</i>	0.009 (0.001) ***	0.005 (0.002) **	0.003 (0.002) *	0.004 (0.001) ***	0.000 (0.001)	0.000 (0.002)	0.002 (0.001)	0.000 (0.002)	0.000 (0.002)
<i>Rainfall</i>	1.034 (0.168) ***	0.650 (0.196) ***	0.739 (0.119) ***	0.583 (0.150) ***	0.214 (0.109) *	0.384 (0.170) **	0.123 (0.131)	-0.127 (0.152)	-0.060 (0.140)
<i>Irrigation</i>	0.005 (0.003)	0.001 (0.003)	0.001 (0.003)	0.002 (0.002)	-0.001 (0.002)	0.000 (0.003)	0.003 (0.002)	0.000 (0.003)	0.001 (0.003)
<i>Seeds</i>	-0.118 (0.370)	-0.498 (0.297)	-0.282 (0.282)	0.062 (0.028) **	0.031 (0.023)	0.047 (0.027) *	-0.218 (0.456)	-0.483 (0.459)	-0.603 (0.443)
<i>Agricultural credit</i>	-	0.104 (0.031) ***	-	-	0.112 (0.018) ***	-	-	0.059 (0.023) **	-
<i>Foreign aid</i>	-	-	0.060 (0.012) ***	-	-	0.041 (0.013) ***	-	-	0.021 (0.011) *
<i>Constant</i>	-0.271 (0.363)	0.561 (0.425)	0.053 (0.269)	-0.056 (0.257)	0.691 (0.226) ***	0.156 (0.329)	1.203 (0.326) ***	1.700 (0.358) ***	1.504 (0.345) ***
Observations	22	22	22	22	22	22	22	22	22
R-squared	0.76	0.83	0.87	0.53	0.83	0.70	0.27	0.41	0.34

Notes : 1. Parameters estimated using ordinary least squares. 2. Robust standard errors are shown in parentheses. 3. Significance levels of 1 percent, 5 percent and 10 percent are denoted by (\*\*\*), (\*\*) and (\*), respectively. 4. Agricultural credit and foreign aid are measured in billions of constant Nrs (1995/96 = 100). 5. Rainfall is measured in thousands of mm. 6. Fertilizer and seed inputs are measured in thousands of metric tons. 7. Irrigation area is measured in thousands of hectares.

Table I.2. The Determinants of Paddy Yields

(Regional data)

	(1)	(2)	(3)	(4)	(5)
<i>Irrigation</i>	0.008 (0.009)	-0.011 (0.009)	0.001 (0.007)	-0.006 (0.005)	-0.007 (0.004)
<i>Rainfall</i>	0.416 (0.110) ***	0.454 -0.108 ***	0.491 (0.084) ***	0.303 (0.090) **	0.203 (0.090) *
<i>Seeds</i>	-	-	-0.314 (0.187)	-0.421 (0.177) *	-0.767 (0.139) ***
<i>Fertilizer</i>	-	-	0.008 (0.001) ***	0.000 (0.001)	0.002 (0.001)
<i>Agricultural credit</i>	-	-	-	-	0.176 (0.024) ***
<i>Foreign aid</i>	-	-	-	0.086 (0.010) ***	-
<i>Central region</i>	0.173 (0.097) *	0.054 (0.151)	0.153 (0.009) ***	0.172 (0.011) ***	0.188 (0.014) ***
<i>Western region</i>	-0.319 (0.122) **	-0.547 (0.151) ***	-0.391 (0.044) ***	-0.289 (0.053) ***	-0.221 (0.061) **
<i>Mid-western region</i>	0.004 (0.107)	-0.284 (0.130) **	-0.032 (0.041)	-0.079 (0.027) **	-0.081 (0.026) **
<i>Far-western region</i>	0.018 (0.118)	-0.245 (0.166)	-0.008 (0.051)	-0.082 (0.037) *	-0.099 (0.031) **
<i>Irrigation*Central region</i>	-	0.014 (0.014)	-	-	-
<i>Irrigation*Western region</i>	-	0.032 (0.018) *	-	-	-
<i>Irrigation*Mid-western region</i>	-	0.095 (0.029) ***	-	-	-
<i>Irrigation*Far-western region</i>	-	0.088 (0.044) **	-	-	-
<i>Constant</i>	1.325 (0.205) ***	1.403 (0.210) ***	0.905 (0.188) ***	0.828 (0.195) **	1.495 (0.184) ***
Observations	110	110	110	110	110
R-squared	0.20	0.29	0.47	0.67	0.68

Notes: 1. Standard errors are adjusted for clustering by region. 2. Measurement units are described in Table A1.

Table I.3. The Determinants of Wheat Yields  
(Regional data)

	(1)	(2)	(3)	(4)	(5)
<i>Irrigation</i>	0.005 (0.006)	-0.002 (0.007)	0.002 (0.003)	-0.003 (0.001) *	-0.003 (0.002)
<i>Rainfall</i>	0.223 (0.067) ***	0.222 (0.069) ***	0.295 (0.064) **	0.102 (0.024) **	0.175 (0.065) *
<i>Seeds</i>	-	-	0.045 (0.017) *	0.019 (0.014)	0.030 (0.015)
<i>Fertilizer</i>	-	-	0.003 0.000 ***	-0.001 (0.001)	-0.001 (0.001)
<i>Agricultural credit</i>	-	-	-	0.128 (0.016) ***	-
<i>Foreign aid</i>	-	-	-	-	0.054 (0.007) ***
<i>Central region</i>	0.035 (0.048)	-0.02 (0.068)	0.019 (0.010)	0.042 (0.004) ***	0.032 (0.009) **
<i>Western region</i>	-0.19 (0.065) ***	-0.278 (0.089) ***	-0.25 (0.043) ***	-0.136 (0.017) ***	-0.183 (0.042) **
<i>Mid-western region</i>	-0.153 (0.053) ***	-0.281 (0.064) ***	-0.172 (0.020) ***	-0.205 (0.009) ***	-0.2 (0.011) ***
<i>Far-western region</i>	-0.182 (0.061) ***	-0.236 (0.093) **	-0.191 (0.024) ***	-0.252 (0.009) ***	-0.236 (0.018) ***
<i>Irrigation*Central region</i>	-	0.007 (0.010)	-	-	-
<i>Irrigation*Western region</i>	-	0.015 (0.016)	-	-	-
<i>Irrigation*Mid-western region</i>	-	0.045 (0.018) **	-	-	-
<i>Irrigation*Far-western region</i>	-	0.006 (0.024)	-	-	-
<i>Constant</i>	1.022 (0.114) ***	1.081 (0.125) ***	0.645 (0.124) ***	0.998 (0.066) ***	0.613 (0.124) ***
Observations	110	110	110	110	110
R-squared	0.37	0.41	0.50	0.82	0.71

Notes: 1. Standard errors are adjusted for clustering by region. 2. Measurement units are described in Table A1.

Table I.4. The Determinants of Maize Yields  
(Regional data)

	(1)	(2)	(3)	(4)	(5)
<i>Irrigation</i>	0.007 (0.004) *	-0.004 (0.006)	0.005 (0.005)	0.002 (0.004)	0.002 (0.005)
<i>Rainfall</i>	0.013 (0.066)	0.008 (0.064)	0.026 (0.062)	-0.056 (0.041)	-0.035 (0.072)
<i>Seeds</i>	-	-	-0.366 (0.282)	-0.262 (0.306)	-0.487 (0.277)
<i>Fertilizer</i>	-	-	0.002 0.000 ***	0.000 (0.001)	0.000 (0.001)
<i>Agricultural credit</i>	-	-	-	0.064 (0.022) **	-
<i>Foreign aid</i>	-	-	-	-	0.026 (0.012) *
<i>Central region</i>	0.119 (0.055) **	0.029 (0.093)	0.114 (0.007) ***	0.123 (0.005) ***	0.120 (0.007) ***
<i>Western region</i>	-0.064 (0.069)	-0.243 (0.105) **	-0.08 (0.032) *	-0.034 (0.022)	-0.046 (0.036)
<i>Mid-western region</i>	0.000 (0.066)	-0.136 (0.095)	-0.013 (0.032)	-0.03 (0.025)	-0.028 (0.030)
<i>Far-western region</i>	-0.012 (0.077)	-0.099 (0.101)	-0.023 (0.039)	-0.052 (0.030)	-0.047 (0.039)
<i>Irrigation*Central region</i>	-	0.012 (0.008)	-	-	-
<i>Irrigation*Western region</i>	-	0.033 (0.010) ***	-	-	-
<i>Irrigation*Mid-western region</i>	-	0.038 (0.013) ***	-	-	-
<i>Irrigation*Far-western region</i>	-	0.012 (0.016)	-	-	-
<i>Constant</i>	1.491 (0.136) ***	1.585 (0.145) ***	1.403 (0.156) ***	1.509 (0.098) ***	1.396 (0.154) ***
Observations	110	110	110	110	110
R-squared	0.15	0.22	0.26	0.36	0.32

Notes: 1. Standard errors are adjusted for clustering by region. 2. Measurement units are described in Table A1.

## Rainfall

13. **Rainfall remains an important determinant of agricultural productivity in Nepal.** The importance of good monsoon rains for paddy and wheat yields is illustrated by the sign, size and significance of the variable *Rainfall* in Tables I.1–I.3. The magnitude of the coefficient in Table I.1, Column (3), for example, implies that an additional 100 mm of rainfall is associated with an increase in the paddy yield by 0.074 metric tons per hectare. The insignificant effect of *Rainfall* in the maize yield regressions is surprising, given that the bulk of maize production in Nepal is rainfed.

## Chemical Fertilizers

14. **The use of chemical fertilizers has broadly contributed to the rise in paddy and wheat productivity, while maize productivity has been mostly unaffected.** In the paddy equations, the magnitude of the positive effect is such that a ten-thousand-ton increase in fertilizer use is associated with a productivity rise in paddy production in the range of 0.03–0.09 metric tons per hectare (Table I.1, Columns (1)–(3)).<sup>10</sup> In the wheat yield equations, the positive effect of fertilizer use is statistically significant only in some specifications. In the maize equations, the coefficients of the variable *Fertilizer* are insignificant in all estimations that use aggregate data. Nevertheless, the regional sample regressions indicate that the yield of maize crops in the Central region have benefited from the increase in fertilizer use (Table I.4).

15. **The established differential impact of the use of chemical fertilizers on crop productivity is not surprising.** Unlike paddy and wheat, only a small proportion of maize growers use fertilizers in Nepal. For example, only 18 percent of the total maize area was fertilized in 1991/92. In contrast, 46 percent of the paddy area was fertilized during the same year.<sup>11</sup> Moreover, chemical fertilizers in maize production are likely to be more popular in some regions, but not in others. The varying effect of fertilizer use on the productivity of maize production across regions is recovered using the regional data.

## Improved Seeds

16. **The use of improved seeds is associated with higher yields of wheat crops only.** In particular, the coefficient of *Seeds* suggests that a two-hundred-ton increase in the use of improved seeds is linked to a rise in wheat productivity by 0.01 metric tons per hectare

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<sup>10</sup> Not surprisingly, the magnitude of the coefficient on *Fertilizer* is lower in the regressions that include *Agricultural credit* and *Foreign aid* as regressors. This can be explained by the fact that the purchase and subsequent use of chemical fertilizers are largely determined by the availability of foreign grants used to import the main inorganic nutrients—nitrogen, phosphorous, and potash.

<sup>11</sup> See <http://www.panasia.org.sg/nepalnet/agriculture/pest.htm>.

(Table I.1, Column (6)). In the paddy and maize equations, however, the variable *Seeds* has the wrong sign in all specifications, although these coefficients are not statistically significant.<sup>12</sup> The finding that improved seeds increase the yield of wheat crops is consistent with the fact that the use of improved seeds is most common in growing wheat crops, with over 80 percent of all improved seeds going toward the production of wheat (Annex Table I.1).

### **Irrigation**

17. **The beneficial effect of improved access to irrigation facilities is found in several specifications only.** Using the aggregate sample, the effect of irrigation is found to be statistically insignificant for all crop yields. In almost all cases, the coefficient of *Irrigation* is insignificant in the regional regressions as well. One of the exceptions is the positive and significant effect of irrigation on maize productivity (Table I.4, Column (1)), which implies that a one-thousand-hectare increase in irrigated land is associated with an increase in the crop yield by 0.007 metric tons per hectare. The possibility of a differential (regional) effect of irrigation on crop yields is explored by including region-irrigation interaction terms in the regressions for each crop (Tables I.2, I.3 and I.4, Column (2)). The results suggest that all types of crops in the Mid-western region have benefited from the expansion of irrigation facilities (compared to those of the reference category *Eastern region*). In addition, the positive impact of irrigation on paddy productivity is stronger in the Far-western and Western regions.

### **Agricultural Credit**

18. **Access to agricultural credit is linked to higher agricultural yields for all crops.**<sup>13</sup> The coefficient of the credit variable is positive and statistically significant in all specifications in Table I.1. In the paddy and wheat equations, for example, the size of the coefficient on *Agricultural credit* implies that an additional Nr. 100 million (1995/96 = 100) is related to an increase in paddy (or wheat) productivity by 0.01 metric tons per hectare. However, one needs to be cautious in interpreting this as a convincing piece of evidence of a causal relationship. Although credit is obviously important for agricultural production, endogeneity problems could be biasing the estimated coefficients.

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<sup>12</sup> The descriptive statistics of *Seeds\_paddy*, *Seeds\_wheat* and *Seeds\_maize* are reported in Annex Table I.1.

<sup>13</sup> Unfortunately, we do not have data on credit disbursements for the production of different crops.

## Foreign Aid<sup>14</sup>

19. **Larger foreign aid disbursements are associated with higher crop yields.** The coefficient estimates suggest that a one-billion-rupee increase in foreign aid disbursements is correlated with an increase in the paddy yield in the amount of 0.06 metric tons per hectare. This finding could be interpreted as indicating that foreign aid has been effective in raising agricultural productivity in Nepal. However, as in the case of agricultural credit, one needs to keep in mind that endogeneity problems could be biasing the coefficients on *Foreign Aid*

## E. Conclusion

20. **The findings of this paper lend support to the following conclusions.** First, weather conditions continue to be a crucial factor, determining to a large extent the yields of crops in Nepal. Second, the increased use of input—chemical fertilizers, improved seeds, and irrigation—has broadly contributed to the overall increase in agricultural productivity in Nepal, although this effect has not been uniform across regions and crops. Third, the access to agricultural credit and foreign aid disbursements play an important role in raising crop productivity.

21. **Although drawing strong policy conclusions from the empirical analysis is difficult due to data limitation and possible endogeneity problems, the results suggest that credit availability is a key factor in raising agricultural productivity.** In this context, the development of well-designed rural credit systems and their effective management in Nepal could play an important role in raising agricultural productivity and the living standards in the country.

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<sup>14</sup> The variables *Agricultural credit* and *Foreign aid* are highly collinear, with a correlation coefficient of 0.87. Therefore, these two variables are not included *together* in any of the model specifications in Tables I.1-I.4.

## Descriptive Statistics and Model Specification

### Descriptive Statistics

The summary statistics of the aggregate sample are presented in Annex Table I.1 below. The units of measurement are described in the second column. Note that the nominal series for agricultural credit and foreign aid have been deflated (1995/96 = 100).

Table I.1. Summary Statistics

Variable	Description	Mean	Median	St. Dev.	Min.	Max.
<i>Paddy</i>	Paddy yield in metric tons per hectare	2.13	2.09	0.30	1.45	2.60
<i>Wheat</i>	Wheat yield in metric tons per hectare	1.38	1.36	0.17	1.17	1.79
<i>Maize</i>	Maize yield in metric tons per hectare	1.59	1.61	0.17	1.33	2.10
<i>Fertilizer</i>	Chemical fertilizer in thousands of metric tons	52.20	46.68	21.96	18.54	90.26
<i>Rainfall</i>	Mean annual rainfall in thousands of mm	1.81	1.85	0.17	1.39	2.02
<i>Irrigation</i>	Irrigated area in thousands of hectares	29.59	23.54	17.53	7.84	59.63
<i>Seeds_paddy</i>	Improved seeds in thousands of metric tons	0.26	0.24	0.12	0.14	0.69
<i>Seeds_wheat</i>	Improved seeds in thousands of metric tons	2.35	2.19	0.76	1.44	4.67
<i>Seeds_maize</i>	Improved seeds in thousands of metric tons	0.11	0.10	0.05	0.03	0.28
<i>Agricultural credit</i>	Disbursements in constant Nrs. (1995/96 =100)	2.38	2.00	1.28	0.60	5.16
<i>Foreign aid</i>	Disbursements in constant Nrs. (1995/96 =100)	10.42	11.20	2.78	5.23	14.49

### Model Specification

In the aggregate sample, three different specifications for each crop yield (paddy, wheat and maize) were estimated. In the first specification (Table I.1, Columns (1), (4) and (7)), the agricultural yields are regressed on a constant and four input variables (*Irrigation*, *Rainfall*, *Fertilizer* and *Seeds*). The financial input *Agricultural credit* is added to the explanatory variables in the second specification (Table I.1, Column (2), (5) and (8)). The third specification uses *Foreign aid* as a regressor (and drops *Agricultural credit*), given the high degree of collinearity between the two variables ( $\rho = 0.87$ ).

In the regional sample, five specifications were estimated for each of the three crops, using four regional dummies (with a reference category *Eastern region*). The first model specification includes a constant, the regional dummies, and the region-varying regressors *Irrigation* and *Rainfall* (Tables I.2, I.3 and I.4, Column (1)). In the second specification, interaction terms between the regional dummies and *Irrigation* are included (Tables I.1-I.4, Column (2)), in order to account for the possibility that different crop varieties (found in different regions) have different irrigation requirements. The aggregate nonfinancial variables *Fertilizer* and *Seeds* are added to the third specification (Tables I.1-I.4, Column (3)). In the fourth and fifth specifications, the regressions contain *Agricultural credit* and *Foreign aid* as explanatory variables, respectively. The standard errors of the last three specifications are adjusted for clustering (Moulton (1991)).



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## II. EXPORT PERFORMANCE: COMPETITIVENESS AND OTHER ISSUES<sup>15</sup>

### A. Introduction

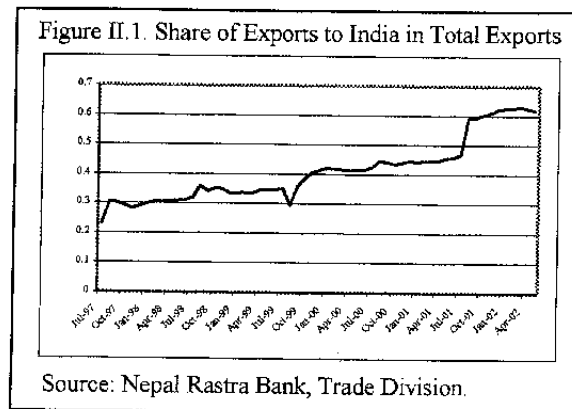
1. **Nepal's export performance has recently deteriorated.** This chapter reviews some factors that may explain the poor performance, and concludes that, while external factors seem to have a large influence on Nepal's exports, certain domestic factors such as higher transportation costs and the Maoist insurgency may have deepened the impact of negative external shocks.

2. **The chapter explores possible causes of the poor export performance.** The next section reviews the recent trends in exports both to India and the rest of the world. External factors that might explain poor performance are then examined, including the global economic slowdown as well as shifts in policies of countries that import Nepalese goods. Domestic factors are reviewed next: the movements of the real exchange rate, disruptions caused by the Maoist insurgency, and additional costs associated with the country being landlocked. A brief concluding section follows.

### B. Recent Trends in Exports

3. **Exports concentration, particularly in terms of markets, has risen over time.** Like other South Asian countries, Nepal is dependent on a few markets and a relatively small number of products, which has made it vulnerable to demand and policy changes in destinations. Over the course of the last decade, dependence on the same few markets has increased for all South Asian countries, but more so for Nepal as 90 percent of its total exports go to only three destinations (Table II.1). Similarly, a few products, such as garments (U.S. market), carpets (German market) and vegetable ghee, copper products, soaps and polyester yarn (Indian market) dominate Nepal's export profile.

4. **Dependence on exports to India has recently increased sharply.** Over half of Nepal's exports are marketed in India where market access has expanded on the basis of a preferential trade treaty signed in December 1996. Since then, Nepal's exports to India has expanded by 2½ times. As this strong growth was accompanied by a slowdown in exports to other key markets, and limited success in penetrating other regional markets, India's share in total exports (cumulative by fiscal year) rose from 23 percent in July 1997 to 62 percent by May 2002 (Figure II.1).



<sup>15</sup> Prepared by Jesmin Rahman (PDR).

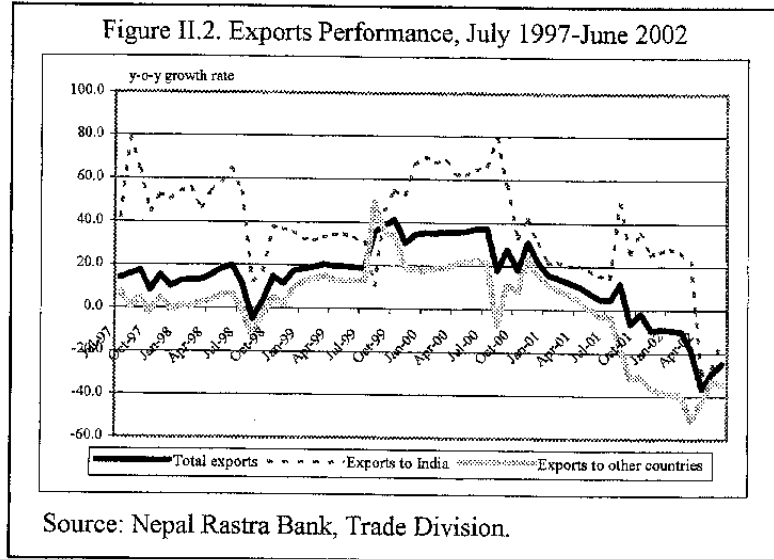
Table II.1: Evolution of Export Market Concentration of Nepal and Comparator Countries

	Share of Top 3 Destinations			Share of the Top Destination		
	1991	1996	2001	1991	1996	2001
	(In percent)					
Nepal	75 (U.S., Germany and India)	81 (U.S., Germany and India)	90 (U.S., Germany and India)	45 (Germany)	34 (Germany)	55 (India)
Bangladesh	45 (U.S., UK and Germany)	52 (U.S., UK and Germany)	48 (U.S., UK and Germany)	27 (U.S.)	31 (U.S.)	30 (U.S.)
Pakistan	28 (U.S., Germany and Japan)	30 (U.S., Germany and UK)	36 (U.S., UK and Germany)	11 (U.S.)	17 (U.S.)	24 (U.S.)
Sri Lanka	42 (U.S., UK and Germany)	50 (U.S., UK and Japan)	53 (U.S., UK and Germany)	28 (U.S.)	34 (U.S.)	38 (U.S.)
Cambodia	61 (Germany, Thailand and Malaysia)	44 (Thailand, Singapore and Germany)	73 (U.S., Germany and UK)	26 (Germany)	15 (Thailand)	58 (U.S.)
Vietnam	62 (Japan, Singapore and Hong Kong)	45 (Japan, Singapore and Korea)	32 (Japan, Australia and China)	33 (Japan)	21 (Japan)	17 (Japan)

Source: Direction of Trade Statistics database and for Nepal (2001), Nepal Rastra Bank.

**5. Exports have declined drastically on account of plummeting sales to third countries<sup>16</sup> and, since April 2002, also to India.**

Overall exports (y/y) grew strongly at an average rate of 22 percent between July 1997 and November 2000, but have since grown at an average rate of only 1 percent. This slowdown was caused first by a marked decline of exports to outside India—growth turned negative in mid-2001 and continued to



deteriorate (Figure II.2). On an annual basis, exports to third countries as of June 2001/02 were 40 percent below the level a year earlier. Exports to India remained strong until the bilateral trade treaty was revised and more restrictive terms were applied in March 2002. Exports to India during April-June 2002 contracted by 24 percent compared to the same period last year, down from an increase of 22 percent in the fiscal year up to March.

### C. Possible Causes of Export Deterioration

6. A number of factors can be considered to have caused this slowdown, including: weaker world demand; adverse policy shifts in key markets; deterioration in external competitiveness; and impacts of the Maoist insurgency, which has disrupted production and transportation activities in some parts of the country.

#### External Factors

7. Weak external demand seems to have affected Nepal's exports to third countries. One explanation for recent lackluster performance is weak demand in major markets, such as the United States and Germany. Imports from developing countries into these markets declined in 2001, by 5 percent and 1 percent respectively, compared with respective increases of 24 percent and 14 percent the previous year. In particular, U.S. apparel imports, a product that constitutes almost 90 percent of Nepal's exports to the United States, declined by 1 percent in 2001 compared with an increase of 13 percent in the previous year, explaining partly Nepal's performance in these two years (Table II.2). Similarly, growth of imports from developing countries into India slowed down to less than 2 percent in 2001 from 13 percent in 2000.

<sup>16</sup> Third countries refer to all destinations except India.

Table II.2: U.S. Apparel Exports to the United States, Comparative Performance 2000–2002

	Nepal	Bangladesh	Pakistan	Sri Lanka	Cambodia	Vietnam	Sub-Saharan Africa	Caribbean Countries	All Exporters
	(In percent)								
Growth Rate									
2000	31	26	26	16	38	31	28	8	13
2001	-17	-1	1	2	16	1	26	-2	-1
04/01– 04/02	-38	-7.1	-9	-2.2	5.2	84	31	-5	-3
Market Share									
2000	0.31	3.7	1.6	2.6	1.4	0.08	1.3	16.7	
2001	0.26	3.7	1.6	2.7	1.7	0.08	1.7	16.6	
04/01– 04/02	0.20	3.7	1.6	2.7	1.7	0.16	1.5	15.7	

Source: U.S. Office of Textiles and Apparel (OTEXA) Website, [http://otexa.ita.doc.gov/ctrynam\\$.htm](http://otexa.ita.doc.gov/ctrynam$.htm)

8. **Nepal, however, seems to be affected much more by the slowdown in major markets than its neighbors.** A comparison of its performance with other Asian countries indicates that Nepal’s exports have performed much more poorly.<sup>17</sup> For example, while Bangladesh and Sri Lanka were able to maintain their respective market shares in the United States, Nepal lost about one third of its share between 2000 and the first quarter of 2002 (Table II.2).

9. **Nepal’s exports are subject to high volatility.** Based on data over the last decade, the following three observations can be made (Table II.3): (i) Nepal’s exports is least correlated with overall changes in imports by the United States; (ii) unlike others, Nepal’s market share varies with its yearly export performance; and (iii) Nepal’s exports are more volatile. In other words, while exports from other South Asian countries to the United States follow more or less the usual fluctuations in U.S. demand, Nepal faces larger gyrations making its market share sensitive to export performance (Annex Figures II.1-II.5).

Table II.3: Growth and Volatility of Apparel Exports to the United States, Nepal and Others

	Correlation between Exports Growth Rate and Growth Rate of Overall U.S. Imports	Correlation between Export Growth Rate and Market Share	Volatility (St. Deviation of Exports Growth)
Nepal	0.42	0.49	0.23
Bangladesh	0.75	-0.18	0.17
India	0.70	0.24	0.12
Pakistan	0.72	0.04	0.16
Sri Lanka	0.44	-0.17	0.10
World			0.06

Data source: U.S. Office of Textiles and Apparel (OTEXA) Website, [http://otexa.ita.doc.gov/ctrynam\\$.htm](http://otexa.ita.doc.gov/ctrynam$.htm)

<sup>17</sup> We chose here Bangladesh, Pakistan, Sri Lanka, Cambodia and Vietnam for the purpose of comparison.

10. **Excessive concentration makes Nepalese exports vulnerable to import policy changes and international competition at destination countries.** In 2001, two trade treaties came into effect in the United States, which can be considered as negative policy shocks for Nepal. These two treaties, namely the African Growth and Opportunity Act (AGOA) and Caribbean Basin Trade Partnership Act (CBTPA), grant producers in sub-Saharan Africa (SSA) and the Caribbean preferential access to the U.S. market.<sup>18</sup> Large increases in exports experienced by Sub-Saharan African countries in a year of overall slowdown point to the fact that these countries are making use of their preferential access under the AGOA.<sup>19</sup> Even though exports from Nepal in 2001 fared much worse than some other Asian exporters, who are also outside the treaty (Table II.2 and Table II.4), it is not possible to conclude whether the first year of AGOA has had a significant negative impact on Nepal's garments exports per se. However, such preferential treaties and the envisaged elimination of the Multifiber Agreement by 2005 put producers like Nepal, who have poor transit facilities and marketing network and are almost exclusively dependent on imported inputs, at a disadvantage.

11. **At the same time, increased dependence on India has elevated risks arising from Indian policy shifts.** The recently renewed India-Nepal trade treaty is more restrictive than its 1996 predecessor<sup>20</sup> as it imposes: (i) binding quantitative restrictions and a 4 percent Special Addition Duty on four products: vegetable ghee, copper wire, acrylic iron and zinc oxide,<sup>21</sup> and (ii) a requirement for minimum value addition of 25 percent this year, and 30 percent in subsequent years. India has also granted monopsony purchasing power to Central Warehousing Corporation for all imports of vegetable ghee from Nepal. This change in policy,

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<sup>18</sup> Under these treaties, duty- and quota-free access is granted to apparel assembled from fabrics that are made and cut in the United States or fabrics manufactured from U.S. yarn. Foreign trimmings and interlinings, provided they do not exceed 25 percent of total component costs, are also allowed. A special rule under the AGOA allows for countries with per capita GNP under \$1500 in 1998 (a total of 28 such countries) to access the U.S. market duty-free for apparel made from fabrics originating anywhere in the world until September 20, 2004.

<sup>19</sup> The overall performance of Caribbean countries, however, does not provide strong evidence of benefits materializing from the CBTPA.

<sup>20</sup> Signed in December 1996 for a period of 5 years, this treaty provided Nepal, on a non-reciprocal basis, quota- and duty-free access to the Indian market, with a few exceptions. The treaty had provisions for bilateral action if there were a surge in exports without actually defining "export surge." Similarly, the treaty did not preclude imposition of anti-dumping duties and other non-tariff barriers.

<sup>21</sup> Exports exceeding the quota levels will be subject to MFN duties and unutilized quotas cannot be carried forward to the next year. The specific levels (vegetable ghee: 100,000 tons, copper wire: 7500 tons, acrylic yarn: 10,000 tons and zinc oxide: 2500 tons) are considerably below those of last year's exports.

from virtual free trade into one with a number of restrictions, has had an immediate negative impact on Nepal's trade performance. (For growth rates by products, see Annex Table II.3).

### Internal Factors

12. **In addition to the above external factors, there could be domestic factors that explain the decline in exports.** One possibility is the loss of external competitiveness. Another possibility is that exports have been severely disrupted by the 6-year old Maoist insurgency that has spread to almost one quarter of the country. To assess developments in competitiveness, two broad indicators, the CPI-based real effective exchange rate (REER) and comparative labor costs in manufacturing between 1980–84 and 1995–99 are examined.

13. **The REER has been stable.** The REER index taken from the Fund's Information Notice System shows that Nepalese rupee (NR), which has been pegged to the Indian rupee (IR) at 1.6NR:1IR since February 1993, has been rather stable over the last several years in real effective term (Figure II.3). To see if Nepal has lost competitiveness in relative terms compared with other South Asian countries, the ratios of the REER index of Nepal with those of these countries are examined. Except in the case of Pakistan which shows that Nepal's REER has appreciated relative to that of Pakistan's, the relative REERs seem to be stable.

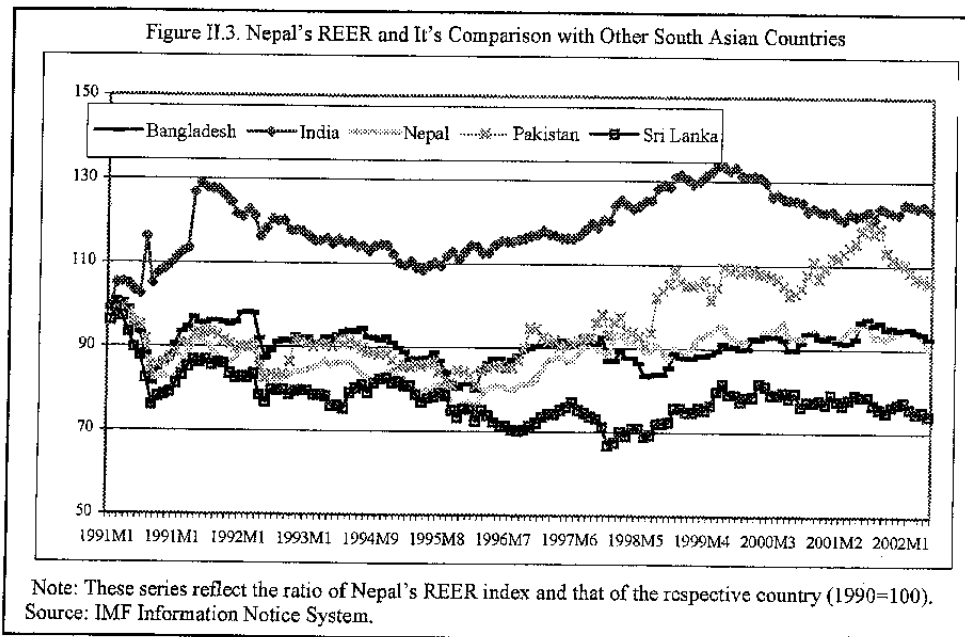


Table II.4: U.S. Market Shares, 2000–2001

(In percent)

	Nepal		Bangladesh		Pakistan		Sri Lanka		Vietnam		Cambodia		SSA	
	2000	2001	2000	2001	2000	2001	2000	2001	2000	2001	2000	2001	2000	2001
Total MFA 1/	0.30	0.26	3.08	3.14	2.56	2.74	2.34	2.42	0.07	0.07	1.14	1.36	1.08	1.39
Apparel	0.31	0.26	3.70	3.72	1.61	1.65	2.57	2.67	0.08	0.08	1.41	1.66	1.31	1.68
Cotton Apparel	0.44	0.39	4.09	4.24	2.58	2.66	2.32	2.52	0.11	0.12	1.89	2.12	2.05	2.63

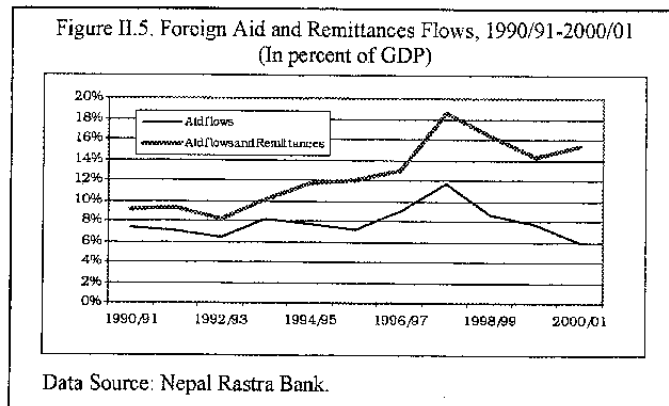
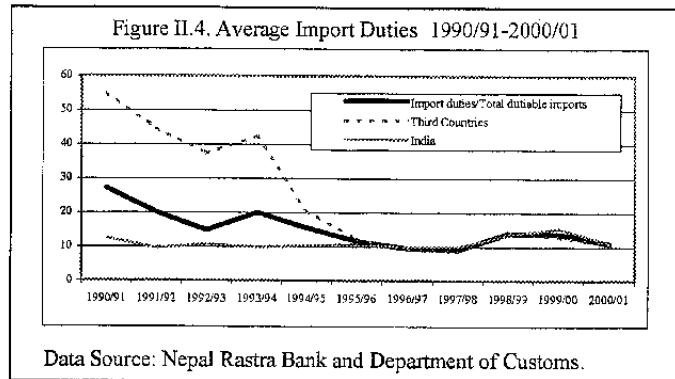
Data source: U.S. Office of Textiles and Apparel (OTEXA) Website, [http://otexa.ita.doc.gov/ctrynam\\$.htm](http://otexa.ita.doc.gov/ctrynam$.htm).

1/ Multifiber Arrangement.



14. **In addition, there is no evidence that the equilibrium REER has changed.** An assessment of REER also requires comparing movement in the REER with its equilibrium value since even a stable REER could imply overvaluation if economic fundamentals determine that the equilibrium REER should be depreciating. The policy and exogenous variables that affect equilibrium REER are terms of trade, trade protection, capital flows, government expenditure on nontradables, and productivity growth.<sup>22</sup>

15. **A heuristic analysis of the key determinants does not suggest any change in the equilibrium REER** although any formal estimation of the equilibrium REER is hampered by the absence of a long enough time series for these key variables. During 1990s, Nepal rapidly lowered its trade protection (Figure II.4) and established a regime that is far more liberal than its South Asian neighbors.<sup>23</sup> While this would put demand pressure on the equilibrium REER, increasing foreign aid and remittances during the same period could counter some or all of such pressure (Figure II.5). There has been no distinct trend detected in Nepal's terms of trade and government expenditure on nontradables.<sup>24</sup>



16. **Wage comparison cannot be conclusive, but appears unlikely to have caused a loss of competitiveness.** Average manufacturing wage in Nepal in U.S. dollar terms has declined during the second half of 1990s compared with the average in the first half of 1980s.

<sup>22</sup> For a detailed discussion, see Edwards, Sebastian (1994) and Elbadawy, Ibrahim A. (1994).

<sup>23</sup> In the Fund's 10-point trade restrictiveness index, Nepal has an overall rating of 2, while the same for Bangladesh, India, Pakistan and Sri Lanka are 8, 8, 7 and 5 respectively.

<sup>24</sup> The terms of trade indices calculated in the WEO are broadly stable. In the absence of data for government expenditure on nontradables, the relative domestic wages in the tradable and nontradable sectors are examined to indirectly gauge if demand has been higher for nontradable goods and services. Based on the data submitted by the authorities, the relative wage of the nontradable sector actually seem to have been declining in recent years.

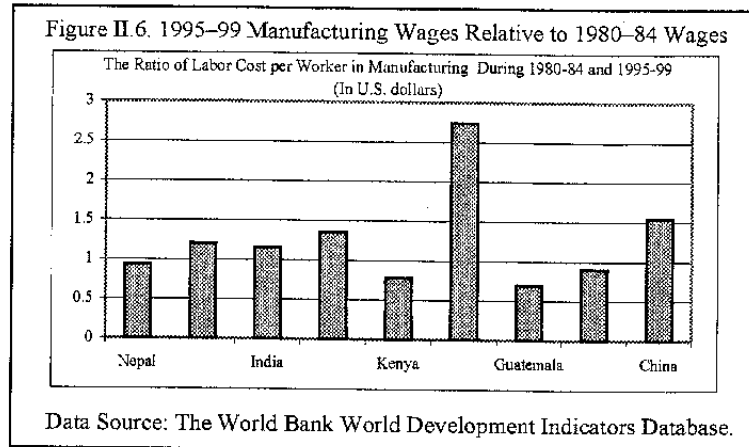
This has been the case for some other developing countries that compete with Nepal in export markets but some others have shown increases (Figure II.6).<sup>25</sup> While this does not take into account productivity changes, this crude comparison of manufacturing wages across time and countries at least does not indicate a loss of competitiveness. Similar pattern is visible in agricultural wages as well (Annex Figure II.6).<sup>26</sup>

**17. However, transportation and other transit costs are high in Nepal and may reduce competitiveness.**

Being landlocked, transportation costs and delivery time for Nepalese products are higher than in neighboring countries. For garment products, transportation costs are 7 percent of the final

invoice value. Similarly, it takes, on average, 45 days for products to leave Katmandu and be shipped off from Calcutta port as transit routes have to follow pre-arranged agreements. While wages and CPI-based real effective exchange rates do not point to a loss of competitiveness in the recent past, higher transportation costs and longer delivery time probably affect adversely Nepal's competitiveness. This may provide an explanation for Nepal's disproportionate response to changes in demand abroad as importers turn toward Nepal only when there is an overflow of demand from lower cost exporters (see paragraph 9). The volatile and uncertain demand in turn prevents producers from maintaining a permanent work force, hiring workers only seasonally and paying premium wages to skilled workers.<sup>27</sup>

**18. The Maoist insurgency may have aggravated the situation.** The Maoist insurgency movement took a new turn last year in terms of targeting businesses in Katmandu valley and neighboring large cities. Maoist-organized *bandhs*/strikes shut down all economic activities in Katmandu altogether for 9 days in the last fiscal year disrupting production and transportation of goods. In addition, the negative publicity and uncertainties created by these activities may



<sup>25</sup> The choice of countries was dictated by data availability and comparability.

<sup>26</sup> Agricultural wages are also compared because agricultural products feature prominently in Nepal's exports to India and neighboring countries.

<sup>27</sup> Interview with Mr. Kiran Saakha, President of the Garments producers' Association in Nepal during 2002 Article IV mission (May 2002).

have resulted in cancellation of foreign buying orders.<sup>28</sup> A number of export manufacturers have also reported to be subjected to forced monetary contributions by the insurgents.

#### **D. Conclusion**

19. **Two factors seem to explain most Nepal's recent slowdown in exports:** greater sensitivity to downturns in import demand in the United States, possibly arising from a less competitive position vis-à-vis other South Asian exporters, and vulnerabilities to negative policy shocks resulting from excessive concentration of exports in a few markets. The limited competitiveness is not a recent development, rather it is a structural phenomenon arising from, among other things, being landlocked and having poor domestic infrastructure. However, the presence of a prolonged domestic insurgency could exacerbate the situation. A sustainable and timely resolution of the conflict is necessary to keep Nepal's existing trading partners on board. Similarly, while Nepal cannot escape constraints imposed by its geographic location, diversifying its export markets and improving domestic infrastructure would make exports more resistant to external shocks.

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<sup>28</sup> These *bandhs* took place on December 7, February 22-23, and April 21-25.

Table II.1. Evolution of Market Shares in Key International and Regional Markets

(In percent of total imports from developing countries)

	U.S.			EU			ASEAN			China			India		
	1991	1996	2001	1991	1996	2001	1991	1996	2001	1991	1996	2001	1991	1996	2001
	Nepal	0.03	0.03	0.04	0.06	0.04	0.02	0.01	0.00	0.01	0.00	0.00	0.00	0.27	0.27
Bangladesh	0.27	0.38	0.43	0.29	0.46	0.54	0.09	0.05	0.08	0.03	0.05	0.01	0.08	0.32	0.24
Cambodia	0.00	0.00	0.18	0.01	0.03	0.08	0.04	0.08	0.06	0.00	0.01	0.04	0.00	0.00	0.00
Pakistan	0.34	0.36	0.42	0.71	0.65	0.47	0.46	0.28	0.18	0.28	0.54	0.31	0.80	0.21	0.26
Sri Lanka	0.31	0.39	0.36	0.27	0.32	0.30	0.11	0.07	0.06	0.02	0.01	0.01	0.16	0.19	0.25
Vietnam	0.00	0.09	0.20	0.08	0.46	0.79	0.43	0.60	1.33	0.03	0.49	0.83	0.53	0.01	0.08

Source: Direction of Trade Statistics Database.

Table II.2. Growth Rates of Apparel Exports to the United States of Nepal and Others, 2001

(In percent)

Product category	Nepal	SSA	Caribbean	World	Bangladesh	Cambodia	Pakistan	Sri Lanka	Vietnam
Total MFA	-15	26	-2	-2	1	17	5	1	-1
Apparel MFA	-17	27	-2	-1	-1	16	1	2	1
	(83)	(96)	(99)	(80)	(96)	(99)	(50)	(88)	(95)
Cotton Apparel	-13	27	-3	-1	3	11	2	7	4
	(66)	(85)	(67)	(45)	(59)	(74)	(45)	(44)	(71)
Wool Apparel	-74	7	-4	-1	-29	29	-65	33	196
	(8)	(6)	(3)	(5)	(2)	(2)	(0.05)	(1)	(.1)
MMF Apparel <sup>1/</sup>	19	55	-3	-2	35	32	-6	-3	-6
	(8)	(7)	(30)	(38)	(30)	(21)	(12)	(51)	(25)

Data source: U.S. Office of Textiles and Apparel (OTEXA) Website, <http://otexa.ita.doc.gov/ctrynamS.htm>.

Note: Numbers in brackets represent share of this product in the country's total MFA exports to the United States.

1/ MMF: Man-made fabric.

Table II.3. Growth Rates of Exports to India (Y/Y) Before and After the New Treaty

(In percent)

	Y/Y Growth Rate March 2002	Y/Y Growth Rate April 2002	Share in Total Exports
Total exports to India.	35	20	
Vegetable ghee	223	174	29
Copper wire rod	139	86	11
Tooth paste	-13	-24	5
Pulses	59	44	4
Polyester yarn	61	42	3
Medicine (Ayurvedic)	4	-3	2
Sacks	23	7	2
Pashmina	-83	-83	2

Source: Nepal Rastra Bank, Trade Division.

Figure II.1. Nepal's Growth Rates of Apparel Exports and Market Share in the United States

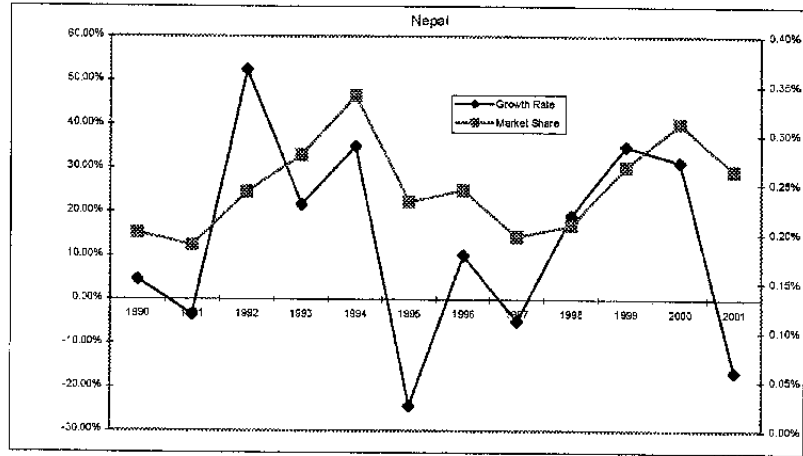


Figure II.2. Bangladesh's Growth Rates of Apparel Exports and Market share in the United States

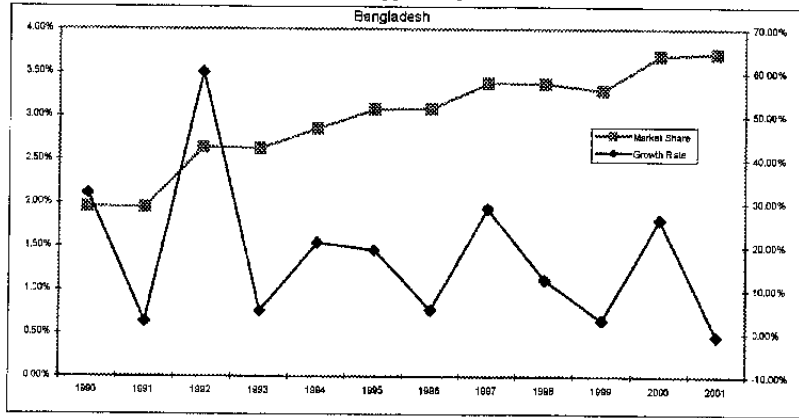


Figure II.3. Pakistan's Growth Rates of Apparel Exports and Market Share in the United States

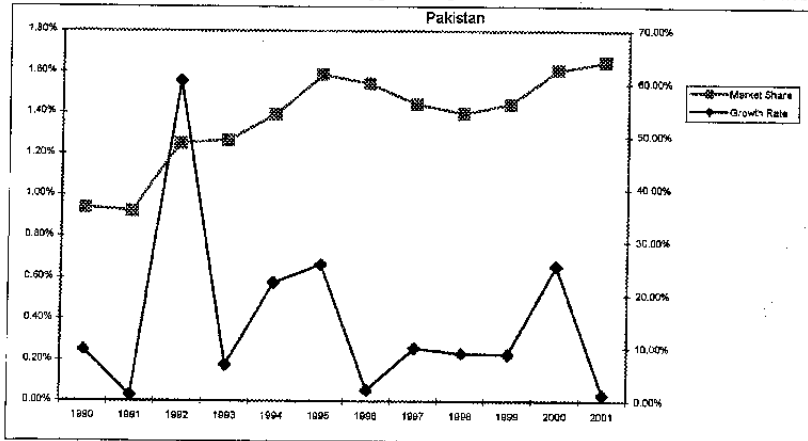


Figure II.4. Sri Lanka's Growth Rates of Apparel Exports and Market Share in the United States

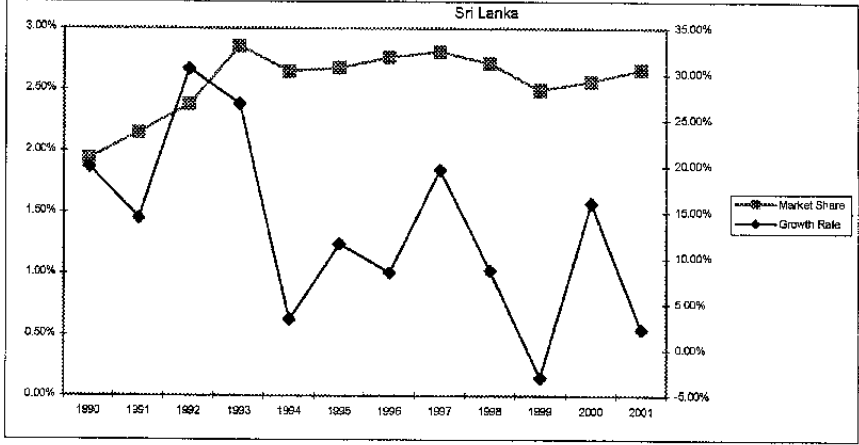


Figure II.5. India's Growth Rates of Apparel Exports and Market Share in the United States

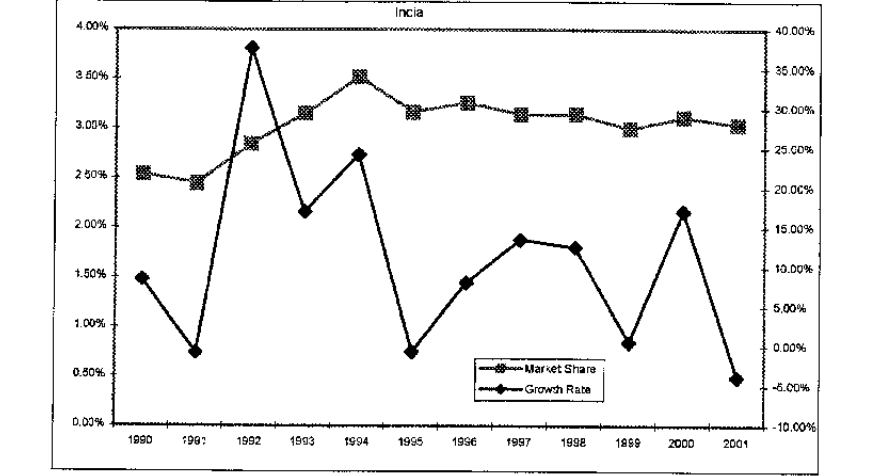
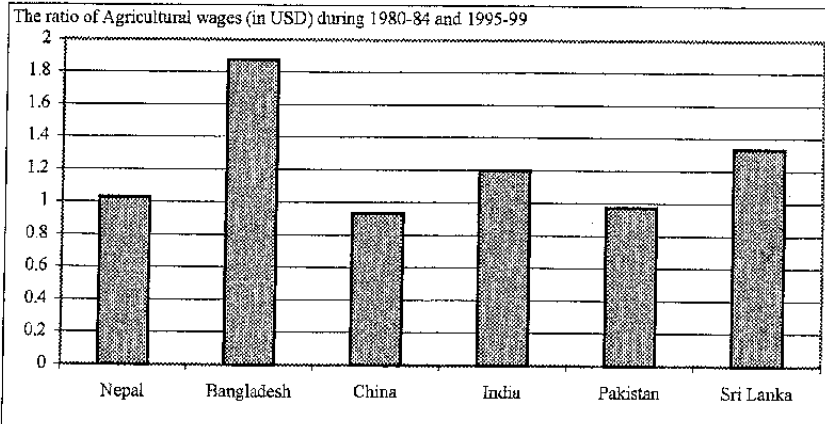


Figure II.6. Agricultural Wages in Nepal and Comparator Countries





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### III. FISCAL DECENTRALIZATION<sup>29</sup>

#### A. Introduction

1. **Nepal remains among the poorest countries in the world with forty percent of the population living in poverty.** Poverty incidence has not declined over the last two decades, with disparities perceived to be widening across regions, ethnic groups, and genders. The forthcoming Poverty Reduction Strategy Paper identifies poor service delivery in the rural areas resulting from inefficient public resource management as among the main causes of pervasive poverty.
2. **The government has decided to devolve a significant part of spending responsibilities especially in social areas to improve service delivery, and to a lesser extent, revenue-raising responsibilities.** This action stems from the belief that local governments are in principle better equipped to design and implement policies tailored to local residents' needs and preferences—especially of the poor. In addition, a higher degree of local autonomy and hence local participation in collective decision-making is believed to reduce perception of alienation among residents outside the major urban centers. Proponents of decentralization argue that, if these effects in fact could be realized, decentralization would also weaken the base for support for the Maoist movement.
3. **A legal framework and implementation plans for decentralization are being prepared.** The Local Self-Governance Act (LSGA) was enacted in 1999 and associated regulations were issued in 2000. They define legal and institutional framework for the local government structure geared toward decentralization. However, other relevant laws have not been amended in line with provisions of the LSGA. As a consequence, the current legal framework contains duplications and inconsistencies with regard to roles and responsibilities of central and local governments.<sup>30</sup> To move ahead with decentralization, the government issued in January 2002 a Decentralization Implementation Plan (DIP), a comprehensive strategy to implement fiscal decentralization. In addition, an Immediate Action Plan (IAP) was issued in July 2002. The IAP contains a plan to develop a grant allocation formula based on poverty situations in individual jurisdictions and to devolve management of limited numbers of primary schools and health sub-posts to local communities.
4. **The chapter discusses the status of these plans and the future prospects for decentralization.** It first describes Nepal's current local government system along with its revenue base and expenditure assignments. The next two sections discuss the government's

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<sup>29</sup> Prepared by Joong Shik Lee (APD).

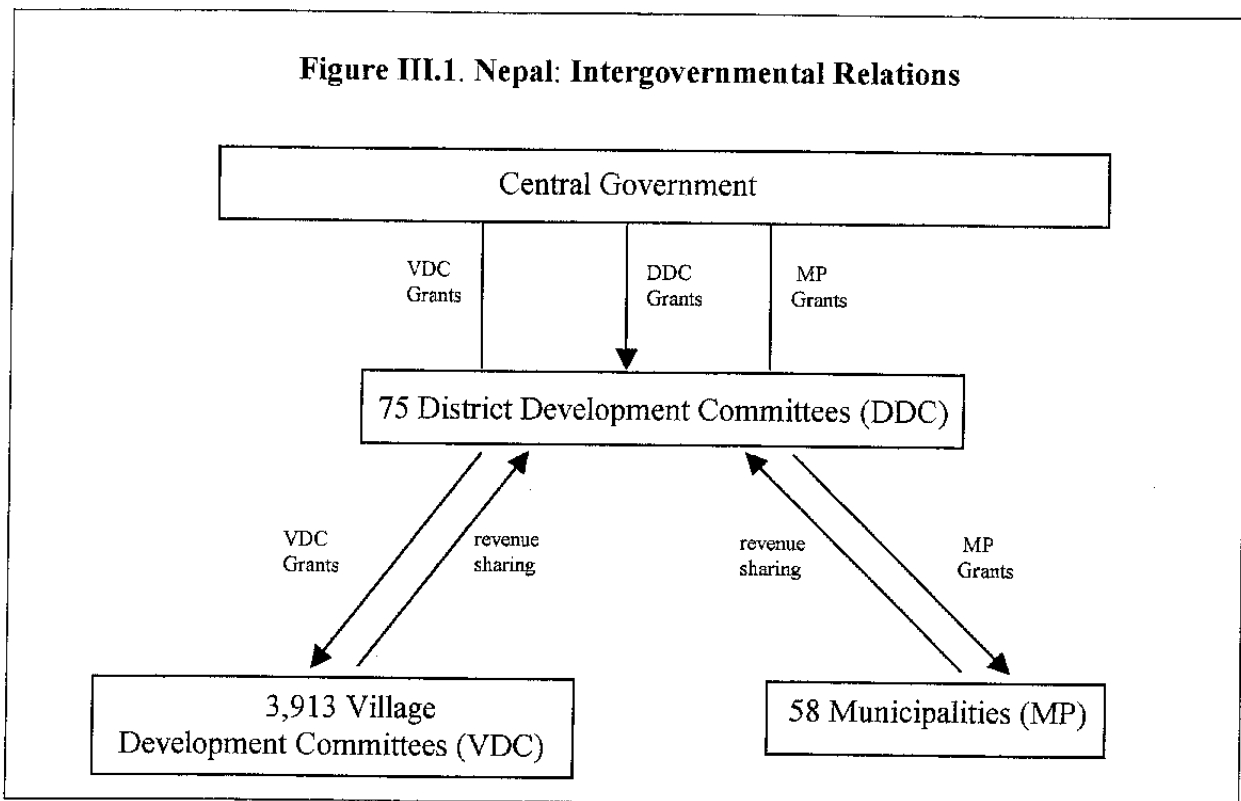
<sup>30</sup> The government has identified 23 sectoral acts conflicting with the LSGA. Of these, 14 acts have been redrafted to make them consistent with the LSGA and submitted to Parliament, but none has been enacted.

ongoing reform initiatives and challenges ahead. The paper concludes with a few key observations including the need to proceed carefully to ensure benefits of decentralization can be reaped.<sup>31</sup>

## B. Local Government Structure

### Levels of Local Governments

5. Nepal has two tiers of local governments: district governments at the higher tier, and municipal and village bodies at the lower tier (Figure III.1). The LSGA spells out roles and responsibilities of these local governments.



6. **District Development Committees (DDC), district level governments, coordinate between the central government and lower-tier local governments.** There are 75 DDCs. DDCs plan and monitor implementation of development projects within the jurisdiction, and participate in the central government's budgetary process. DDCs also provide technical,

<sup>31</sup> Financial information pertaining to local governments in Nepal is extremely limited. Only very rudimentary data are available for municipalities as discussed below.

managerial, and financial support to lower-tier local bodies. Each district has a district council comprising mayors and deputy mayors of municipalities, chairpersons and vice chairpersons of village development committees, and chairperson, vice chairperson, and members of the concerned DDC. All these officials are elected through local elections every five years.<sup>32</sup>

**7. Municipalities and village councils constitute second-tier local governments.**

The 58 municipalities govern local urban areas and each municipality (an average population size of 60,000) has a council consisting of mayor, deputy mayor, and nominated members. The 3,913 village bodies are called Village Development Committees (VDC) served by chair and vice chairpersons. The average population size of a village is 5,000.

**8. The LSGA authorizes local governments to hire their own staffs but the center sends staff to facilitate and monitor local government management.** Local government staffs are generally limited to lower-level civil servants. The central government appoints a secretary in each local government to monitor local government activities, and deposes additional professional staff such as accountants and engineers at DDCs. They are paid by and accountable to the central government. Nevertheless, the overall extent of monitoring is weak, reflecting lack of established monitoring standards and insufficient (and sometimes undermotivated) deputed central government staff—350 VDC secretary positions are currently vacant.

### **Revenue Base of Local Governments**

**9. Local governments' own revenue collection is limited despite the provisions of the LSGA, which in principle allow them to collect various taxes and fees (Table III.1).** Local revenue collection is low as business opportunities in most jurisdictions are limited and the capacity of local tax officials is weak. Also, as the legal framework does not define the role of each level of the government consistently, the central authorities continue to provide most public services needed in local jurisdictions. This reduces local authorities' incentives to raise own revenues as they depend on the center for provision of necessary services.

**10. Local governments as a result depend heavily on development and administrative grants from the central government but total central government**

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<sup>32</sup> However, elected posts in the local bodies have been vacant since the tenure of the elected officials expired on July 16, 2002, as previously scheduled local elections were not held due to security reasons in the affected areas. The central government expressed its intention to make appointments to replace all elected representatives instead of extending the tenure of the local elected representatives. This action has been criticized as against the spirit of decentralization—including by the donor community.

Table III.1. Financial Resource Base in Local Governments  
(As of July 2002)

Type	DDCs	Municipalities	VDCs
Taxation	<ul style="list-style-type: none"> <li>• Tax on roads, paths, bridges, irrigation, ditches and ponds</li> <li>• Tax on wool, herbs, turpentine, worn and torn goods (35 to 50 percent of collection provided to concerned municipalities and VDCs)</li> </ul>	<ul style="list-style-type: none"> <li>• Land revenue and house and land tax (25 percent of collection handed over to concerned DDC)</li> <li>• Rent and tenancy tax</li> <li>• Enterprise tax</li> <li>• Vehicle tax</li> <li>• Unified property tax</li> <li>• Entertainment tax</li> <li>• Commercial video tax</li> <li>• Advertisement tax</li> </ul>	<ul style="list-style-type: none"> <li>• Land revenue and house and land tax (25 percent of collection handed over to concerned DDC)</li> <li>• Rent and tenancy tax</li> <li>• Business tax</li> <li>• Vehicle tax</li> <li>• Entertainment tax</li> <li>• Commercial video tax</li> <li>• Advertisement tax</li> </ul>
Fees and charges	<ul style="list-style-type: none"> <li>• Licensing and renewal fee for television</li> <li>• Approval fee</li> <li>• Recommendation fee</li> </ul>	<ul style="list-style-type: none"> <li>• Parking charges</li> <li>• Service charges for waste management and sanitation</li> <li>• Fees for parks, and other public facilities</li> </ul>	<ul style="list-style-type: none"> <li>• Parking charges</li> <li>• Fees for natural resources utilization</li> <li>• Service charges for waste management and sanitation</li> <li>• Entrance fees on tourist places</li> <li>• Service charge on entertainment performances</li> </ul>
Sales	<ul style="list-style-type: none"> <li>• Sand, stones, soil, wood (35 to 50 percent of proceeds provided to concerned municipalities and VDCs)</li> </ul>	-	<ul style="list-style-type: none"> <li>• Soil of barren land, products of public ponds and gardens, forest products</li> </ul>
Transfers and grants from the central government	<ul style="list-style-type: none"> <li>• Development support grant (40 percent of program cost)</li> <li>• Administrative grant</li> </ul>	<ul style="list-style-type: none"> <li>• Local development fees, allocated on the basis of 1997/98 Octroi collections</li> <li>• Development support grant (40 percent of program cost), excluding municipalities with own-source revenues more than Nr 10 million</li> <li>• Administrative grant</li> </ul>	<ul style="list-style-type: none"> <li>• Administrative grant, annually Nr 0.5 million<sup>2/</sup> for all the VDCs</li> </ul>
Loans	-	<ul style="list-style-type: none"> <li>• Loans from Town Development Fund</li> </ul>	-

Source: Financial Provision of Local Self-Governance Acts 1999.

1/ An interim measure to supplement revenue loss from the abolishment of the Octroi tax in 1998/99.

2/ Released amount was reduced by up to 50 percent in 2001/02.

**transfers are declining in real terms.** The nominal amount of the transfers has stayed relatively constant at Nr 3 billion for the last five years (0.7 percent of 2001/02 GDP, or 4 percent of central government total spending in the same year) and its real value has declined by 35 percent over the same period. Of this amount, DDCs receive Nr 700-800 million, municipalities Nr 200-300 million, and VDCs nearly Nr 2 billion.

**DDCs**

**11. Central government grants are the largest resources available to DDCs.** Development grants cover 40 percent of the cost of selected development and self-help programs. However, criteria for selecting projects eligible for grants are not clear. Other revenue sources in DDCs, albeit limited, include taxation on rural roads and bridges, licensing and renewal fees for video equipments, and sales of natural resources. Some revenue sharing with VDCs and municipalities has also been in place.

**Municipalities**

**12. Total resource available to municipalities is about Nr 1.5 billion a year or ½ percent of 1998/99 GDP** (Table III.2). The local development fees (LDF) account for Nr 700-800 million. LDF replaced the Octroi tax (1 percent of invoice of any goods entering a jurisdiction) with the enactment of LSGA 1998/99. LDF is collected at the customs at a rate of 1.5 percent of import duties and allocated across municipalities in proportion to each municipality's 1997/98 Octroi collection. Because LDF was introduced as an interim measure to replace revenue loss from the abolishment of the Octroi tax, the central government plans to phase out the LDF within five years by broadening municipal revenue sources.

Table III.2. Municipality Resources, 1996/97-98/99

	1996/97	97/98	98/99	1996/97	97/98	98/99
	(In millions of Nepalese rupees)			(In percent of total)		
Total resources 1/	1,047	1,586	1,545	0.4	0.5	0.5
Local taxes	686	984	869	65.6	62.0	56.3
<i>O/w</i> : Octroi/Local dev. fees	557	782	683	53.2	49.3	44.2
Fees, fines, and rentals	100	118	140	9.6	7.5	9.1
Grants	85	262	247	8.1	16.5	16.0
Loans and refunds	41	35	69	3.9	2.2	4.4
Other income	135	187	220	12.9	11.8	14.3

Source: Ministry of Local Development.  
1/ Percent of total refers to percent of nominal GDP.

**13. Central government grants are around 15 percent of available municipal resources.** All municipalities receive administrative grants based on the number of local staff. Development grants are provided to less developed municipalities, defined as those with annual revenue generation of less than Nr 10 million. Municipalities can also finance selected social infrastructure projects and revenue generating projects through loans from the Town Development Fund—established in 1989 under the assistance from the World Bank and Germany (GTZ) as a fully autonomous financial institution. Loans are provided for 90 percent of eligible project costs, and repaid at 6 percent interest rate for 10 years after a grace period of two years.

*VDCs*

14. **VDCs own revenues are also limited.** Most of the recurrent fiscal activities in the VDCs are supported by the administrative grant from the central government—an equal amount of Nr 0.5 million for each VDC.<sup>33</sup> Collections from other sources, including taxation, fees, and revenue sharing, are reported to be almost negligible at this stage.

**Expenditure Assignment**

15. **Spending responsibilities of central and each level of local governments are not clearly defined.** The LSGA defines national or economy-wide functions (for example defense) as those of the central government while services with substantial local benefits (including social sectors, local road maintenance and garbage collection) as those that should be performed by local governments. However, local governments have not taken over most of these responsibilities because (i) preparation for devolution with a timetable and supporting measures started only with DIP; (ii) local governments do not yet have sufficient financial resources or technical capacity to carry out what are described in the LSGA as local government responsibilities; and, most importantly (iii) the central government has continued to provide public services in most jurisdictions due in part to the ambiguities in the legal framework as discussed above. It is also said that central ministries have been reluctant to devolve functions that were under their purview.

16. **A significant part of local government spending appears to be recurrent expenditures, and given limited resources, spending on social sector programs is limited.** DDCs spent Nr 1,360 million in 1999/2000, of which Nr 660 million was recurrent. In case of municipal expenditures, the share of current expenditures increased consistently, reaching about the same level as capital expenditures in 1998/99 (Table III.3). Debt payments on principal and interest have been limited to around 3 percent of the total expenditure. Spending in the VDCs is reported to be almost exclusively on general administration, mostly in the form of salaries and various types of allowances.

Table III.3. Municipality Expenditure, 1996/97-98/99

	1996/97	97/98	98/99	1996/97	97/98	98/99
	(In millions of Nepalese rupees)			(In percent of total)		
Total expenditure 1/	904	1,383	1,392	0.3	0.5	0.4
Current expenditure	390	619	654	43.1	44.8	47.0
o/w: Salaries & allowances	217	361	400	24.0	26.1	28.7
Debt payment	26	44	35	2.9	3.2	2.5
Capital expenditure	443	714	670	49.0	51.6	48.1
Social program	71	50	68	7.9	3.6	4.9

Source: Ministry of Local Development.

1/ Percent of total refers to percent of nominal GDP.

<sup>33</sup> In 2001/02, the actual release had been reduced by up to 50 percent in view of the escalated security expenses in the midst of the Maoist insurgency.

### C. Summary of the Ongoing Reform Initiatives

17. **With the approval of the DIP and the IAP, implementation of the fiscal decentralization is expected to accelerate.** Limited basic education and health services will be devolved to local committee as pilot cases in the IAP, and the Budget 2002/03 has been formulated to incorporate such activities.

#### **Decentralization Implementation Plan (DIP)**

18. **The government has prepared the DIP after the enactment of the LSGA in 1999 with the aim of formulating a comprehensive time-bound plan toward decentralization.** The DIP incorporates views and recommendations of a wide range of concerned parties including government agencies, donors, representatives of the local government associations, and Public Expenditure Review Commission. With the DIP, the government hopes that all decentralization efforts including those made with donor assistance can be brought into a unified and consistent framework.

19. **The DIP addresses many important decentralization issues, including planning, budgeting, capacity building, legal framework, and monitoring.** It emphasizes the need to enhance local governments' capacity to raise and manage fiscal resources. DIP also identifies sectors to be devolved in different phases: primary education, basic health, agricultural extension, and postal services in the initial phase; and drinking water, irrigation, road, and rural electrification in the next phase.

20. **The DIP consists of 26 major tasks, divided into more than 60 activities, to be implemented by different ministries.** Each activity is classified into three different time horizons: short-term activity (within one year), medium-term activity (within three years), and longer-term activity (within five years).

- **Short-term activities focus on building strong revenue base in the local governments** by identifying new local revenue sources and establishing an appropriate tax collection system. A grant allocation system will also be designed reflecting local needs and differences (see below), and preparations will be made to introduce proper auditing and accounting systems.
- **In the medium-term, emphases are placed on the implementation of the agenda established in the short-term.** These include: implementing the new grant allocation system, reviewing and restructuring local tax and service rates, enhancing local governments' human capital, ensuring local governments' functions are properly funded, and installing adequate monitoring and accounting systems.
- **Longer-term activities aim to establish self-governance at local levels.** Transfer of local development fees to the municipalities will be eliminated, replaced by sufficient own revenue mobilization. The local government structure will be reviewed, and possibly be streamlined from an efficiency standpoint.



### **Immediate Action Plan (IAP)**

21. **The IAP focuses on activities that can be implemented in the immediate future—within this fiscal year.** While the DIP provides a comprehensive list of measures toward successful decentralization, its coverage is broad and its proposed measures are still not specific enough for implementing decentralization. To address this and wider economic problems the country is facing, the government has formulated IAP identifying key measures to be implemented immediately. The Plan includes decentralization as part of an important reform agenda.<sup>34</sup>

22. **The first key IAP task associated with fiscal decentralization is to develop a poverty based grant allocation formula** by October 31, 2002 to be used in the Budget 2003/04. Survey on human resource development provides necessary information on district-wise indicators of relative poverty.<sup>35</sup>

23. **The other important task in the IAP is to support the devolution of the primary education and basic health sectors in 10 to 12 selected districts.** In case of primary education, operation (including management and teacher recruitment) of the 100 public primary schools<sup>36</sup> will be handed over to the School Management Committee (SMC) of the concerned schools. Draft of the new Education Act contains a provision which will facilitate the transfer of school management. An elected parent will serve as chairperson of the SMC, and members of the committee will consist of parents and representatives from corresponding local governments.

24. **In the health sector, management of about 1,000 sub-health posts will be handed over to the Local Health Office Operating and Management Committee at the VDC level by the end of 2002/03.** So far, 20 sub-health posts in ten districts have been identified for immediate devolution. The concerned VDCs and the District Health Offices will be responsible for monitoring the operational status of the sub-health posts including range of services and staff attendance.

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<sup>34</sup> Implementation of IAP is linked with prospective budget support by several donors, which, if approved, could total up to US\$128 million.

<sup>35</sup> It has, however, been found through NPC's field surveys that poorest districts have the least absorptive capacity in terms of community institutions and awareness.

<sup>36</sup> As of end-2000, there are about 26,000 primary schools in Nepal.

## **D. Challenges Ahead**

25. **Successful decentralization should lead to better resource allocation and improved service delivery on the ground.** This success will, however, be predicated on improved information on local public finance and enhanced accountability and administrative capacity of local authorities. Also, local governments will need to have sufficient financial resources to fund devolved activities. If any of these elements is missing, decentralization efforts could end up in transferring inefficiencies, and possibly corruption, from the center to local levels. Nepal faces significant challenges because many of these required elements are not yet in place.

### **Capacity of Local Governments**

26. **The administrative capacity of local governments in planning and delivering public services is weak.** Most local governments suffer from insufficient human and physical resources. In particular, management skills are in short supply. Significant technical assistance from the central government and/or donors is needed to address this issue. It is also expected to take some time before adequate skills are accumulated at local levels.

### **Accountability of the Local Governments**

27. **Local governments are not held accountable by local residents or the central government** mostly because the central government has been providing important public services. But if decentralization is to work well, accountability will be key to success—residents should be able to demand that local governments provide services tailored to their needs while the central government, when it supports local bodies financially, should be able to see to it that the service quality exceeds the minimum acceptable standards. The latter is particularly important when services provided have a large impact outside a single local jurisdiction—such as primary education or flood control.

### **Monitoring of Local Government Activities**

28. **Monitoring, reporting, and evaluation of local government fiscal activities have been virtually nonexistent.** Collecting and analyzing information on local government finance—and making collected information available—is critical for holding local governments accountable. So far, there is no firm requirement for local governments to report their full budgetary accounts to the central government or make its detail public. The central government on the other hand does not insist on monitoring and evaluating fiscal activities of local governments even though it deposes a secretary to each local government. As a result, no comprehensive local government revenue and spending data are compiled even at aggregate levels.

## Financial Resources

29. **Local governments do not have sufficient financial resources to carry out devolved functions.** Their revenues barely cover basic administrative expenses. The authorities need to gauge the costs of devolved activities, and ensure that local governments can finance them with their own revenues supplemented, as needed, by transfers from the central government. The authorities are in the process of designing a grant allocation formula that takes the local poverty levels into account (as an indicator of social service needs). But, a simple gap-filling grant reduces local governments' incentives to raise revenues and increases incentives to inflate their needs. Also as the authorities have recently found out, poorer regions tend to have less implementation capacity. It would be important to devise a grant allocation framework that ensures funding without distorting local governments' incentives to raise revenues or willingness to address poverty issues.

## E. Concluding Remarks

30. **The concept of fiscal decentralization is appealing, particularly in view of Nepal's diversity and geographical characteristics as well as its security problems.**

Decentralization should in principle improve public service delivery meeting the needs of residents and lead to better resource allocation.

31. **However, building blocks required for implementing decentralization successfully are largely absent in Nepal.** These building blocks include: improved information on local public finance and adequate administrative capacity, as well as accountability of the local authorities. As in many other developing countries, even the most basic demographic information is not available for local units in Nepal, not to mention information on potential revenue capacity of local governments or cost of public service provision. With the lack of available information, it is difficult to hold local governments accountable. Furthermore, administrative capacity of local officials is limited.

32. **In this environment, rapid devolution of fiscal activities can pose a significant threat to the central government in maintaining overall fiscal discipline.** Examples of such cases can be found in a number of countries, in which fiscal decentralization places severe constraints to macroeconomic management (Ter-Minassian, 1997).

33. **Decentralization should thus be implemented cautiously.** There should be a clear understanding by both central and local authorities on the activities to be devolved and the timing of devolution. Implementation should be in small steps so that it would be consistent with the pace of development of local capacity. In this regard, the ongoing efforts to start decentralization through transferring to communities management of 100 primary schools and 20 sub-health posts with close monitoring by and technical assistance from both the central government and donors appear appropriate. Larger scale decentralization could take place only after sufficient experience is gained in managing and monitoring the process by both local and central governments.

34. **Clear understandings are also needed on the revenue base of local governments and a system of intergovernmental transfers.** Such understandings should provide an effective budget constraint to local governments. It is important that the formula for grant allocation should contain no discretionary (or negotiated) element so that local governments' budget constraint is hard. The formula should also allow local governments to provide an acceptable level of required social services while maximizing incentives to raise local government revenues. Nepal could also learn from other country experience in designing a strategy for decentralization with an appropriate formula for grant allocation.

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#### IV. THE CIVIL SERVICE SECTOR: KEY ISSUES AND REFORM PLANS<sup>37</sup>

##### A. Introduction

1. **The civil service sector plays an important role in promoting sustained growth and social development.** The presence of efficient, competent, and motivated civil servants is associated with a better provision of public services to the population, as well as an enhanced capacity of the government to perform core functions and implement reform plans.
2. **This chapter presents and discusses the problems and reform initiatives in the civil service in Nepal.**<sup>38</sup> The main problems of the civil service are related to its size, structure, composition, and compensation, as well as its pension liabilities. In order to address these issues, the authorities have begun to implement a series of reforms.
3. **The remaining part of the chapter is organized as follows.** Section B describes the data source and sample used to illustrate the characteristics of the core civil service in Nepal. Section C discusses the main problems of the civil service sector. Section D presents and assesses the key reform initiatives undertaken by the authorities, and Section E concludes.

##### B. Data Source and Sample

4. **Since the characteristics of the core civil service had been largely unknown, the authorities conducted a census with the assistance of the Asian Development Bank (AsDB).** Started in early 2000, the census was expected to end by late November 2000. However, delays from five districts under the control of the Maoist insurgents and technical problems postponed its completion. In addition, concerns about accuracy prompted the verification of the collected records, which continued throughout 2001. The aggregate results of the census are currently available, together with a large sample of the individual-level data.<sup>39</sup>
5. **The discussion in this chapter is based on the quantitative analysis of 75 percent of the filled civil service positions recorded in the census.** The sample used in the statistical analysis consists of 67,333 individual records, with information about the age, gender, ministry, post level, and position of each civil servant. The data in the sample are used to

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<sup>37</sup> Prepared by Petya Koeva (EU1).

<sup>38</sup> The discussion focuses on core civil servants only. The civil service sector in Nepal comprises core civil servants, teachers, army, and police.

<sup>39</sup> The complete computerization of the obtained personnel records and the linking of positions and individuals are still in progress.

present a complete picture of the current employment structure and composition of the core civil service in Nepal.<sup>40</sup>

### C. Main Issues

6. **The problems of the core civil service in Nepal arise from its size, structure, composition, wage structure, and pension liabilities.** In particular, the number of civil servants is large at the lower grades. Moreover, the composition of the civil service by ministry and gender is skewed, with few ministries employing the majority of the (predominantly male) civil servants. In addition, wages are compressed, i.e., the ratio of highest to lowest paid is low. Another cause for concern is the level of pension liabilities, which is likely to increase over time.

#### Size

7. **The core civil service in Nepal comprises 106,000 positions, accounting for about 0.4 percent of the population.** According to the civil service census, the numbers of filled and unfilled positions are 89,000 and 17,000, respectively. As a percentage of the total population, the size of the Nepalese core civil service is comparable to those in other countries (see Table IV.1)—larger than the average for South Asia (0.3 percent), but lower than the average for low-income countries (0.5 percent).<sup>41</sup>

#### Structure

8. **However, the lower echelons of the civil service are large, leading to a bottom-heavy distribution of positions** (see Figure IV.1).<sup>42</sup> Approximately one third of the

Table IV.1. Civil Service Employment in Selected Low-Income Asian Countries in 1996-2000<sup>1/2/</sup>  
(In percentage of total population)

Country	Size
	(In percent)
Nepal	0.4
India	0.3
Bangladesh	0.4
Mongolia	0.2
Cambodia	0.2
South Asia average	0.3
Low-income group average	0.5

Source: World Bank cross-country database.

1/ Data are for the latest year available.

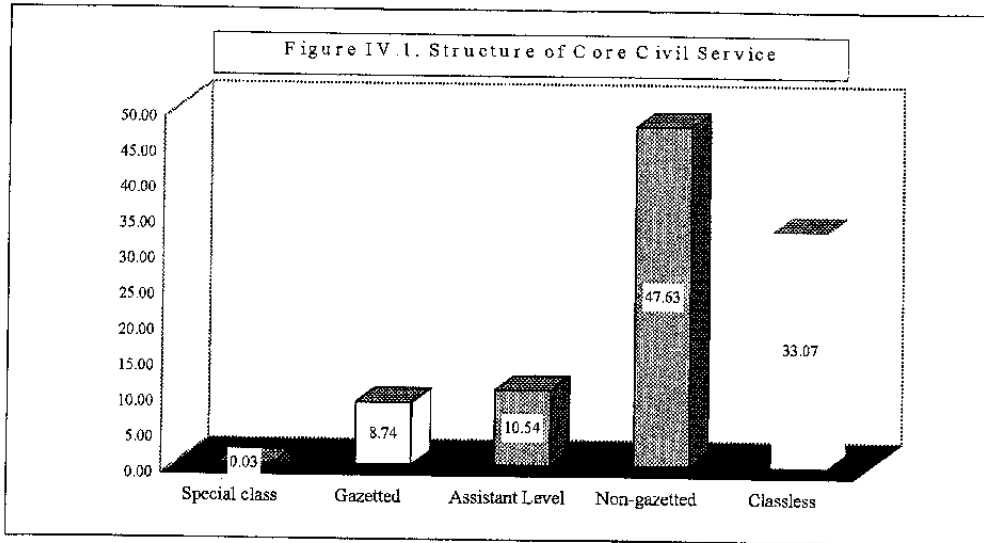
2/ Permanent employees in the civilian central government (excluding education, health, and police, if available).

<sup>40</sup> The results are representative of the entire core civil service, as long as the individual records are entered in a random order, i.e., the remaining 25 percent of the records are not "exceptional" in any way. There is no evidence to suggest that this is the case.

<sup>41</sup> See *Cross-National Data on Government Employment and Wages*, provided by the World Bank at <http://www1.worldbank.org/publicsector/civilservice/development.htm>.

<sup>42</sup> According to the Public Expenditure Review Commission (PERC) report of March 2001, the employment structure became bottom-heavy after 1991. In particular, the number of peon positions increased by 20 percent between 1991 and 2000.

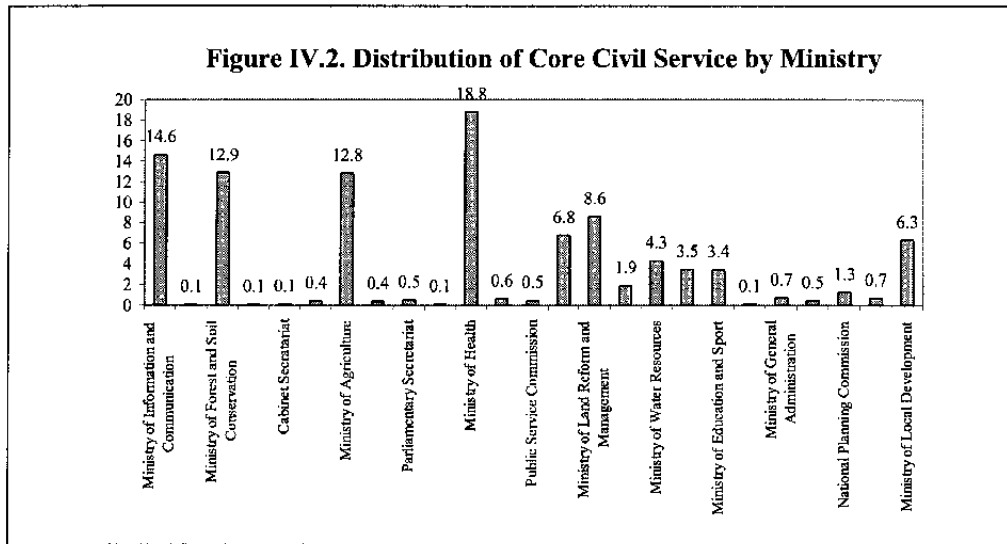
civil servants are at the *Classless* level, which includes low-rank positions such as peon, driver, guard, etc. The nongazetted staff—typists, assistant technicians, rangers and others—comprise around 48 percent of all core civil servants. In contrast, the percentage of gazetted employees (auditing and accounting officers, engineers, chemists, inspectors, etc.) is only 9 percent. As expected, the highest rank civil servants (*Special class*) account for a small percentage (less than 1 percent) of the employment in the core civil service sector.



### Composition by Ministry and Gender

9. **The composition of the civil service by ministry is uneven, with four ministries accounting for around 60 percent of the total number of filled positions** (see Figure IV.2). The four ministries with the largest employment shares are as follows: Health (18.8 percent), Information and Communications (14.6 percent), Forest and Soil Conservation (12.9 percent), and Agriculture (12.8 percent). The relative sizes of the Ministry of Health and Ministry of Agriculture are hardly surprising and can be justified by the health care needs of the population and the dominant role of agriculture in the economy. However, the case for high employment numbers in the Ministry of Information and Communications and Ministry of Forest and Soil Conservation is not as clear, especially since more than 50 percent of the employees in these two ministries (over 70 percent in the case of Information and Communications) hold classless positions such as peons, drivers, etc.





10. **Few women are employed in the core civil service.** The sample results indicate that only 7 percent of the core civil servants in Nepal are female. Almost 50 percent of the female civil servants are working in the Ministry of Health. However, the proportion of women working in lower-grade positions is comparable to that of men.

### Compensation

11. **The compensation in the civil service in Nepal is heavily compressed, leading to incentive problems.** The compression ratio (defined as the ratio of highest to lowest paid) in the Nepalese core civil service is 3.6 (for salary) and 3.3 (for total net compensation), which means that a ministry secretary is paid only three and a half times more than a peon in the same ministry.<sup>43</sup> This ratio is low compared to other developing countries. For example, the compression ratio in Bangladesh is 10.<sup>44</sup> As a consequence of the compressed compensation structure in Nepal, civil service employees do not have sufficient incentives to perform well, leading to low quality of service provision and, possibly, even corruption.

### Pension Liabilities

12. **Expenditures for the unfunded civil service pension system have grown in recent years, following an increase in civil service wages and an implementation of a voluntary early retirement scheme (VERS).** Total pension expenditures, which also include army and

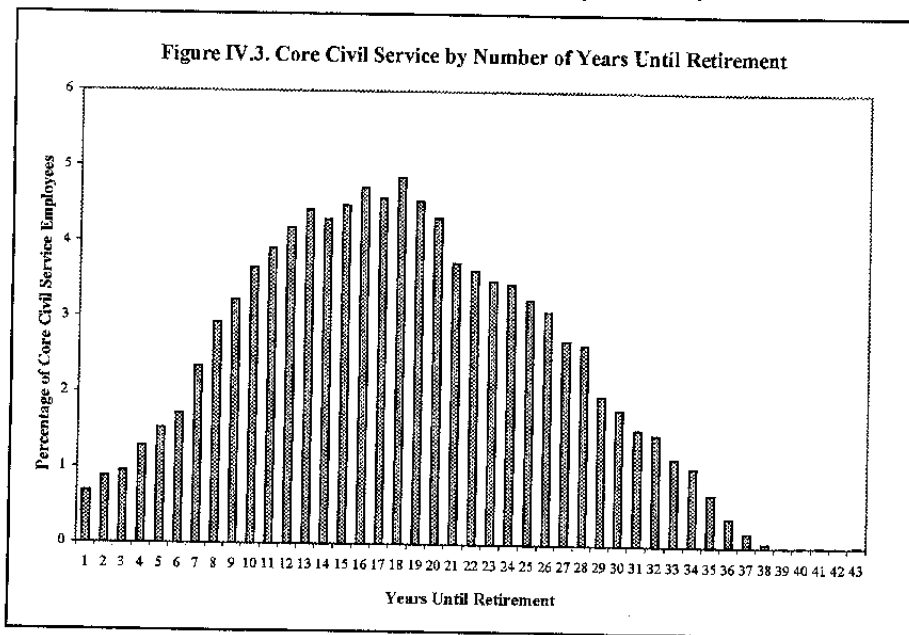
<sup>43</sup> Staff estimates.

<sup>44</sup> See footnote 41.

police pensions,<sup>45</sup> have risen from an average of 0.3 percent of nominal GDP between 1997/98 and 1999/2000 to 0.5 percent of nominal GDP in 2000/01 and an estimated 0.7 percent of nominal GDP in 2001/02. An increase in civil service wages in mid 2000 (discussed in Section D) led to a rise in pensions by two thirds of the pay increase for the corresponding employment grade. In addition, the implementation of a VERS in 2000/01 (also discussed in Section D) increased the number of retirees, thus contributing to the rise in pension outlays.

13. **Due to structural factors, the number of core civil service retirees is expected to rise substantially in the next decade, increasing the pension liabilities of the system.** More specifically, the core civil service is aging, partly owing to the hiring freeze policy implemented in recent years. This aging problem is illustrated in Figure IV.3, which shows

what percentage of the current core civil servants is expected to retire in each year of the following four decades. The distribution in Figure IV.3 is skewed to the left, suggesting that a disproportionately large part of the core civil service (approximately 60 percent of the employees) is expected to retire



within the next 20 years. In addition to the aging factor, the steady increase in life expectancy in Nepal—including that of core civil servants—would lead to higher pension liabilities in the future.

#### D. Reform Initiatives

14. **To address the problems in the civil service, the authorities have embarked on a civil service reform, partly with AsDB technical assistance under a Governance Reform Program (GRP) initiated in 2001.** The general goals of the GRP are to improve the efficiency of the civil service; to enhance the competence and motivation of civil servants; to

<sup>45</sup> The breakdown of civil service pension expenditures by employment category is not available. Consequently, part of the increase in pension outlays may be explained by developments outside the core civil service.

develop internal capacity for reform; to reduce corruption and improve governance; and to establish a process for improving the performance of key ministries.

15. **The authorities have undertaken or are planning to undertake the following policy steps to reform the civil service.** Measures to reduce the size of civil service employment include *eliminating vacant positions, implementing a voluntary early retirement scheme, maintaining a hiring freeze, and rationalizing the administrative structure.* The initiatives to improve the structure and composition of the civil service comprise *reducing the overstaffed lower grades and implementing an affirmative action program.* Plans for *payroll and pension reform* in the core civil service are being considered as well.

#### **Elimination of Vacant Positions**

16. **The elimination of vacant positions is important to the permanent reduction of the civil service size.** As mentioned in paragraph 7, the number of vacancies is about 17,000, i.e., 16 percent of the core civil service. Although these positions are currently vacant, the risk that they will be filled remains, unless the positions are eliminated.

17. **Unfortunately, progress in eliminating these vacancies has been slow as a result of ministry resistance.** For example, a proposal to eliminate vacant positions in three lead offices (Ministry of Finance, National Planning Commission, and Ministry of General Administration) was submitted for cabinet approval in 2001. In practice, only a small fraction of them has been eliminated so far. This lack of progress is mainly owing to the reluctance of ministries to provide information about their vacancies. According to the current Civil Service Act, a vacant position can be abolished if it is not filled within a year. However, ministries have hindered the elimination process by not disclosing which positions have been vacant for more than one year. In order to allow for more flexibility in this area, the authorities intend to change the Civil Service Act by July 2003.<sup>46</sup>

#### **Voluntary Retirement Scheme**

18. **To reduce the size of the core civil service, a pilot VERS was initiated in 2000/01.** The notification for the scheme appeared in the press in September 2000. The eligibility requirements included 20 years of continuous service and 50 years of age. The total number of applications was about 2,600, of which close to 2,300 were approved. The VERS benefits included a lump-sum pension advance, fixed medical allowances, accumulated home leave, and accumulated sick leave.

19. **The scheme was discontinued due to its excessive cost and limited success in removing low-grade and low-productivity staff.** A consultants' report for the Department for International Development (DFID) estimated that the cost per retiree—between Nr 205,000

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<sup>46</sup> However, this amendment to the Civil Service Act has not been drafted yet.

and Nr 444,000—was high by international standards.<sup>47</sup> In addition, anecdotal evidence suggested that many of the employees who took advantage of the early retirement scheme were likely to be among the high-grade and high-productivity staff.

20. **Given the experience with the pilot VERS, the authorities have decided to re-evaluate the design of the scheme before proceeding further.** A report—soon to be finalized—is supposed to present different options for an affordable and viable retirement scheme. The Cabinet is expected to approve the revised VERS before July 2003.

### **New Hiring**

21. **New hiring has been limited, in order to constrain the size of the core civil service.** The policy of no new hiring has begun to be implemented, as suggested by the results of the civil service census. For example, only about 850 of the 67,333 civil service employees in the sample were appointed in 2000. Compared to the previous year, the new hires in 2000 were about 60 percent fewer. This policy is expected to be maintained and enforced during the reform period.

### **Administrative Structure Rationalization**

22. **Another reform initiative focuses on rationalizing the administrative structure of the core civil service; however, progress in this area has been limited.** The rationalization involves streamlining the number of ministries and eliminating duplicate positions within and across ministries. Some positive steps were taken in 2000—the reduction in the number of ministries from 26 to 21 and the elimination of duplicate positions in several ministries, for example. However, this progress was undone in the following year, when the number of cabinet ministers increased to 40. Currently, a proposal to reduce the number of ministries and eliminate the duplication of positions has been submitted to the Cabinet and is awaiting its approval.

### **Reduction of Overstaffed Lower Grades**

23. **The reduction of the overstuffed lower grades has been planned, but is yet to be implemented.** As illustrated in Section C, the composition of the filled positions is heavily skewed toward the lower grades. This problem was also identified in the report of the Public Expenditure Review Commission (PERC) in 2001, which recommended that low-grade staff positions be eliminated as soon as they become vacant and that some services be contracted to the private sector. Another proposed way of reducing the overstuffed lower grades is through devolution to the local authorities. However, the implementation of this option may cause

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<sup>47</sup> Report by Oxford Policy Management, prepared for DIFD in 2001.

serious problems by shifting the burden to local governments.<sup>48</sup> A manual, summarizing the proposed procedures for eliminating lower grade positions, has been prepared by the Ministry of General Administration. However, the document is still not operational, as it awaits Cabinet approval.

### **Affirmative Action**

24. **An affirmative action plan is being developed in order to increase the number of women in the civil service.** The Cabinet is expected to approve the plan in the following months. The procedures for the implementation of the affirmative action program, including gender-sensitive recruitment measures, are scheduled to be introduced by July 2003.

### **Payroll Reform**

25. **The changes to the compensation structure that were implemented in mid 2000 lessened the degree of wage compression, but increased the core civil service wage bill.** In particular, the basic salary of civil servants was increased and some allowances were eliminated. The pay increases varied with the employment grade. For example, the basic salary of a ministry secretary and a peon rose by 100 percent and 50 percent, respectively. As a result, the core civil service compression ratio—the ratio of highest to lowest paid—increased from 3.1 to 3.6 for salary and from 2.9 to 3.3 for total net compensation, thereby improving the incentive structure in the sector.<sup>49</sup> However, the fiscal cost of this initiative was high—the wage bill of the core civil service increased from Nr 7,124 million in 1999/2000 to Nr 11,312 million in 2000/01 (as a percentage of nominal GDP, the wage bill rose from 2.1 percent in 1999/2000 to 2.8 percent in 2000/01).

26. **To enhance further the performance incentives of civil service employees, the authorities plan to implement payroll reform in the near future.** The introduction of a new salary structure (to be approved by the Cabinet by July 2003) is expected to decompress wages further. Another element of the payroll reform is linking employees' pay raises to their performance, which would be evaluated through an annual review process.

### **Pension Reform**

27. **The authorities have taken first steps toward reforming the civil service pension system.** The transition from unfunded to a funded pension system was among the key recommendations of the 2001 PERC report. Details of the arrangement were provided in the

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<sup>48</sup> Since the fiscal accounts of local governments are largely unreported, the overstaffing problem at the local level may be hidden and difficult to monitor.

<sup>49</sup> Staff estimates.

report as well.<sup>50</sup> Following these recommendations, the authorities have announced plans to establish a pension plan covering the pension liabilities of new entrants to the civil service.

### E. Policy Conclusions

28. **The main lessons from examining the issues and reform initiatives in the core civil service in Nepal can be summarized as follows:**

- **Given the bottom-heavy structure of the core civil service, reductions in employment should target the elimination of lower-grade—filled and unfilled—positions.** For example, the new VERS could incorporate better participation incentives for lower-grade staff. In addition, the planned elimination of vacant positions across ministries could start with the lower grades. The prompt implementation of the initiative to contract filled lower-grade positions to the private sector would help alleviate the problem as well.
- **The reform of the compensation system should be implemented taking into consideration the fiscal cost of the initiative, as well as its impact on voluntary retirement for lower-grade staff.** Unlike the decompression of the compensation structure in 2000, which involved wage increases for civil servant of *all* grades, the new initiative should focus on improving the relative pay of skilled and professional staff. Otherwise, the incentive for lower-grade employees to take advantage of early retirement schemes would decline. In addition, the fiscal cost of the payroll reform could soar, given that lower-grade staff account for a large part of total core civil service employment.

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<sup>50</sup> See Chapter 6 of the 2001 PERC report.

### **References**

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Oxford Policy Management Report prepared for DFID, 2001.

## V. MICROFINANCE AS A POVERTY ALLEVIATION TOOL IN NEPAL<sup>51</sup>

### A. Introduction

1. **Poverty reduction has been a key objective of the government and donors in Nepal.** Poverty incidence is higher in rural areas, and highest in the remote areas of the mid-and far-western regions and the northern mountain belt. The rugged geographical terrain and low population density in remote areas complicate the delivery of public services and development of commercial activity.

2. **The government and donors have supported microfinance as a key tool in fighting rural poverty for the last three decades.** A range of institutions and programs provide microfinance services in Nepal.<sup>52</sup> What distinguishes microfinance institutions (MFIs) from conventional banking activity is their commitment to providing financial services to poorer households and microenterprises. Such households often lack negotiable assets to use as collateral, represent higher risk, and require substantially higher operational costs. Innovative schemes are utilized by MFIs worldwide to overcome these obstacles.

3. **The primary justification for government intervention in directing credit to, among others, the poor lies in asymmetric information in capital markets.**<sup>53</sup> Banks' reluctance to lend to the poor is often due to lack of information on the borrowers' ability to pay. In addition, they are often restricted from charging the higher interest rates needed to overcome higher risk and the cost of servicing clients in remote areas. Government intervention can help in overcoming these informational asymmetries either through start-up subsidies or targeted and transparent interest rate subsidies.

4. **MFIs have had mixed success world-wide with respect to sustainability and impact on the poor, but there is now an emerging consensus on best practice.** The failures have to do with poor program design, skill limitations, faulty implementation, and inadequate incentives and accountability. Political interference leads to waste and substantially reduces incentives for MFI sustainability. A number of academics and donors have analyzed the impact on the poor to determine how best to apply short-term subsidies, if needed, without interfering with the objective of sustainability. There is an emerging consensus as to what constitutes more effective design and the optimal role of donors and government support. Nepal could apply more of this consensus in its policy making.

5. **Moreover, there is a growing recognition that microfinance may not be the best form of government intervention to assist the poorest.** Borrowing by the hard-core poor,

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<sup>51</sup> Prepared by Wafa Abdelati (APD).

<sup>52</sup> Microfinance consists of microcredit, savings schemes, and insurance services.

<sup>53</sup> Calomiris and Himmelberg (1993). See also Hardy, Holden and Prokopenko (2002).



and destitute groups in severely disadvantaged rural areas, could lead them to become debt ridden without improving their prospects. In the absence of basic infrastructure and access to market services and opportunities, alternative intervention mechanisms may be better suited to expand the economic options of the hard-core poor.

6. **This paper explores the effectiveness of MFIs in Nepal** drawing on recent studies in Nepal and elsewhere. Section B reviews the sector's institutional setup and the role of the central bank and commercial banks. Section C discusses the effectiveness of programs in Nepal in reaching the poor and achieving sustainability. Section D outlines lessons learned about best practice design for MFI and reform efforts in the sector. Section E concludes.

### **B. The Microfinance Sector in Nepal**

7. **There are three types of MFIs in Nepal—informal, private and public—and the central bank plays a key role in the sector.**<sup>54</sup> The informal sector consists of money lenders, pawnbrokers, and savings and credit groups. The formal sector consists of government-owned institutions and private-owned institutions, including local NGOs. There are also a number of international NGOs and sector associations that provide support services and grants. In addition, the central bank plays a key role in the promotion and development of microfinance.

#### **Main microfinance institutions**

8. **In the informal sector, traditional money lenders are increasingly replaced by thousands of unregistered groups engaged in microfinance.** The traditional rotating saving and credit associations (ROSCs) are community-based groups referred to in Nepal as “Dhikuties”, typically with 20-50 members contributing an equal amount of Nr 10-100 that are lent out on rotation. In addition, tens of thousands of newly formed unregistered savings and credit groups (SCGs) of 5-25 members rely on member funding, but these do not operate on a rotating basis. Lending interest rates of village money-lenders are reported to be between 35-60 percent, while those of SCG are 24-36 percent.

9. **Formal arrangements with public support began in the late 1960's.** Public sector institutions, accounting for over one half of microcredit, consist of the Agricultural Development Bank of Nepal (ADBN), the five regional development banks (RRDBs) and the Rural Microfinance Development Corporation (RMDC). The ADBN is the 3<sup>rd</sup> largest deposit taking institution, established in 1968, to provide agricultural and rural credit. It operates a commercial wing and an agricultural development wing, in addition to managing the Small Farmer Development Program which targets low income farmers. SFDP was launched in 1975, to extend credit to the poorer farmers on a group-guarantee basis. It has 380 offices serving 600 of the 4,000 Village Development Committees (VDCs) areas in the country. The

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<sup>54</sup> See World Bank (2002) for a detailed description of microfinance institutions and Annex Box V.1 for an overview of institutional programs.

five RRDBs were established between 1992 and 1996 and cover about 40 out of 75 districts. The RMDC was established in 1998 to act as an apex institution to distribute donor funding and provide training and other support services.

10. **Most of the formal private sector is dependent on some form of public or donor support.** The largest two institutions, Nirdhan and the Center for Self-Help Development (CSD), receive funding and technical support from donors. Both were registered under the Society's Registration Act (SRA) as NGOs, but transformed to development banks partly to facilitate savings mobilization. NRB has licensed a total of 25 NGOs and 34 cooperatives for providing financial services. Several microfinance development banks have only started operations in 2002, with some forty additional applications pending approval. There are many smaller microfinance institutions. An unknown number of the estimated 25,000 NGOs registered under the SRA are engaged in microfinance; of these, about 70 receive some form of NRB support. An estimated 2,000 out of 6,000 cooperatives registered under the Cooperatives Act operate as savings and credit institutions.

#### **Involvement of NRB and commercial banks**

11. **NRB has had a dominant and growing role in the promotion and development of microfinance in Nepal.** From its inception in 1956, NRB's mandate included the delivery of credit to the rural poor.<sup>55</sup> NRB's promotional role includes encouraging the establishment of coops and NGOs, and in recent years, development banks.

12. **NRB has also supported microfinance programs in several direct ways.** Its involvement has included equity participation, program administration, management, board representation, guarantees, refinancing, and directed lending (Annex Table V.1) NRB has provided refinancing from donor funds to the two largest commercial banks for a number of development programs, including two gender-based programs and irrigation and livestock projects (Annex Box V.1.). It also administers the government-funded Rural Self-Reliance Fund which provides funds at 6 percent interest to registered coops and NGOs for on-lending to micro-entrepreneurs.

13. **NRB is an equity shareholder in a number of microfinance institutions,** including the Credit Guarantee Corporation (CGC), the five RRDBs and RMDC. CGC is majority owned by NRB and is to absorb 75 percent of the risk incurred by banks in lending to priority sectors. Although banks have rarely filed claims, this remains a significant contingent liability. NRB is also a majority shareholder in the RRDBs and most of the senior managers were, until this year, NRB officers. It also holds 26 percent of the equity in RMDC.

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<sup>55</sup> The new NRB Act (2002) gives prominence to macroeconomic objectives and safeguarding the health of the financial system but it does not shed the developmental role.

14. **By NRB directive, commercial banks are required to provide microfinance.**<sup>56</sup> priority sector lending was introduced in 1974, and initially required all commercial banks to lend 5 percent of their “loanable funds” to priority sector borrowers, i.e., small borrowers in agriculture, cottage industries, and services. Later, this amount was increased to 7 percent, and then to 12, percent. One quarter of priority sector loans must go to the poor referred to as “deprived sector” in amounts up to a maximum of Nr 30,000 (\$375) per borrower.<sup>57</sup> The definition of priority sector and limits have been gradually relaxed. To satisfy the priority sector lending requirement, banks provide equity participation in RMDC and on-lend funds they cannot invest directly in small loans to the RRDBs and other MFIs.

### C. Effectiveness of Microfinance Programs in Nepal

15. **There has been a growing recognition that microfinance has not developed into the hoped-for panacea for poverty alleviation.** This section outlines the sector’s main weaknesses and summarizes available information on its effectiveness in terms of (i) outreach, (ii) targeting, (iii) sustainability, and (iv) the regulatory and supervisory framework. Although quantitative analysis is limited, a number of recent donor-supported studies provide partial assessments.

#### **Outreach—proportion of the poor served**

16. **The microfinance sector remains relatively small in Nepal.** After decades of promotional and developmental activities, microcredit accounts for less than 5 percent of total credit and of total deposits (Annex Table V.2, Figures V.1, and V.2) Microfinance services have increased at a relatively slow rate in spite of the rapid increase in a number of institutions.

17. **There remains considerable unsatisfied demand for micro-credit in Nepal.** Estimates vary widely in terms of both the size of effective demand and actual microcredit outstanding and to date there has been no in-depth study of demand, outreach and targeting.

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<sup>56</sup> The Priority Sector Credit Manual, NRB (July 20002) stipulates that commercial banks “provide micro-credit for the purpose of operating self-employment oriented industries and business to deprived and low-income people and particularly those socially backward women, tribes and low caste as well as motivated and energetic blind, hearing-impaired and physically-handicapped people and squatters families” and that “efforts shall be made to provide the customers with necessary technical skills, marketing and other facilities and subsidies”.

<sup>57</sup> Relaxation of the priority sector lending requirements is discussed further below. NRB introduced the “Intensive Banking Program” in 1981 whereby the two state-owned banks and the first joint-venture bank, Nepal Arab Bank Ltd (NABIL) were to meet specific rural lending targets through group-based lending and without collateral requirements. This program continues to be part of the priority sector lending program. NRB (2002).

An NRB study estimated effective demand at Nr 18 billion in 1999 (½ percent of GDP). An AsDB study estimates effective demand for microcredit at around Nr 10 billion in 1998, compared to an estimate of Nr 4 billion in outstanding microcredit at the time and total outstanding loans of commercial banks of Nr 70 billion.<sup>58</sup>

**18. Program outreach is lower than in other countries and lower in the poorer regions of the country.** The World Bank estimates that while on average 30 percent of the poor in Nepal have access to microcredit, only about 15 percent of those living in the hills have access to microcredit. This compares to 60 percent access in Bangladesh. Outreach is much higher in the southern and eastern Terai, where there is easier accessibility.

#### **Targeting the poor and hard-core poor**

**19. Not all microfinance programs were designed to target the poor.** Besides poverty alleviation, the government aims to facilitate microcredit schemes for cottage industries, export finance, and rural finance. Unlike other countries, there has been no study dedicated to identifying the income levels of microfinance borrowers and the impact of microfinance on their income. The largest program, the directed priority sector lending of commercial banks, is not targeted to the poor. There are no income tests for loans classified as part of priority sector lending, and the current limit of \$375 for the deprived sector lending is substantially higher than Nepal's per capita income level. This suggests that less than 25 percent of total priority sector lending goes to the poor.<sup>59</sup>

#### **Sustainability**

**20. The majority of programs report a high repayment rate but nearly all are accumulating losses.** Many programs report repayment rates of 95-100 percent. The publicly funded SFDP program has the lowest reported recovery rate, of around 50 percent. But a high repayment rate does not ensure financial viability because of the extremely high operating costs, typical of MFIs worldwide. The low interest rates charged in Nepal preclude coverage of operating costs. Moreover, there are few incentives to minimize operating costs. The RRDBs have high transaction costs due to a complex organization, bloated staff, and unspecialized management. Four of the five banks have had their equity eroded by losses. Recent reviews found that virtually no institution has achieved financial sustainability and all are dependent on grants and/or eroding their capital.

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<sup>58</sup> Sinha (1999). This was based on assumed demand from 2 million families for credit of about \$73 per household.

<sup>59</sup> Outside the deprived sector, the limit ranges from \$25,000 for agriculture to \$250,000 for hydropower projects.

21. **The price of micro-credit is very low in Nepal and is an important impediment to financial viability.** MFIs around the world typically charge high interest rates, often in the range of 30-50 percent per annum. Self-sustaining MFIs charge higher interest rates than the average for all MFIs.<sup>60</sup> This is because operating costs typically amount to 30 percent of the value of assets, with two thirds going to pay for salaries. Microfinance credit rates in Nepal range from 2-25 percent per annum.

**22. NRB's policies contribute to repressively low interest rates.**

Although the provision of low cost credit is not a stated objective of the NRB, it is a de facto outcome of its various interventions. The effective interest rate on lending from

RSDF is as low as 2 percent per annum; it lends to NGOs and coops at the low interest rate of 8 percent per annum, with a 6 percent rebate for on-time repayments. The Financial Intermediary Society's Act (FISA) gives NRB the right to review and alter the interest rate charged by NGOs engaged in micro-finance. The RRDBs generally charge around 10 percent interest on loans. Commercial banks who provide funding to microfinance institutions to meet their priority sector requirement are obliged to maintain low interest rates in order to maintain a reasonable repayment rate and compete with the low rates charged by the state-owned RBB and NBL to the same institutions.

**Regulation and supervision**

23. **MFIs' effectiveness is limited due in part to overlapping legislation,** including the Development Act, the Cooperatives Act, and Society's Registration Act. Coops and NGOs, even those that are also NRB-licensed, cannot accept public deposits. All microfinance NGOs are governed by FISA. Until the recent 2002 amendment, the Act assigned NRB the responsibility for the repayment of loans by the approved MFIs in case of the default of the

Outreach and Reported Loan Recovery of Main MFIs  
(In millions of Nepalese rupees, unless otherwise stated)

	Loans	Borrower	Average Loan Size (In thousands of Nepalese rupees)	Districts Covered	Recovery Rate	Model 1/ Target Group
<b>Public sector 2/</b>						
SFDP (1975)	1,600	210,000	7.6	75	<50	conv. Farmers, per capita income <Nrs 2500
PCRW (1982)	186	66,718	2.8	55	64	conv. Poor women with projects
RRDB (1992-97) 1/	290	52,566	5.5	...	99	group. Poor borrowers
RRDB (1992-97) 2/	718	119,732	6.0	38	...	group. ...
Eastern	251	44,281	5.7	...	99	group. ...
Western	200	30,415	6.6	...	100	group. ...
Central region	84	18,150	4.6	...	100	group. ...
Far Western	96	11,895	8.1	...	86	group. ...
Mid Western	88	14,991	5.9	...	97	group. ...
MCFW (1994)	116	5,700	20.4	12	83	conv. Poor women with projects
Public sector total 2/	2,192	335,014	6.5			
<b>Private sector 3/</b>						
Registered coops	243	81,283	3.0	...	...	group. Members
Mirdhan	120	26,618	4.5	...	100	group. Poor borrowers
CSD	154	29,370	5.2	...	100	group. Poor borrowers
SFCL	726	55,000	13.2	...	58	group. Farmers, per capita income <Nrs 2500
SAPROSC	6	12,000	0.5	...	...	...
DEPROSC	20	14,000	1.4	...	...	...
Others (estimate)	33	50,000	0.7	...	...	...
Private sector total 3/	1,301	288,273	4.9			
<b>Memorandum items:</b>						
Informal coops	997	802,000	1.2	75	...	group. Farmers
Priority sector 4/	13,194					

Sources: Sinha (1999), based on mid-1997 data; and World Bank (2002).  
 1/ Conventional model of lending (based on collateral) or community based group lending model.  
 2/ Based on AsDB's Sinha (1999) study estimates.  
 3/ Based on WB (2002) study estimates.  
 4/ 12 percent of commercial banks' lending portfolio in January 2002.

<sup>60</sup> Hardy, Holden and Prokopenko (2002).

organization, and in exchange it requires the organization to seek prior NRB approval for each loan or grant received by the MFI. Amendment to the Cooperatives Act and the Development Act are under consideration, and these will hopefully set clear and consistent guidelines for MFIs.

24. **At this time, regulation is limited to NRB licensed MFIs and a supervisory framework is largely lacking.** In practice, the application of the regulations to NRB-licensed NGOs and cooperatives is perfunctory and the large number of MFIs remain outside the scope of NRB regulation and supervision. NRB does not have the capacity to collect and review financial data and effectively supervise these institutions.

#### **D. Lessons Learned and Reform Initiatives**

25. **Weak performance results from the sector's ad-hoc development with overlapping objectives and institutional roles.** Programs simultaneously target agricultural credit, export and microenterprise finance, and poverty alleviation. NRB's direct involvement in the sector is inconsistent with its supervisory role. No distinction is made in program design between the needs of different target groups (poor households, farmers, microenterprise, exporters, and hard-core poor) and the financial services best suited to them. There has been no stated NRB policy that explains the shift away from issuing licenses for coops and encouraging new development banks. A large number of MFIs fall outside any regulatory or supervisory framework.

#### **Best-practice program design considerations**

26. **There is broad consensus on best practice in MFI design.** Successful programs are those that achieve sustainability, greater outreach, and higher income impact. These three objectives have implications for the role of state-owned development banks and commercial banks, for the role of public and donor support, and for optimal regulation.

27. **The key features of programs that have achieved financial sustainability are:**

- **repayment incentive structures.** Material incentives to borrowers and lending staff help to maximize repayment. Also, group-based lending and more intensive collection of loans repayments increases the repayment rate.
- **market-based pricing.** Higher interest rates ensure sustainability and weed out low-return projects and less-poor borrowers who have access to other sources of finance.

- **cost containment.** A lean structure, skilled staff, accountability, and innovative schemes (group self-monitoring) help maintain low operating costs. Larger, more established MFIs on average have lower administrative costs and cost of funds.
- **availability of voluntary savings and insurance facilities.** The potential to mobilize savings also helps to reduce the dependence on public and donor support.

Indicator	All MFIs	Best 1/
Number in sample	148	57
Years of operation	8	11
Total assets (U.S. dollar million)	5.5	21.2
Loan/assets	68	71
Deposits/assets	13.7	53
Borrowing at commercial rates/loans	59.4	96.2
Number of active borrowers	10,710	89,370
Average loan/per capital GDP	46	76.3
Revenue from loans/loans	38.1	41
Inflation-adjusted revenue from loans/loans	28.8	33
Return on assets	-3.7	5.1
Operating expenses/assets	31.2	26.2
Administrative expenses/assets	19.8	17
Interest margin/assets	18.9	24

Sources: the MicroBanking Bulletin, November 2001, reprinted from Hardy et al. (2002).  
1/ Best refers to those that are financially self-sufficient.

28. **Financially sustainable institutions have had a better impact on reducing poverty.**<sup>61</sup> A study of 300 microfinance borrowers showed that the income impact on the poor is higher for the best performing institutions. This has been attributed to the use of best-practice design features where the higher interest rates, more frequent loan installments, and savings programs tend to screen out less-creditworthy borrowers.<sup>62</sup>

### The role of public and donor support

29. **The availability of public funds to bail out loss-making MFIs reduces incentives to achieve self-sustainability.** Support is best provided in the form of training and transfer of know-how. Lack of coordination between government and donor sponsored programs can slow down progress in providing such services to MFIs. One-time start-up grants have also been used successfully to assist in financing equipment and training. If budgetary interest rate subsidies are used to expand coverage to remote areas, they should be limited to covering the cost differential incurred in servicing remote areas by otherwise operationally efficient MFIs. In this case, the subsidies should be transparent.

30. **Alternative intervention mechanisms should be considered for the hard-core poor.** Borrowing by the hard-core poor in severely disadvantaged rural areas, could lead them to become debt ridden without improving their prospects. The remote hills and mountain areas, where 50 percent of Nepalis live, have proven particularly challenging for the delivery of microfinance services. Sustainable microfinance requires the existence of basic

<sup>61</sup> Hulme and Mosley (1996).

<sup>62</sup> Hardy, Holden and Prokopenko (2002).

infrastructure, access to market services and opportunities, and a minimum of entrepreneurial skills. When these conditions are absent, alternative intervention mechanisms may be better suited to expand the economic options of the hard-core poor. These include employment programs, marketing assistance, provision of human capital development (education, training and health services), infrastructure projects (access to roads, water, electricity), and, in some instances, direct income support (micro-grants).<sup>63</sup>

### **The viability of state-owned development banks for microfinance**

31. **Private-owned institutions operated on a commercial basis are more likely to achieve sustainability.** However, reform of state entities may be necessary as a transitional stage until private entities can take over. State-owned development banks tend to be politicized and place greater emphasis on credit flows than on recovery. The most critical factors behind the failure of state-owned DBs in the delivery of microfinance are the lack of political autonomy and the inadequate financial and human capital to carry out their mandate.

32. **Reforming state-owned development banks is a challenging task.** There are few examples of self-sustaining state-owned development banks. The most often cited example is that of Bank Rakyat Indonesia (BRI), outlined in Annex Box V.2. The BRI underwent a rigorous reform program in the mid-eighties as part of deregulation and financial sector reform. Key reforms included staff training and accountability, higher interest rates to allow sustainability and screen out wealthier borrowers, and introducing clear and transparent reporting.<sup>64</sup>

33. **The NRB has recently initiated reforms in ADBN and the RRDBs.** ADBN is undergoing an external audit to determine the operational performance of its commercial and development activities. Being the major shareholder of the RRDBs, the NRB presented a reform strategy in June 2002 that aims to restructure the banks in order to prepare them for privatization within 1-5 years, depending on their financial state. The NRB aims to reduce its share in these institutions to 16½ percent, consistent with the new NRB Act. The strategy focuses on implementation of action plans for each institution to reduce staff, conduct training (through RMDC), select more experienced management, improve loan recovery, and increase transparency of reporting.

### **Why don't commercial banks provide needed microfinance services?**

34. **Commercial banks will voluntarily increase their involvement in microfinance under certain conditions.** Commercial banks' operational designs may be ill-suited for the delivery of microfinance without significant investment in altering their services to cater to small borrowers. The best strategy is to eliminate repressive financial regulations, such as

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<sup>63</sup> Parker and Pearce (2001).

<sup>64</sup> Mukherji (1997) and Seibel (200). See also Annex Box V.1.



interest rate ceilings and targeted credit schemes.<sup>65</sup> This would allow microfinance lenders to compete in open markets, create incentives to reduce operating costs and provide innovative products, and cover their risks and the opportunity cost of capital.

35. **NRB recognizes that the development objectives of the priority sector lending program conflict with the goals of sound commercial banking practices.** NRB officials completed a study of priority sector lending in 2000 to identify the burden on commercial banks and the impact of its removal.<sup>66</sup> The study reported that 60 percent of total borrowers benefiting from priority sector lending programs believed they could find alternative financing through the development banks and other MFIs. Nevertheless, NRB officials concluded that elimination of the requirement should be preceded by the establishment of adequate rural banking institutions and other microfinance programs and that this was likely to require about five years. As a first step, however, NRB reduced the penalty for noncompliance with the priority sector requirement by 25 percent in July 2002. It also announced its intention to remove the penalty entirely within four years.

#### **How much regulation and supervision?**

36. **The rapid spread of MFIs has prompted reconsideration of how they should be regulated.** Regulators must strike a balance between the benefits and costs of regulation, and determine the appropriate degree of regulation depending on the nature and size of an MFI.<sup>67</sup> For small microfinance institutions, non-prudential regulation is sufficient. Non-prudential regulation is that which applies to all business (not only financial sector), and typically includes, registration, account keeping, labor relations, disclosure, and bankruptcy procedures. All businesses, including NGOs, should meet these basic requirements. In the case of donor-funded NGOs engaged in micro-finance, and small savings and credit cooperatives that only cater to members, no other form of supervision should be required.

37. **Larger MFIs that depend on public deposits and borrowing should be subject to stringent regulatory and supervisory scrutiny.** A system of graduated regulation and supervision is required, with guidelines that require MFIs to re-register as they change the nature of their operation or grow in size. Non-donor-funded MFIs that collect non-member deposits represent particular risk as they lack the capacity to augment their capital when needed.

38. **The NRB is preparing new regulations for microfinance NGOs and development.** New directives were recently issued to NRB-licensed cooperatives. A preliminary draft manual has been prepared for inspection of NGOs and of cooperatives. However, NRB officials have

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<sup>65</sup> Baydas, Graham and Valenzuela (1998).

<sup>66</sup> NRB (2000).

<sup>67</sup> Christen and Rosenberg (2000).

expressed their reluctance to take on the role of supervising NGOs and Coops as they consider them too small to be of systemic importance and too many for their limited staff resources. There has been some discussion of the merits of a second tier supervisory institution, but it is not considered a priority reform area. NRB is also considering approval of a proposed National Cooperative Bank to facilitate financing of coops, which would compete with RMDC, and which could take over regulation and supervision of cooperatives.

### **E. Conclusions**

**39. In spite of the priority accorded to microfinance in Nepal, it remains limited in outreach and virtually no institution has succeeded in achieving sustainability.**

Significant steps are required, both in the design and governance of MFIs, as well as in reducing the dominant role of the central bank and commercial banks, if the microfinance sector in Nepal is to achieve its potential. In particular, greater focus is needed on achieving long-term sustainability through market-based interest rates and an incentive structure that reduces operating costs. Extending the outreach of microfinance to the poor and rural communities requires that MFIs are run on financially sound and self-sustaining basis. A supervisory framework must be established with adequate resources and reform of state microfinance institutions should proceed without delay. The elements of NRB's reform strategy are summarized in Box V.1. Donors have a role to play in coordinating their efforts to support this strategy.

**40. Nepal can benefit from lessons learned from other countries' experiences in microfinance.** Short-term public or donor support can facilitate coverage of initial start-up costs and training, and the transfer of know-how, but perceived long term support will reduce efficiency and provide room for waste and mismanagement. Programs that receive public support should be monitored to ensure they target the poor. Any subsidies provided to MFIs will have limited impact on the poor if microfinance programs continue to have multiple objectives, including export finance and microenterprise development. Experiences have also shown that microfinance may not be the best tool to target the hard-core poor and that alternative government interventions should be considered.

### **Box V.1. Key Elements in a Microfinance Reform Strategy**

**A comprehensive micro-finance strategy is being developed in Nepal, in collaboration with donors involved in microfinance.** The strategy needs to include the following elements:

- **Political commitment to best practice for MFI.** For microfinance to be effective, public officials need to be committed to the goals of commercial sustainability and targeting the poor (not the hard-core poor) without political interference. Best-practice MFI designs should be encouraged. Alternative assistance mechanisms need to be considered for the hard-core poor.
- **Change NRB's role.** NRB should provide a conducive environment for MFI development and withdraw its equity participation in MFIs, including RRDBs and refrain from involvement in the administration of and representation in MFIs. NRB could encourage, but not be directly involved in, rating and guaranteeing of MFI activities.
- **Develop supervisory framework.** NRB needs to establish an adequate supervisory framework for larger MFIs while allowing smaller, own-funded, and donor-supported MFIs sufficient flexibility. Compliance with the newly issued regulations should be monitored and enforced. Minimal reporting requirements to NRB and/or the public are needed. If a second-tier supervisory institution is to be developed, this should be initiated without delay.
- **Legislative change.** The legislative framework needs to be rationalized. The by-laws for the FISA need to be modified in line with the 2002 amendment of the Act. Guidelines should be set for the type of financial services and size that require NRB licensing, and those which can be undertaken by entities registered under the Cooperatives or Societies Act.
- **Reform development banks.** NRB needs to demonstrate its ability to effectively supervise existing development banks and to enforce remedial measures on existing ailing institutions.
- **Rationalize public programs and support services.** The multitude of publicly-sponsored micro-finance programs should be rationalized. Programs that target the hard-core poor should be separated from those that target the less poor and small enterprise. Special "microfinance plus" models may need to be developed for hilly regions. Public and donor support for technical assistance, training, and other services should be coordinated with transparent subsidies for income transfer programs. Additional resources will be needed if RMDC is to provide the training facilities for MFIs and to serve as a wholesale institution to channel donor support.

### Box V.1. Microfinance Institutions and Public Programs

- **Informal Community-based Institutions**

- Money lenders and pawnbrokers.
- Traditional rotating savings and credit associations (ROSCA's) include Dhikuties, Dharam Bhakari (grain storage associations), and Guthies (cultural heritage associations).
- New informal savings and credit groups (SCGs). A 1997 survey by the development bank, Deprosc, estimated some 20,000 SCGs serving 320,000 households.

- **Public Institutions**

- Five regional rural development banks (RRDBs) with NRB equity modeled after Grameen banks.
- ADBN established in 1968 to specialize in agricultural and rural credit.
- Rural Microfinance Development Center (RMDC) established in 1999 as a development bank to act as an apex institution for donor funds.
- Small Farmers Development Bank (SFBD) established in 2002 as an apex institution.

- **Private Sector Institutions**

- Center for Self Help Development, (CSD) is the largest private sector MFI, set up in 1991 as an NGO, receives support from Women's World Banking.
- Nirdhan, initially established as NGO, now a development bank, receives support from CGAP.
- Some 25,000 NGOs registered under the Societies Registration Act (SRA) of 1977. The proportion engaged in microfinance is not known. Twenty-five are also NRB-licensed.
- About 2,000 out of an estimated 6,000 savings and credit coops (SCC) registered under the Cooperatives Act. Twenty-eight are also NRB-licensed cooperatives for microfinance.
- An additional twelve development banks with some microfinance activity.

- **Associations and Federations**

- Microfinance Association of Nepal (MIFAN) established in 1999 under SRA.
- Center for Microfinance (CMF), established in 1998 as a USAID project.
- National Federation of Savings and Credit Cooperative Unions Ltd (NEFSCUN) established in 1998 to act as an apex institution for savings and credit coops, and to promote the credit union movement.
- National Cooperative Federation (NCF) registered in 1993 to develop the cooperative movement.

- **NRB-Supported Programs**

- Small Farmer Development Program (SFDP) operated by ADBN since 1981 with refinancing from donor funds and NRB. Under a GTZ-sponsored program, 100 of the 380 SFDP have been transformed into locally managed MFIs with the purpose of becoming self-sustaining.
- Priority Sector Lending (PSL) program, introduced by NRB in 1974, requires all commercial banks to lend 12 percent of their "loanable funds" to priority sector borrowers, and of this one quarter to the "deprived sector", up to a maximum of Nr 30,000 (\$375) per borrower.
- Intensive Banking Program (IBP) introduced in 1981 to target rural finance as part of PSL.
- Production Credit for Rural Women (PCRW) funded by IFAD since 1982, administered through RBB, NBL with support from UNICEF and Min Local Development, has 60,000 borrowers in 36 districts.
- Micro-Credit Project for Women (MCPW) funded by AsDB is an extension of PCRW from 1994-2002 that uses NGOs and coops to carry out work in 12 districts.
- Self-Reliance Rural Fund (RSRF) established by NRB in 1990 to provide funds at 8% interest to NRB licensed MFIs and 70 non-licensed NGOs for onlending to micro-entrepreneurs.
- Banking with the Poor, a program launched by RBB in 1992 and implemented in 20 districts.
- Third Livestock Development Program, launched in 1999/2000 with AsDB support, operating in 26 districts. The program provides participating banks with NRB refinancing at 6 percent rate.
- Community Underground Irrigation Project with AsDB support, with refinance facilities at 5 percent.
- The Poverty Alleviation Fund (PAF) established in 1999 but has not yet received any donor funding. PAF is expected to have a microfinance component.

### **Box V.2. Country Experiences**

#### **Unit Desa of Bank Rakyat Indonesia**

**The Unit Desa system is a unique example of a successful public-owned rural finance development bank.** The Unit Desa or village banks were established in 1984 as a separate profit center within the Bank Rakyat Indonesia. The system is based on a large network of village units (over 4,000) and relies heavily on village agents that have substantial knowledge and access to information on borrowers. The Unit Desa also provide a wide range of financial services, including flexible savings schemes, convenient banking hours, and a range of incentives including bonuses.

**The system was aimed at the replacement of directed credit to agriculture by broad based credit for any kind of rural activity.** The focus was not limited to targeting the poor but to increase access of financial services in rural areas. The system has been profitable with both low-income and more conventional loans. Profitability is promoted through an incentive structure that links staff compensation to loan recovery with penalties for default and a low base salary and large potential incentive payments.

**The success of the system has resulted in a significant increase in the use of financial services by the poor.** Deposit mobilization has been especially successful and this has made the system independent of state or other donor funds. New branches receive a one-time capital subsidy to assist in equipment and set-up costs.

#### **Banco del Trabajo in Peru**

**The success of Peru's Banco del Trabajo is based on the availability of an active credit information system.** A computerized information system on VAT payments, including in the informal sector, was made available to commercial banks to identify creditworthy prospective borrowers. The Superintendency of Banks also compelled commercial banks to make available information on credit histories to their customers, and this assisted in the establishment of three credit bureaus. The credit information system has assisted the development of commercially-oriented microfinance lenders, including the Banco del Trabajo.

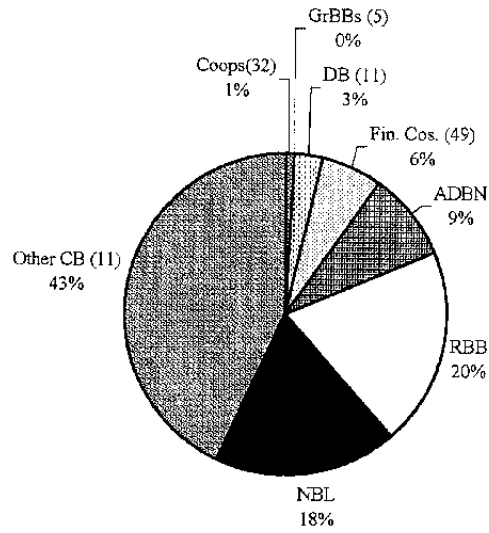
**The Banco de Trabajo has earned returns on equity and assets that are above the average for commercial banks in Peru.** The bank focuses exclusively on small borrowers (average loan size of \$400) and makes about 20,000 loans per month. The portfolio is split between consumer credit and microenterprise loans, and the interest rates charged are between 50 and 50 percent on an annual basis (compared to a discount rate of 14 percent). It has developed a computerized credit rating system that allows decisions on loan applications to be made within 48 hours and which appears to predict the likelihood of repayment with a high degree of accuracy. Default rates are reported to be below 4 percent. A significant proportion of the loan portfolio is unsecured, and all loans include life insurance on borrowers so that the loan can be repaid in the even of death.

#### **Grameen Banks in Bangladesh**

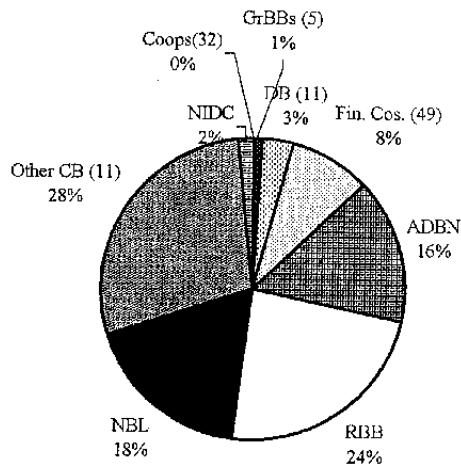
**A recent study evaluating the Grameen Banks suggested that the impact of programs is substantially overstated.** The programs provide loans to households who own less than ½ acre, with innovative loan schedules. Programs served 4 million poor and are reported to have been quite successful. In earlier studies, the that top quartile of borrowers from the Grameen Bank were found to consume 15 percent more and have almost twice as high proportion of sons in school and much higher proportion of daughters compared to the bottom quartile. However, an evaluation based on a survey of 1800 households in 87 villages, surveyed three times between 1991-92 suggests these early results were over-stated. In particular, the study found that impact is significantly greater for the less poor borrowers. One implication has been that programs should target borrowers that are immediately above the poverty line.

Figure V.1. Nepal: Distribution of Deposits and Credit, 2001

**Distribution of Deposits**



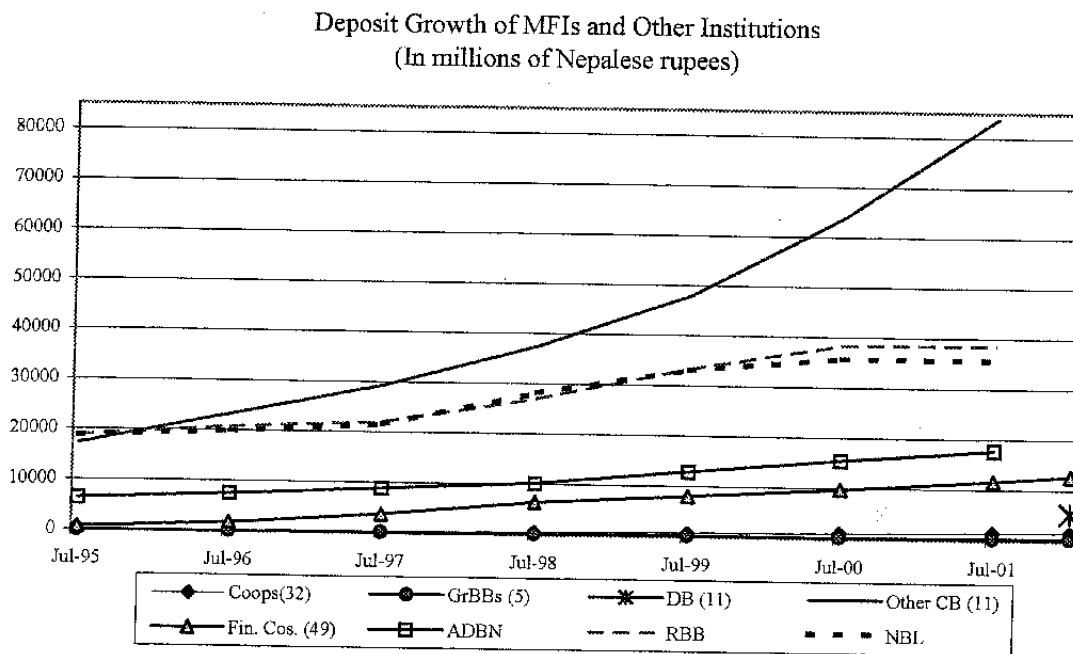
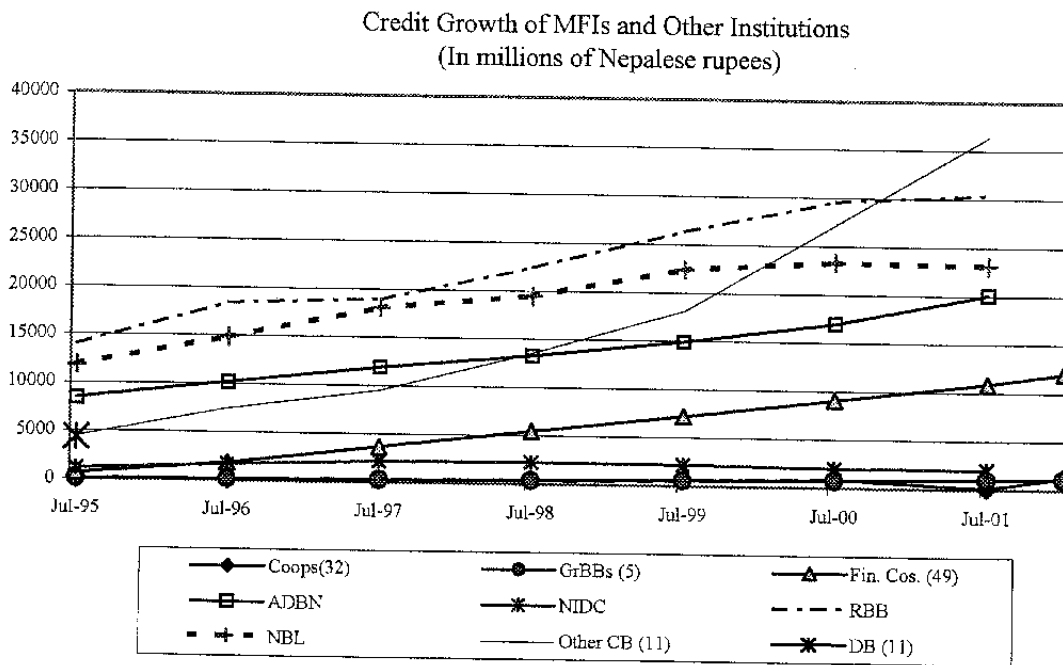
**Distribution of Credit**



Coops(32)	GrBBs (5)	DB (11)
Fin. Cos. (49)	ADBN	RBB
NBL	Other CB (11)	NIDC

Source: NRB - Nonbank statistics.

Figure V.2. Nepal: Deposit and Credit Growth, 1995-2001



Source: NRB, Non-bank Financial Statistics Bulletin.

Table V.1. NRB's Role in the Development of Microfinance in Nepal

Year	Institution	Legislation or Program	NRB Role	Commercial Banks	Government Role	Honors	Private Sector
1956	First credit cooperatives				Provided support through the Cooperatives Fund		member deposits
1963	Cooperative Bank (later became ADBN)				Fully state-owned		
1968	Agricultural Development Bank of Nepal (ADBPN)		NRB refinancing		Fully state-owned	AsDB financing	
1974		Priority lending directives to commercial banks	Directed by NRB, NRB guarantees 76 percent of bad loans				
1974	Credit Guarantee Corporation (GCC)		NRB owns 58 percent				
1975	Small Farmer Development Program launched within ADBN.						
1978		Society Registration Act (under which some NGOs established)					
1979	Department of Cooperatives						
1981		Intensive Banking Program (IBP) by RBB, NBL and NABIL	NRB guarantees default, monitored and supervised by NRB				
1982		Production Credit for Rural Women (PCRW)	NRB provides refinance from IFAD	RBB, NBL, ADBN given lending targets	MoLD program	UNICEF involved	
1991		Rural Self-Reliance Fund	NRB funding			Government funding Nrs 20 million	On-lending through NGOs and Coops
1992-97	Five regional development banks		NRB holds 67% of equity	23 percent of equity	10 percent of equity		
1992		Cooperatives Act					
1994		Micro-credit Project for Women (MCPW)	NRB provides refinance from AsDB funds		MoLD program	Supported by AsDB	NGOs utilized as intermediaries
1996		Development Bank Act					
1998		Financial Intermediary Societies Act					
1999	Establishment of RMDC		26 percent of equity, provides refinancing from AsDB funds	40 percent of equity			27 percent of equity, onlending through NRB-licensed NGOs, RRDB and coops
1999-02	Licenses granted to ten more development banks, and some 40 applications are pending						
Memorandum items: main banking developments							
1937	Nepal Bank Limited (1st commercial bank) was established						
1956	NRB (central bank) established						
1956	RBB (2nd commercial bank) established						
1984	Commercial Bank Act						

Sources: Sinha (1999), and NRB.



Table V.2. Growth of Financial Institutions Since 1995

	Jul-95	Jul-96	Jul-97	Jul-98	Jul-99	Jul-00	Jul-01	Jan-02
<b>Number of MFI</b>								
Development banks	2	2	2	2	5	7	9	10
Rural MF DBs	4	5	5	5	5	8	8	10
S&C coops	8	13	19	29	35	35	34	34
FI-NGO's	0	23	29	34	30	10	15	16
Total	14	43	55	70	75	60	66	70
<b>Memorandum item:</b>								
Finance Companies	20	34	41	43	45	46	48	49
<b>Growth of deposits and loans</b>								
<b>Coop Societies (32)</b>								
Deposits (Nrs mn)	57	122	267	468	714	1073	1425	1475
Loans	59	117	244	406	591	875	122	1272
<b>Grameen Vikas Banks (5)</b>								
Deposits	3	34	62	100	156	218	283	291
Loans	99	168	260	374	556	733	1000	1050
<b>Microfinance NGOs (13)</b>								
Borrowings	...	...	...	...	...	...	...	16
Microcredit extended	...	...	...	...	...	...	...	16
<b>Other development banks (11) 1/</b>								
Deposits	...	...	...	...	...	...	...	5280
Loans	...	...	...	...	...	...	...	4389

Source: NRB-Nonbank Financial Statistics, 2002.

1/ The 11 Development Banks, exclude data on the 5 Grameen Replicas, ADBN and NIDC, and two of the newly established DBs. Include: Nepal Development Bank (NDB), Enterprise Development Bank (EDB), Malika Development Bank, Sidhartha Development Bank, Development Credit Bank, Nepal CSI Development Bank (CSI), United Development Bank (UDB), Nirdhan Utan Bank, Narayani Audyogik Bikas Bank, Chhimek Development Bank, RMDC.

Table V.3. Regulatory Requirements for MFI Compared to Banks and Finance Companies

	Commercial Bank	Development Bank	Finance Company	NRB-licensed NGO	NRB-licensed Cooperative
1. Minimum Capital Requirements pre-1995 1995	Nrs 60 million Nrs 500 million in KTM, Nrs 250 other districts	Nrs 10 million		none	Nrs 2.5 million for branches in same district and Nrs 10 million for branches outside their district
July 2001					
2. Shareholding maximum by one organization maximum foreign owned, pre-2001 maximum foreign owned, from 2001	15 percent 50 percent 75 percent				
3. Authority to collect deposits	Yes	No (only time deposits of 3 months or more)	Yes (less than 10 times their paid-up capital)	yes	Not explicitly (nominally less than ten times their capital)
4. Collateral requirements on lending		only for loans >Nrs 100,000			
5. Capital Adequacy Requirement Ratio to risk-weighted assets	8 percent				8 percent
6. Loan Classification & Provisioning					
General - Pre 2001 Specific - Pre-2001	1 percent of loans 100 percent if over 60 months overdue		100 percent if over 12 months overdue	10 percent of profits	100 percent if more than 12 months overdue
General - Since July 2001 Specific - Since July 2001					
7. Liquidity Requirements Pre December 2001 From January 2002 From August 2002	10 percent average 8 percent average 7 percent average				
8. Reporting Requirements	monthly detailed, new call report forms introduced in 2001		monthly	quarterly details requested on occasional basis with no quality assurance	quarterly
9. Auditing Requirements	Annual audited reports within 60 days of end of fiscal year.			NRB requires "C" Certified auditor	NRB requires "B" Certified auditor

Sources: Sinha (1999), and NRB.

Table V.4. NRB-Licensed Companies Serving Rural Microfinance: Sources and Uses of Funds

	S&C Coops (18)		Grameen Banks (5)		NGO's (25)		Development Banks (11) <sup>1/</sup>		ADB <sup>2/</sup>		NIDC	
	1995	2002	1995	2002	1995	2002	1995	2002	1995	2002	1995	2002
Number	8	34	5	5	8	34	2	11	...	...	...	...
1. Capital	20	235	118	309	...	3	...	721	1,010	1,551	308	416
2. Deposits	57	1,475	3	295	...	1	...	5,280	42	1,607	...	...
3. Borrowings	1	93	101	1,085	...	16	...	286	3,964	4,762	981	1,418
4. Others	3	376	98	353	...	5	...	207	1,367	3,556	...	...
5. P/L Account	-	14	-	5	...	3	...	89	...	...	...	...
Total	80	2,193	320	2,047	...	28	...	6,583	6,385	11,476	...	...
1. Liquid Funds	13	398	27	107	...	6	...	1,471	345	754	...	...
2. Investments	2	200	76	378	...	4	...	411	961	2,651	...	...
3. Loans and Advances	59	1,272	99	1,050	...	16	...	4,389	8,458	20,088	1,140	2,070
4. Others	6	280	119	345	...	2	...	309	(1,369)	3,034	...	...
5. P/L Account	-	42	-	167	...	0	...	3	...	...	...	...

Source: NRB, Nonbank Financial Statistics, 2002.

1/ The 11 Development Banks, exclude data on the 5 Grameen Replicas, ADBN and NIDC, and two of the newly established DBs.

Include: Nepal Development Bank (NDB), Enterprise Development Bank (EDB), Malika Development Bank, Sidhartha Development Bank, Development Credit Bank, Nepal CSI Development Bank (CSI), United Development Bank (UDB), Nirdhan Uthan Bank, Narayani Audyogik Bikas Bank, Chhimek Development Bank, RMDC.

2/ Development wing of ADBN.

Table V.5. Deposits and Loans of Development Banks, 2002

	Licensed	Operating	Capital Fund	Deposits	Borrowing	Liquid Funds	Investments	Loans
<b>Development Banks</b>								
1 Agricultural Development Bank (ADBN)	Jun-68	Jun-68	1,551	1,607	4,762	11,476	754	20,088
2 Nepal Industrial Development Corp (NIDC)	Oct-59	Oct-59	416	...	1,418	...	...	2,070
3 Nepal Development Bank (NDB)	May-99	May-99	170	1,989	...	511	55	1,542
4 Enterprise Uddyam Development Bank (EDB)	Jun-99	Jun-99	4	8	...	1	...	9
5 Malika Development Bank	Apr-99	Apr-99	12	37	4	8	0	43
6 Sidharta Development Bank	Dec-98	Dec-98	11	10	2	4	...	17
7 Development Credit Bank Ltd	May-01	May-01	116	913	...	170	127	717
8 United Development Bank (UDB)	Jul-01	Aug-01	4	8	...	1	...	5
9 Nepal CSI Development Bank (CSI)	Sep-01	Oct-02	88	196	...	142	...	123
10 Narayani Audyogik Bikas Bank	Jan-02	Feb-02	2	6	...	2	...	5
<b>Micro-finance DBs</b>								
1 Purbanchal (Eastern)	Jun-93	Jun-93	66	109	260	11	1	360
2 Sudur Pashchimanchal (FarWest)	Jun-93	Jun-93	59	43	146	8	63	119
3 Paschimanchal (Western)	Jul-95	Jul-95	62	68	338	50	139	184
4 Madhya Paschimanchal (MidWest)	Jul-95	Jul-95	61	41	84	18	16	125
5 Madhyamanchal (Central)	Oct-96	Oct-96	61	34	255	20	159	162
6 Nirdhan Uttan Bank	Jul-99	Jul-99	27	56	250	135	...	194
7 RMDC	Mar-00	Mar-00	81	...	...	31	110	20
8 Deprosc	Apr-01	Oct-02	...	...	...	...	...	...
9 Chhimek Development Bank	Mar-02	Mar-02	7	1	30	32	...	4,043
10 Shawalamban Development Bank	Apr-02	Jun-02	...	...	...	...	...	...

Source: NRB, Noubank Financial Statistics, 2002.

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Table 1. Nepal: Nominal Gross Domestic Product by Sector, 1995/96–2000/01

	1995/96	1996/97	1997/98	1998/99	1999/00	2000/01
(In billions of Nepalese rupees, at current prices)						
Agriculture, fisheries, and forestry	96.9	108.8	112.5	132.4	144.6	149.0
Mining and quarrying	1.3	1.5	1.6	1.7	1.8	2.0
Manufacturing	22.5	24.8	27.0	30.3	33.6	35.6
Electricity and water	3.6	4.5	4.4	4.6	5.9	7.0
Construction	26.1	29.3	30.5	33.3	37.4	39.6
Trade, restaurants, and hotels	28.3	30.6	33.7	39.3	42.9	45.4
Transport and communications	15.9	19.3	22.6	24.6	29.3	33.1
Financial and real estate	23.5	27.2	29.8	33.2	36.9	41.8
Community and social services	21.3	23.7	27.8	30.6	33.8	40.1
GDP at factor cost	239.4	269.6	289.8	330.0	366.3	393.5
Agricultural GDP	96.9	108.8	112.5	132.4	144.6	149.0
Non-agricultural GDP	142.5	160.8	177.3	197.6	221.6	244.4
Value of imputed banking services	5.9	7.0	7.9	9.4	10.7	11.9
Net indirect taxes	15.5	18.0	18.9	21.5	23.9	28.6
GDP at market prices	248.9	280.5	300.8	342.0	379.5	410.2
(Percentage share in nominal GDP)						
Agriculture, fisheries, and forestry	40.5	40.4	38.8	40.1	39.5	37.9
Mining and quarrying	0.6	0.6	0.5	0.5	0.5	0.5
Manufacturing	9.4	9.2	9.3	9.2	9.2	9.0
Electricity and water	1.5	1.7	1.5	1.4	1.6	1.8
Construction	10.9	10.9	10.5	10.1	10.2	10.1
Trade, restaurants, and hotels	11.8	11.3	11.6	11.9	11.7	11.5
Transport and communications	6.6	7.2	7.8	7.5	8.0	8.4
Financial and real estate	9.8	10.1	10.3	10.1	10.1	10.6
Community and social services	8.9	8.8	9.6	9.3	9.2	10.2
Agricultural GDP at factor cost	40.5	40.4	38.8	40.1	39.5	37.9
Nonagricultural GDP at factor cost	59.5	59.6	61.2	59.9	60.5	62.1
(Annual percentage change)						
Memorandum items:						
Deflator for GDP at market prices	7.8	7.3	4.2	8.8	4.4	3.1
Agriculture-sector deflator	8.4	7.8	2.3	14.6	4.2	-1.2
Nonagriculture-sectors deflator	7.4	7.2	4.9	5.5	4.7	4.9

Sources: The Central Bureau of Statistics in Nepal; and Nepal Rastra Bank.

Table 2. Nepal: Real Gross Domestic Product by Sector, 1995/96–2000/01

	1995/96	1996/97	1997/98	1998/99	1999/00	2000/01
(In billions of Nepalese rupees, at 1994/95 prices)						
Agriculture, fisheries, and forestry	88.8	92.7	93.5	96.2	100.9	105.2
Mining and quarrying	1.3	1.3	1.4	1.4	1.5	1.5
Manufacturing	21.3	22.8	23.6	24.9	26.6	27.6
Electricity and water	3.4	3.5	3.3	3.5	4.0	4.3
Construction	24.7	26.4	27.0	28.8	31.5	31.8
Trade, restaurants, and hotels	25.4	26.5	28.0	29.1	31.0	31.9
Transport and communications	14.8	15.9	17.2	18.4	19.6	20.9
Financial and real estate	22.1	23.1	24.5	25.7	27.0	28.1
Community and social services	20.1	20.8	22.4	23.9	25.2	29.0
GDP at factor cost	221.9	233.0	240.8	251.8	267.5	280.3
Agricultural GDP	88.8	92.7	93.5	96.2	100.9	105.2
Non-agricultural GDP	133.1	140.3	147.3	155.6	166.6	175.1
Value of imputed banking services	5.6	5.7	6.2	6.6	7.2	7.8
Net indirect taxes	14.6	15.7	15.5	16.2	17.5	18.6
GDP at market prices	230.9	243.0	250.2	261.4	277.8	291.1
(Annual percentage change)						
Agriculture, fisheries, and forestry	3.8	4.4	0.9	2.9	4.9	4.3
Mining and quarrying	13.0	6.8	1.3	3.7	4.5	3.9
Manufacturing	9.0	7.1	3.4	5.3	7.2	3.6
Electricity and water	19.3	1.8	-4.1	5.7	14.3	7.9
Construction	7.1	6.6	2.2	6.8	9.6	0.9
Trade, restaurants, and hotels	4.5	4.1	5.8	3.9	6.8	2.7
Transport and communications	5.5	7.7	8.1	6.8	7.0	6.2
Financial and real estate	7.6	4.7	5.9	5.0	5.1	3.8
Community and social services	6.2	3.6	7.6	6.6	5.6	15.0
GDP at factor cost	5.7	5.0	3.3	4.6	6.2	4.8
Agricultural GDP	3.8	4.4	0.9	2.9	4.9	4.3
Nonagricultural GDP	7.0	5.4	5.0	5.6	7.1	5.1
Value of imputed banking services	11.0	1.5	8.4	6.9	9.4	8.3
Net indirect taxes	2.1	7.7	-0.9	4.5	7.8	6.4
GDP at market prices	5.3	5.3	2.9	4.5	6.2	4.8

Sources: The Central Bureau of Statistics in Nepal; and Nepal Rastra Bank.



Table 3. Nepal: Gross Domestic Product by Expenditure Components, 1995/96–2000/01

	1995/96	1996/97	1997/98	1998/99	1999/00	2000/01
(In billions of Nepalese rupees, at current prices)						
GDP at market prices	248.9	280.5	300.8	342.0	379.5	410.2
Consumption	213.1	235.4	256.9	294.1	321.6	356.6
Public	23.0	25.6	27.8	31.9	36.5	45.8
Private	190.1	209.9	229.1	262.2	285.1	310.8
Gross domestic investment	67.7	71.1	74.7	70.1	91.7	99.5
Gross fixed investment	56.1	60.8	65.4	65.3	73.3	78.0
Public	17.6	19.4	19.0	19.0	19.4	21.2
Private	38.5	41.4	46.4	46.3	54.0	56.8
Change in stocks	11.6	10.3	9.4	4.8	18.4	21.5
Net exports 1/	-31.9	-26.0	-30.8	-22.2	-33.7	-45.9
Exports	56.8	85.9	78.2	86.3	99.0	99.9
Imports	88.7	111.9	109.0	108.4	132.8	145.8
(Percentage share in nominal GDP)						
Consumption	85.6	83.9	85.4	86.0	84.7	86.9
Public	9.2	9.1	9.2	9.3	9.6	11.2
Private	76.4	74.8	76.2	76.7	75.1	75.8
Gross domestic investment	27.2	25.3	24.8	20.5	24.2	24.3
Gross fixed investment	22.5	21.7	21.7	19.1	19.3	19.0
Public	7.1	6.9	6.3	5.6	5.1	5.2
Private	15.4	14.8	15.4	13.5	14.2	13.9
Change in stocks	4.7	3.7	3.1	1.4	4.8	5.2
Net exports	-12.8	-9.3	-10.2	-6.5	-8.9	-11.2
Exports	22.8	30.6	26.0	25.2	26.1	24.3
Imports	35.6	39.9	36.2	31.7	35.0	35.5

Sources: The Central Bureau of Statistics in Nepal; and Nepal Rastra Bank.

1/ Exports and imports of goods and services reflect the revised coverage of the balance of payments.

Table 4. Nepal: Saving and Investment, 1995/96–2000/01

	1995/96	1996/97	1997/98	1998/99	1999/00	2000/01
(In billions of Nepalese rupees, at current prices)						
Gross national savings	46.8	63.1	66.4	71.7	93.7	104.2
Public sector 1/	3.8	3.8	3.9	3.1	4.3	1.0
Private sector	43.0	59.3	62.4	68.6	89.4	103.2
Gross domestic investment	67.7	71.1	74.7	70.1	91.7	99.5
Gross fixed investment	56.1	60.8	65.4	65.3	73.3	78.0
Public sector	17.6	19.4	19.0	19.0	19.4	21.2
Private sector	38.5	41.4	46.4	46.3	54.0	56.8
Change in stocks	11.6	10.3	9.4	4.8	18.4	21.5
Saving-investment gap	-20.9	-7.9	-8.4	1.6	2.0	4.7
Public sector	-13.8	-15.6	-15.0	-16.0	-15.1	-20.2
Private sector	-7.1	7.6	6.7	17.6	17.1	24.9
(In percent of nominal GDP)						
Gross national savings	18.8	22.5	22.1	21.0	24.7	25.4
Public sector 1/	1.5	1.4	1.3	0.9	1.1	0.2
Private sector	17.3	21.2	20.8	20.1	23.6	25.2
Gross domestic investment	27.2	25.3	24.8	20.5	24.2	24.3
Gross fixed investment	22.5	21.7	21.7	19.1	19.3	19.0
Public sector	7.1	6.9	6.3	5.6	5.1	5.2
Private sector	15.4	14.8	15.4	13.5	14.2	13.9
Change in stocks	4.7	3.7	3.1	1.4	4.8	5.2
Saving-investment gap	-8.4	-2.8	-2.8	0.5	0.5	1.1
Public sector	-5.6	-5.6	-5.0	-4.7	-4.0	-4.9
Private sector	-2.9	2.7	2.2	5.1	4.5	6.1

Sources: The Central Bureau of Statistics in Nepal; and Nepal Rastra Bank.

1/ Defined as revenue less regular expenditure and estimated recurrent costs of development expenditure until 1997/98.

Table 5. Nepal: Agricultural Production and Yields, 1995/96-2001/02

	1995/96	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02	1997/98	1998/99	1999/00	2000/01	2001/02
	(In thousands of metric tons)							(Percentage change)				
<b>Production by major crops</b>												
Foodgrains	6,247	6,395	6,331	6,465	6,985	7,172	7,247	-1.0	2.1	8.0	2.7	1.1
Paddy	3,579	3,699	3,641	3,710	4,030	4,216	4,165	-1.6	1.9	8.6	4.6	-1.2
Wheat	1,013	1,056	1,001	1,086	1,184	1,158	1,258	-5.2	8.5	9.0	-2.2	8.7
Maize	1,331	1,312	1,367	1,346	1,445	1,484	1,511	4.2	-1.6	7.4	2.7	1.8
Millet	282	289	285	291	295	283	283	-1.3	2.2	1.2	-4.1	-0.1
Barley	41	39	37	32	31	30	31	-4.4	-14.1	-2.5	-1.7	2.4
Cash crops	2,604	2,721	2,782	3,202	3,428	3,678	3,783	2.2	15.1	7.1	7.3	2.8
Sugarcane	1,569	1,622	1,718	1,972	2,103	2,212	2,248	5.9	14.8	6.7	5.2	1.6
Jute	15	14	15	16	15	16	16	10.0	1.9	-4.5	9.3	-2.4
Oilseeds	116	119	109	120	123	132	135	-8.2	9.5	2.8	7.6	2.0
Potato	898	962	935	1,091	1,183	1,314	1,380	-2.8	16.7	8.4	11.0	5.1
Tobacco	6	5	5	4	4	4	4	-9.8	-15.2	2.6	-0.7	-6.0
Distribution of fertilizer 1/	133	122	109	182	225	12	10	-10.8	67.0	23.6	-94.7	-16.7
<b>Area under cultivation 2/</b>												
Foodgrains	3,242	3,267	3,243	3,253	3,321	3,314	3,296	-0.7	0.3	2.1	-0.2	-0.5
Paddy	1,497	1,511	1,506	1,514	1,551	1,560	1,517	-0.3	0.5	2.4	0.6	-2.8
Wheat	654	667	640	641	660	641	667	-4.0	0.2	3.0	-2.9	4.1
Maize	792	794	799	802	819	825	826	0.6	0.4	2.1	0.7	0.1
Millet	260	260	262	264	263	260	258	0.8	0.8	-0.4	-1.1	-0.8
Barley	39	35	36	32	28	28	28	2.9	-11.1	-12.5	0.0	0.0
Cash crops	353	356	361	379	390	391	393	1.4	5.0	2.9	0.3	0.5
Sugarcane	45	46	49	54	58	59	59	6.5	10.2	7.4	1.7	0.0
Jute	11	11	12	12	15	11	11	9.1	0.0	25.0	-26.7	0.0
Oilseeds	185	182	179	190	190	188	188	-1.6	6.1	0.0	-1.1	0.0
Potato	106	111	116	118	123	129	131	4.5	1.7	4.2	4.9	1.6
Tobacco	6	6	5	5	4	4	4	-16.7	0.0	-20.0	0.0	0.0
<b>Yields</b>												
Foodgrains	1.9	2.0	2.0	2.0	2.1	2.2	2.2	-0.3	2.4	5.0	4.8	0.0
Paddy	2.4	2.4	2.4	2.5	2.6	2.7	2.7	-1.2	3.4	4.0	3.8	0.0
Wheat	1.5	1.6	1.6	1.7	1.8	1.8	1.9	-1.2	8.7	5.9	0.0	5.6
Maize	1.7	1.7	1.7	1.7	1.8	1.8	1.8	3.5	-0.7	5.9	0.0	0.0
Millet	1.1	1.1	1.1	1.1	1.1	1.1	1.1	-2.1	1.1	0.0	0.0	0.0
Barley	1.1	1.1	1.0	1.0	1.1	1.1	1.1	-7.0	-2.7	10.0	0.0	0.0
Cash crops	7.4	7.6	7.7	8.4	8.8	9.4	9.6	0.8	9.0	4.8	6.8	2.1
Sugarcane	34.9	35.3	35.1	36.5	36.3	37.5	38.1	-0.6	4.1	-0.5	3.3	1.6
Jute	1.4	1.3	1.3	1.3	1.0	1.5	1.5	0.8	1.3	-23.1	50.0	0.0
Oilseed	0.6	0.7	0.6	0.6	0.7	0.7	0.7	-6.7	-1.7	16.7	0.0	0.0
Potato	8.5	8.7	8.1	9.2	9.6	10.2	10.5	-7.0	14.2	4.3	6.3	2.9
Tobacco	0.9	0.9	0.9	0.8	0.9	1.0	1.0	8.2	-13.0	12.5	11.1	0.0

Source: The Central Bureau of Statistics in Nepal.

1/ Private sector has participated in fertilizer trading activity since November 1997.

2/ Areas cultivated with more than one crop are included under each crop.

Table 6. Nepal: Manufacturing Production Indices, 1997/98–2001/02

	Weights 1/	1997/98	1998/99	1999/00	2000/01	2001/02 (Six Months) 2/	1997/98	1998/99	1999/00	2000/01	
		(Indices 1996/97 = 100)					(Percentage change)				
Overall production	100.0	103.4	108.9	116.1	120.1	97.1	3.4	5.3	6.6	3.5	
Food	26.2	111.6	118.1	127.3	134.5	94.4	11.6	5.9	7.8	5.7	
<i>Of which:</i>											
Sugar	3.5	104.0	110.2	142.7	119.4	98.7	4.0	6.0	29.4	-16.3	
Vegetable ghee	1.5	115.6	111.5	118.9	153.1	143.8	15.6	-3.6	6.7	28.8	
Rice	2.0	124.0	131.4	125.7	146.3	106.8	24.0	6.0	-4.4	16.4	
Soybean oil	0.8	115.0	131.1	133.5	138.3	126.1	15.0	14.0	1.8	3.6	
Processed milk	3.0	108.0	111.2	114.5	124.1	115.0	8.0	3.0	2.9	8.4	
Beverage	10.5	111.4	120.2	131.1	139.8	75.6	11.4	7.8	9.0	6.7	
Tobacco	13.8	92.2	98.8	108.0	113.9	107.3	-7.8	7.2	9.4	5.4	
Textile	22.4	103.3	107.0	107.1	99.1	83.7	3.3	3.6	0.1	-7.5	
<i>Of which:</i>											
Cotton cloth	1.5	94.0	79.9	70.6	65.9	92.3	-6.0	-15.0	-11.7	-6.6	
Synthetic cloth	3.0	106.0	93.3	99.6	101.5	114.1	6.0	-12.0	6.8	1.9	
Woolen carpet	16.7	102.9	111.2	109.7	99.3	76.9	2.9	8.1	-1.3	-9.5	
Jute goods	1.2	114.0	116.3	135.1	130.9	91.3	14.0	2.0	16.2	-3.1	
Readymade garments	7.2	96.0	103.7	123.5	122.1	71.2	-4.0	8.0	19.1	-1.1	
Processed leather	1.0	109.0	111.2	108.1	134.6	93.4	9.0	2.0	-2.7	24.5	
Wood products	1.2	99.0	95.6	93.3	91.4	111.4	-1.0	-3.4	-2.4	-2.1	
Paper	1.9	101.0	103.0	111.3	125.5	99.0	1.0	2.0	8.1	12.7	
Other chemical products	6.8	98.6	105.5	114.5	130.7	114.0	-1.4	6.9	8.5	14.2	
Rubber products	1.5	96.0	98.0	96.5	96.6	98.1	-4.1	2.2	-1.5	0.1	
Plastic products	1.9	105.0	111.3	110.6	148.6	118.0	5.0	6.0	-0.7	34.4	
Nonmetallic mineral products	8.2	104.7	114.5	120.6	117.9	111.6	4.7	9.4	5.3	-2.2	
<i>Of which:</i>											
Bricks	3.9	83.0	96.5	96.3	96.5	103.5	-17.0	16.3	-0.2	0.2	
Cement	4.3	124.1	130.6	142.4	137.1	118.9	24.1	5.3	9.0	-3.7	
Iron and steel basic industries	5.1	107.9	107.4	120.4	134.1	109.0	7.9	-0.5	12.1	11.4	
Electrical industrial machinery apparatus, appliances, etc	1.8	113.0	116.4	121.0	146.4	123.9	13.0	3.0	4.0	21.0	
Others	0.5	93.1	89.3	98.9	92.6	122.1	-6.9	-4.0	10.8	-6.4	

Source: The Central Bureau of Statistics in Nepal.

1/ Weights are based on the Census of Manufacturing Establishments (1996/97).

2/ Based on the second quarterly survey.

Table 7. Nepal: Energy Consumption, 1995/96–2001/02

	1995/96	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02
	(In thousands of tons of coal equivalent)						
Traditional	6,185	6,268	6,403	6,540	6,681	6,824	6,960
<i>Of which</i> : Fuelwood	5,525	5,574	5,694	5,816	5,941	6,068	6,189
Commercial	651	691	768	811	1,044	1,088	1,202
Petroleum	507	554	625	661	709	734	790
Coal	72	60	61	61	236	246	297
Electricity	72	77	83	89	99	108	115
Total	6,836	6,959	7,171	7,351	7,725	7,912	8,162
	(Annual percentage change)						
Traditional	2.1	1.3	2.2	2.1	2.2	2.1	2.0
<i>Of which</i> : Fuelwood	2.1	0.9	2.2	2.1	2.1	2.1	2.0
Commercial	12.1	6.1	11.1	5.6	28.7	4.2	10.5
Petroleum	12.9	9.3	12.8	5.8	7.3	3.5	7.6
Coal	7.5	-16.7	1.7	0.0	286.9	4.2	20.7
Electricity	9.1	6.9	7.8	7.2	11.2	9.1	6.5
Total	3.0	1.8	3.0	2.5	5.1	2.4	3.2

Source: Data provided by the Nepalese authorities.

Table 8. Nepal: Tourism Indicators, 1995-2001

	1995	1996	1997	1998	1999	2000	2001 <sup>1/</sup>
Tourist arrivals (in thousands)	363.4	393.6	421.9	463.7	491.5	463.0	363.0
(Percentage change)	11.3	8.3	7.2	9.9	6.0	-5.8	-22.0
<i>Of which:</i>							
Europe	137.7	138.9	143.4	157.8	171.6	166.3	130.0
India 2/	117.3	122.5	133.4	143.2	140.7	95.9	65.0
Japan	25.4	28.9	35.0	37.3	38.8	41.0	28.0
United States and Canada	29.7	30.6	36.3	43.0	46.9	49.0	38.0
Average days of stay	11.3	13.5	10.5	10.8	12.8	12.0	12.3
Per capita expenditure							
(In Nrs) 3/	24,617	24,344	23,226	31,282	32,550	32,163	34,345
(In U.S. dollars) 3/	474	430	402	476	479	454	459
(Percentage change)	20.3	-9.3	-6.5	18.4	0.6	-5.2	1.1
Hotel-bed capacity	21,807	25,638	27,612	28,878	32,214	34,958	34,958
(Percentage change)	23.0	17.6	7.7	4.6	11.6	8.5	0.0

Source: Data provided by the Nepalese authorities.

1/ Estimated.

2/ By air only.

3/ Excluding Indian tourists.

Table 9. Nepal: Changes in the Consumer Price Index, 1996/97–2001/02 <sup>1/</sup>

(Average annual percentage change)

	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02
Overall national index	8.1	8.3	11.4	3.4	2.4	2.9
By commodity						
Food and beverages	8.2	7.8	16.2	0.4	-2.3	3.6
Foodgrains	9.1	3.2	18.6	8.6	-13.7	2.3
Milk and milk products	12.0	7.7	9.5	3.7	5.7	1.2
Oil and fats	2.5	8.3	29.0	-22.6	-4.7	8.4
Beverages	9.2	14.8	8.7	3.7	2.0	5.0
Vegetables and fruits	3.7	16.6	19.9	-16.9	4.2	7.3
Other goods and services	8.0	9.0	5.8	7.1	8.1	2.1
Cloth, clothing, and sewing services	7.8	6.9	6.0	4.7	2.2	2.4
Fuel, light, and water	11.2	7.5	2.8	13.2	22.3	-0.2
Regional indices						
Kathmandu	7.8	7.3	8.2	3.7	3.1	2.1
Terai	8.1	9.0	13.3	3.1	1.1	3.5
Hills	8.6	8.0	11.6	3.7	5.1	2.6

Source: The Central Bureau of Statistics in Nepal.

1/ Base year is 1995/1996.

Table 10. Nepal: Monthly Wages in Major Sectors, 1995/96–2000/01

	1995/96	1996/97	1997/98	1998/99	1999/00	2000/01
	(In Nepalese rupees)					
Agriculture						
Kathmandu	2,800	3,000	3,000	3,000	3,000	3,000
Birgunj	1,500	1,500	1,500	1,500	1,620	2,425
Biratnagar	1,350	1,350	1,350	1,500	1,500	1,500
Industry 1/						
Skilled	1,610	1,610	1,960	1,960	2,276	2,276
Unskilled	1,450	1,450	1,800	1,800	2,116	2,116
Construction 2/						
Skilled						
Kathmandu	5,350	5,550	5,700	5,700	5,700	6,000
Birgunj	3,300	3,300	3,390	3,900	4,050	4,313
Biratnagar	3,600	3,600	3,850	4,470	4,500	4,575
Semi-skilled						
Kathmandu	4,625	4,675	4,950	4,950	4,950	5,050
Biratnagar	3,000	3,000	3,150	3,870	3,900	3,975
Unskilled						
Kathmandu	2,950	3,000	3,000	3,000	3,000	3,112
Biratnagar	1,800	1,800	1,920	2,370	2,400	2,400
	(In U.S. dollars)					
Agriculture						
Kathmandu	50.7	52.6	48.5	43.8	42.2	40.6
Birgunj	27.2	26.3	24.3	21.9	22.8	32.8
Biratnagar	24.4	23.7	21.8	21.9	21.1	20.3
Industry 1/						
Skilled	29.2	28.2	31.7	28.6	32.0	30.8
Unskilled	26.3	25.4	29.1	26.3	29.8	28.7
Construction 2/						
Skilled						
Kathmandu	96.9	97.3	92.2	83.2	80.2	81.3
Birgunj	59.8	57.9	54.8	56.9	57.0	58.4
Biratnagar	65.2	63.1	62.2	65.3	63.3	62.0
Semi-skilled						
Kathmandu	83.7	82.0	80.0	72.3	69.6	68.4
Biratnagar	54.3	52.6	50.9	56.5	54.9	53.8
Unskilled						
Kathmandu	53.4	52.6	48.5	43.8	42.2	42.2
Biratnagar	32.6	31.6	31.0	34.6	33.8	32.5

Source: Data provided by the Nepalese authorities.

1/ Minimum monthly wage, including allowances, which are the same in Kathmandu, Birgunj, and Biratnagar.

2/ Carpenters and masons.



Table 11. Nepal: Social Indicators

	Latest Single Year			Same Region/Income Group		
	1970-75	1980-85	1994-00	India	South Asia	Low Income
Total population, mid-year (millions)	13.1	16.2	23.0	1,015.9	1,355.1	2,459.8
Growth rate (percent annual average)	2.0	2.1	2.4	1.8	1.9	2.0
Urban population (percent of population)	5.0	7.8	11.9	28.4	28.4	31.9
Total fertility rate (births per woman)	6.2	5.9	4.3	3.1	3.3	3.6
Total labor force (millions)	...	7	11	439	585	1,085
Females in labor force (percent)	...	39	40	32	33	38
Labor force participation rate	...	48	48	43	43	50
Poverty (percent of population)						
National headcount index	...	...	42.0	35.0	...	...
Urban headcount index	...	...	23.0	30.5	...	...
Rural headcount index	...	...	44.0	36.7	...	...
Income						
GNP per capita (U.S. dollars)	120	170	240	450	440	410
Consumer price index (1995=100)	17	35	137	144	142	140
Food price index (1995=100)	...	33	144	137	...	...
Income/consumption distribution						
Gini index	...	...	36.7	37.8	...	...
Lowest quintile (percent of income or consumption)	...	...	7.6	8.1	...	...
Highest quintile (percent of income or consumption)	...	...	44.8	46.1	...	...
Public expenditure						
Health (percent of GDP)	...	...	1.3	0.8	0.9	1.2
Education (percent of GNP)	1.5	2.6	2.5	2.9	3.0	3.4
Social security and welfare (percent of GDP)	0.1	0.1	0.4	...	...	...
Net primary school enrollment rate (percent of age group)						
Total	...	60	78	77	77	86
Male	...	80	93	83	83	89
Female	...	37	63	71	70	82
Gross secondary school enrollment						
Total	12	27	32	49	...	...
Male	19	39	45	59	...	...
Female	4	14	18	39	...	...
Adult literacy (percent)	...	22	58	68	66	71
Female literacy	...	...	33	45	42	52
Access to an improved water source (percent of population)						
Total	...	...	81	88	87	76
Urban	...	...	85	92	92	88
Rural	...	...	80	86	85	70
Access to electricity (percent)	...	...	15	54	...	...
Population per physician	...	30,221	13,617	2,459	2,500	...
Population per hospital bed	...	5,719	4,308	1,503	1,429	1,152
Immunization rate (percent under 12 months)						
Measles	...	34	73	50	53	57
DPT	...	32	76	55	57	57
Child malnutrition (percent under 5 years)	69	...	47	47	49	...
Life expectancy at birth (in years)						
Total	45	51	59	63	62	59
Male	46	52	59	62	62	58
Female	44	50	59	63	63	60
Mortality						
Infant (per thousand live births)	160	115	74	69	73	76
Under 5 (per thousand live births)	234	180	105	88	96	115
Adult (15-59)						
Male (per 1,000 population)	482	376	260	222	227	294
Female (per 1,000 population)	476	395	265	209	212	261
Maternal (per 100,000 live births)	...	...	830	440	...	...

Sources: Staff reports, EDSS, World Bank 2002 World Development Indicators CD-ROM.

Table 12. Nepal: Balance of Payments by Area, 1997/98–2001/02<sup>1/</sup>  
(in millions of U.S. dollars)

	1997/98			1998/99			1999/00			2000/01			2001/02 (Six Months)		
	India	Third Countries	Total	India	Third Countries	Total	India	Third Countries	Total	India	Third Countries	Total	India	Third Countries	Total
Trade balance	-34	-661	-695	-173	-454	-627	-136	-606	-742	-207	-625	-832	-54	-276	-330
Exports, f.o.b.	553	303	856	423	340	763	557	414	971	539	401	941	306	130	436
Merchandise exports	142	303	445	185	340	525	307	414	721	352	401	754	217	130	347
Re-exports	411	0	411	238	0	238	250	0	250	187	0	187	89	0	89
Imports, c.i.f.	587	964	1,551	596	794	1,390	693	1,020	1,713	747	1,026	1,773	360	406	766
Services (net)	18	187	205	39	274	313	46	227	273	45	171	216	2	48	50
Receipts	108	328	436	140	405	545	142	371	513	133	344	477	47	130	177
Payments	90	141	231	101	131	232	96	144	240	88	173	261	45	82	127
Private transfers (net)	89	266	355	108	230	338	135	362	497	158	522	680	96	363	459
Receipts	113	270	383	122	232	354	153	371	524	175	524	699	108	364	472
Recorded private transfers	49	89	138	66	122	188	74	150	224	73	217	290	41	110	151
Estimated remittances	64	181	245	56	110	166	79	221	300	102	307	409	67	254	321
Payments	24	4	28	14	2	16	18	9	27	17	2	19	12	1	13
Current account balance (excluding grants)	72	-207	-135	-26	50	24	45	-17	28	-4	68	64	44	135	179
Official grants	23	96	119	19	118	137	24	109	133	21	87	108	8	33	41
Current account balance (including grants)	95	-111	-16	-7	168	161	69	92	161	17	155	172	52	168	220
Official capital grants and loans (net)	1	400	401	2	236	238	3	218	221	1	138	139	1	48	50
Official capital grants	1	215	216	2	109	111	3	73	76	1	35	36	1	18	20
Official capital (net)	0	185	185	0	127	127	0	145	145	0	103	103	0	30	30
Loans	0	229	229	0	174	174	0	198	198	0	164	164	0	60	60
Amortization	0	44	44	0	47	47	0	53	53	0	61	61	0	30	30
Private capital grants	0	39	39	0	32	32	0	32	32	0	26	26	0	9	9
Other investment, net and errors and omissions	-57	-184	-240	-66	-229	-295	13	-235	-222	66	-365	-299	31	-261	-230
Overall balance	40	144	184	-71	207	136	85	107	192	84	-46	38	84	-36	48
Memorandum item:															
Current account balance (percent of GDP)	1.5	-4.3	-2.8	-0.5	1.0	0.5	0.8	-0.3	0.5	-0.1	1.2	1.1	0.8	2.4	3.2

Source: Data provided by the Nepalese authorities.

1/ Based on revised BOP methodology.

Table 13. Nepal: Composition of Foreign Trade, 1997/98–2001/02<sup>1/</sup>

(In millions of U.S. dollars)

	1997/98			1998/99			1999/00			2000/01			2001/02 (Six Months)		
	India	Third Countries	Total	India	Third Countries	Total	India	Third Countries	Total	India	Third Countries	Total	India	Third Countries	Total
Exports, f.o.b.	553	303	856	423	340	763	557	414	971	539	401	941	306	130	436
Merchandise exports	142	303	445	185	340	525	307	414	721	352	401	754	217	130	347
Food and live animals	28	23	51	30	25	55	54	7	61	54	11	65	37	3	40
Tobacco and beverages	0	0	0	1	0	1	1	0	1	1	0	1	1	0	1
Crude materials and inedibles	5	3	8	5	2	7	7	1	8	10	1	10	6	0	7
Animal and vegetable oil and fats	32	3	35	50	3	53	42	4	46	53	2	56	61	2	63
Chemicals and drugs	31	0	31	41	0	41	56	1	57	54	1	55	23	0	23
Manufactured goods, classified	41	147	188	48	151	199	81	149	230	120	135	256	71	54	125
Machinery and transport equipment	0	1	1	0	1	1	3	3	6	3	2	5	2	0	3
Miscellaneous manufactured articles	4	126	130	10	158	168	63	249	312	57	250	307	16	70	85
Commodities and transactions n.i.e. 1/	1	0	1	0	0	0	0	0	0	0	0	0	0	0	0
Re-exports	411	0	411	238	0	238	250	0	250	187	0	187	89	0	89
Imports, c.i.f.	587	964	1,551	596	794	1,390	693	1,020	1,713	747	1,026	1,773	360	406	766
Food and live animals	54	25	79	81	31	112	101	56	157	60	21	81	38	9	47
Tobacco and beverages	11	2	13	10	3	13	9	4	13	9	4	12	5	1	6
Crude materials and inedibles	16	96	112	20	72	92	22	79	101	32	70	102	17	28	45
Minerals, fuel and lubricants	153	114	267	128	99	227	129	144	273	151	206	357	85	75	160
Animal and vegetable oil and fats	0	33	33	1	48	49	1	63	64	6	70	76	0	54	54
Chemicals and drugs	85	94	179	81	103	184	91	119	210	90	85	175	35	50	85
Manufactured goods, classified	160	366	526	154	223	377	203	295	498	245	313	558	114	102	216
Machinery and transport equipment	83	187	270	98	168	266	101	196	297	118	194	312	52	69	121
Miscellaneous manufactured articles	22	42	64	20	43	63	34	63	97	35	62	98	12	19	31
Commodities and transactions n.i.e. 1/	3	5	8	3	4	7	2	1	3	2	0	2	2	0	2
Memorandum items:															
Trade balance (percent of GDP)	-0.7	-13.6	-14.3	-3.4	-9.0	-12.5	-2.5	-11.0	-13.5	-3.7	-11.2	-14.9	-1.0	-4.9	-5.9
Exports	11.4	6.2	17.6	8.4	6.8	15.2	10.1	7.5	17.7	9.7	7.2	16.9	5.4	2.3	7.7
Imports	12.1	19.9	31.9	11.8	15.8	27.6	12.6	18.6	31.2	13.4	18.4	31.8	6.4	7.2	13.6

Source: Data provided by the Nepalese authorities.

1/ Includes unclassified exports and imports, and adjustments to reconcile figures with summary balance of payments data.

Table 14. Nepal: Exports of Major Commodities, 1996/97–2001/02

(In thousands of U.S. dollars)

	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02 (Nine months)
Carpets	155,708	136,970	144,253	142,495	116,378	62,378
Pashmina	0	0	0	90,004	92,777	20,468
Ready-made garments	104,419	113,243	142,780	201,859	177,769	78,233
Hides and skins	8,071	9,921	6,637	4,934	9,602	6,170
Jute goods	9,909	11,626	12,818	15,982	17,529	15,669
Pulses	18,218	17,064	17,614	15,300	16,451	11,729
Handicrafts	2,492	2,573	3,238	3,666	3,564	2,293
Cardamon	3,658	3,676	3,435	3,229	4,039	3,575
Catechu	971	1,125	1,726	2,885	2,032	1,894
Ghee	1,578	2,696	577	544	6,375	140
Mustard and linseed	617	153	283	424	513	133
Raw jute	56	81	1	0	1,539	103
Dried ginger	815	670	605	861	826	604
Herbs	1,238	1,052	603	1,105	1,319	1,054
Total	307,750	300,850	334,570	483,288	450,714	204,443
Other exports	89,639	143,706	190,708	238,365	303,100	311,390
<i>Of which: vegetable ghee</i>	0	25,504	46,305	39,713	48,223	86,450
Total merchandise exports	397,389	444,556	525,278	721,653	753,814	515,833
Memorandum items:						
Carpets						
(thousands of square meters)	2,891	2,447	2,575	2,624	2,210	...
Ready-made garments						
(thousands of pieces)	29,954	34,951	37,747	46,836	43,431	...
Pulses (metric tonnes)	15,443	30,567	28,509	2,365	15,094	...
Exc. rate (annual average mid-rate)	57.03	61.95	67.95	69.07	73.24	76.45

Source: Data provided by the Nepalese authorities.

Table 15. Nepal: Services and Current Transfers, 1997/98–2001/02

(In millions of U.S. dollars)

	1997/98			1998/99			1999/00			2000/01			2001/02 (Six months)		
	India	Third Countries	Total	India	Third Countries	Total	India	Third Countries	Total	India	Third Countries	Total	India	Third Countries	Total
Services and current transfers (net)	130	549	679	166	622	788	205	698	903	224	780	1,004	106	444	550
Services (net)	18	187	205	39	274	313	46	227	273	45	171	216	2	48	50
Receipts	108	328	436	140	405	545	142	371	513	133	344	477	47	130	177
Freight and insurance	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Transportation	10	57	67	11	45	56	16	48	64	10	46	56	3	14	17
Travel	56	104	160	53	126	179	55	120	175	47	112	159	16	41	57
Investment income	1	29	30	2	36	38	2	49	51	9	51	60	6	13	19
Compensation of Employee Government, n.i.e.	3	5	8	2	11	13	2	14	16	2	12	14	1	7	8
Other	38	34	72	25	43	68	32	47	79	29	57	86	10	43	53
Payments	90	141	231	101	131	232	96	144	240	88	173	261	45	82	127
Freight and insurance	23	2	25	26	3	29	27	2	29	24	3	27	9	1	10
Transportation	2	32	34	2	34	36	5	38	43	4	41	45	2	19	21
Travel	37	48	85	43	34	77	33	36	69	32	43	75	19	23	42
Investment income	0	23	23	0	26	26	0	31	31	0	51	51	0	26	26
Compensation of Employee Government, n.i.e.	0	1	1	1	0	1	0	0	0	0	0	0	0	0	0
Other	28	27	55	29	25	54	31	28	59	25	29	54	0	4	4
Private current transfers (net)	89	266	355	108	230	338	135	362	497	158	522	680	96	363	459
Receipts	113	270	383	122	232	354	153	371	524	175	524	699	108	364	472
Private remittances	49	89	138	66	122	188	74	150	224	73	217	290	41	110	151
Indian excise refund	19	0	19	18	0	19	19	0	19	7	0	7			0
Other estimated remittances	64	181	245	56	110	166	79	221	300	102	307	409	67	254	321
Payments	24	4	28	14	2	16	18	9	27	17	2	19	12	1	13
Official current transfers (net)	23	96	119	19	118	137	24	109	133	21	87	108	8	33	41
Receipts	23	96	119	19	118	137	24	109	133	21	87	108	8	33	41
Payments	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0

Source: Data provided by the Nepalese authorities.

Table 16. Nepal: External Debt and Debt Service, 1995/96-2000/01

	1995/96	1996/97	1997/98	1998/99	1999/00	2000/01
	(In millions of U.S. dollars)					
Debt outstanding 1/	2,369	2,482	2,562	2,703	2,848	2,786
Total medium and long term	2,319	2,361	2,415	2,533	2,662	2,630
Multilateral	1,939	1,983	2,090	2,169	2,244	2,251
AsDB	757	802	910	948	1,012	1,043
EEC	9	8	8	7	6	6
IDA	1,052	1,059	1,080	1,107	1,123	1,102
IFAD	57	57	44	58	57	55
IMF 2/	43	34	25	21	15	10
NDF	11	16	18	20	20	19
OPEC	10	7	6	9	11	16
UNCDF	0	0	0	0	0	0
Bilateral	380	378	325	363	418	379
Austria	6	5	5	4	6	5
Belgium	8	7	6	6	5	4
Finland	0	6	6	6	7	6
France	53	51	52	48	45	40
Korea	0	0	2	10	10	9
Kuwait	15	13	12	11	10	8
OECD (Japan)	291	286	229	264	309	291
Russia	0	0	0	0	0	0
Saudi Fund	7	10	13	14	26	16
USA	0	0	0	0	0	0
U.S.A.	0	0	0	0	0	0
Australia	0	0	0	0	0	0
Short-term debt 2/	50	121	147	170	186	156
Total debt service	83	83	85	84	83	84
Amortization 3/	60	55	62	59	57	63
<i>Of which</i> : To IMF 4/	8	7	7	5	5	4
Interest 3/	23	27	23	25	26	21
<i>Of which</i> : To IMF	0.2	0.2	0.2	0.1	0.1	0.1
	(In percent)					
Debt-service ratio 5/	6.6	4.8	4.7	5.0	4.7	6.0
<i>Of which</i> : To IMF	0.6	0.5	0.5	0.3	0.2	0.2
Outstanding debt/GDP	52.4	50.5	52.8	53.7	51.8	49.9
<i>Of which</i> : To IMF	1.0	0.7	0.5	0.4	0.3	0.2

Source: Data provided by the Nepalese authorities (Loan Management Section-MOF&NRB).

1/ Consists primarily of medium- and long-term public and publicly guaranteed debt, excluding foreign liabilities of the banking system other than liabilities to the IMF.

2/ Outstanding trade credits.

3/ Includes principal and interest repayments of public enterprises and some private entities, as well as the central government.

4/ Excluding IMF Trust Fund.

5/ In relation to exports of goods and services (excluding re-exports) and private transfers.

Table 17. Nepal: Gross International Reserves, 1995/96–2001/02<sup>1/</sup>

	1995/96	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02 (Six months)
(In millions of U.S. dollars, end of period)							
Foreign exchange reserves							
Nepal Rastra Bank (NRB)	594	636	702	781	932	1,007	1,067
Convertible	488	475	533	709	772	710	729
Nonconvertible	106	161	169	72	160	297	338
Commercial banks	197	219	262	345	401	402	292
Convertible	187	203	246	304	369	364	264
Nonconvertible	10	16	16	41	32	38	28
Total	791	855	964	1,126	1,333	1,409	1,359
Convertible	675	678	779	1,013	1,141	1,074	993
Nonconvertible	116	177	185	113	192	335	366
Other gross foreign assets of NRB	15	15	14	14	14	14	14
SDR holdings	0	0	0	0	0	0	0
Gold 2/	6	6	6	6	6	6	6
Reserve tranche position	8	8	8	8	8	7	7
Total gross foreign assets of NRB	609	651	716	795	946	1,021	1,081
(In months of imports of goods and services)							
Nepal Rastra Bank							
Gross foreign assets	3.7	4.4	5.3	4.9	5.6	6.7	6.6
Foreign exchange reserves	3.6	4.3	5.2	4.8	5.5	6.6	6.6
Of which : convertible reserves	2.9	3.2	3.9	4.4	4.6	4.6	4.5

Source: Data provided by the Nepalese authorities.

1/ Totals differ from monetary sector figures owing to valuation effects.

2/ Valued at historical prices.

Table 18. Nepal: Average Customs Duty by Main Category of Goods, 1998/99–2001/02<sup>1/</sup>

Chapter Numbers	Main Category of Goods	1998/99	1999/00	2001/02 (or latest)
1–10	Live animals	4.0	5.0	10.5
11–20	Grains, vegetable extracts, sugars	11.5	15.6	16.7
21–30	Beverages, tobacco, mineral fuels, pharmaceuticals	10.7	11.7	13.6
31–40	Fertilizers, cosmetics, soaps, chemicals, plastics	14.5	15.3	20.6
41–50	Rawhides, skins, wood, paper, silk	9.8	10.9	11.7
51–60	Wool, cotton, man-made fibres, carpets	12.8	13.2	11.2
61–70	Clothing, footwear, ceramics, glassware, stoneware	18.7	21.1	20.1
71–80	Iron, steel, copper, nickel, aluminium, lead, zinc, tin	11.6	12.9	12.9
81–90	Tools, machinery, vehicles, aircrafts	14.5	11.9	11.9
91–97	Clocks, musical instruments, arms, furniture, art	25.4	20.6	21.1
	Total number of items	5237	5198	5321
	Sum of duties	64149	68310	76441
	Average customs duty	12.25	13.14	14.36

Source: Ministry of Finance and Department of Customs, Kathmandu, Nepal (1999 and 2000).

1/ Harmonized System classification; average of customs duties for all items in each chapter.



Table 19. Nepal: Composition of Imports and Import Duties, 1995/96–2001/02

(In millions of Nepalese rupees)

	1995/96	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02 (Eight months)
Imports from India	24,518	29,941	34,518	42,660	49,421	54,561	34,440
<i>Of which</i> : Dutiable imports	19,369	23,774	27,282	25,462	27,587	44,738	29,329
Import duties from India	2,059	2,359	2,707	3,430	4,218	4,967	3,311
As a percent of dutiable imports	10.6	9.9	9.9	13.5	15.3	11.1	11.3
As a percent of total imports	8.4	7.9	7.8	8.0	8.5	9.1	9.6
Imports from third countries	50,029	71,516	61,812	49,156	60,471	60,101	38,838
<i>Of which</i> : Dutiable imports	34,349	50,701	52,770	31,334	38,567	50,002	21,371
Import duties from third countries	4,195	4,748	4,523	4,479	4,913	5,419	2,956
As a percent of dutiable imports	12.2	9.4	8.6	14.3	12.7	10.8	13.8
As a percent of total imports	8.4	6.6	7.3	9.1	8.1	9.0	7.6
Total imports	74,547	101,456	96,330	91,816	109,892	114,662	73,278
Dutiable imports	53,718	74,475	80,052	56,796	66,154	94,740	50,700
Aid-related imports	20,829	26,981	16,278	35,020	43,738	19,922	22,578
Total import duties	6,254	7,107	7,230	7,909	9,131	10,387	6,267
As a percent of dutiable imports	11.6	9.5	9.0	13.9	13.8	11.0	12.4
As a percent of total imports	8.4	7.0	7.5	8.6	8.3	9.1	8.6

Source: Department of Customs, Ministry of Finance.

Table 20. Nepal: Structure of Interest Rates, 1995/96–2001/02

(Annual percentage rates, end of period)

	1995/96	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02
Refinancing facilities of Nepal							
Rastra Bank to commercial banks							
Export bills	11.0	11.0	9.0	9.0	6.5	6.5	2-4.5
Industrial sector	11.0	11.0	9.0	9.0	7.5	7.5	3-5.5
Agricultural sector	11.0	11.0	9.0	9.0	6.5	6.5	4.5-5.5
Service sector	11.0	11.0	9.0	9.0	7.5	7.5	3-5.5
Commercial banks							
Savings deposits	7.5-8.0	7.5-8.0	6.5-8.0	5.75-8.0	4.0-6.5	3.0-6.5	2.5-6.25
Time deposits							
3 months	6.75-8.0	6.75-9.0	5.0-8.0	4.0-7.5	4.0-6.0	2.5-6.0	2.0-5.25
6 months	7.25-9.0	7.25-9.0	6.0-8.5	6.0-8.0	5.0-6.75	3.5-6.75	2.5-6.0
1 year	9.5-11.0	9.5-11.0	9.0-10.5	7.25-9.5	6.0-7.75	4.5-7.75	3.5-7.0
2 years	negotiable	negotiable	9.5-12.0	7.25-10.25	5.75-8.5	4.25-8.5	3.25-8.0
3 years	negotiable	negotiable	...	...	...	...	...
4 years	negotiable	negotiable	...	...	...	...	...
5 years	negotiable	negotiable	...	...	...	...	...
Loans							
Industry	15.0-17.5	15.0-17.5	13.5-17.0	11.5-17.0	10.5-15.5	9.5-15.0	7.0-14.5
Agriculture	14.5-16.0	14.5-16.0	14.5-15.5	14.0-15.5	12.0-14.5	12.5-14.5	12.0-14
Services	18.0	18.0	18.0	18.0	7.5-17.0	7.5-16.0	7.0-15.5
Export bills	13.0-16.0	14.5-16.5	12.5-16.0	7.5-15.0	7.5-15.0	7.5-12.5	6.5-12.5
Commercial loans and overdrafts	14.5-20.0	14.5-20.0	13.5-20.0	10.0-19.0	9.0-18.0	9.0-18.0	7-17
Agricultural Development Bank of Nepal							
To cooperatives	12.0-15.0	12.0-15.0	13.0-16.0	13.0-16.0	11.0-12.0	11.0-12.0	10.0-12.0
To others	14.0-17.0	14.0-17.0	15.0-18.0	15.0-18.0	12.0-16.0	12.0-16.0	10.0-16.0
Nepal Industrial Development Corporation							
	15.0-16.0	15.5-18.0	15.5-18.0	15.5-18.0	15.5-18.0	15.5-18.0	13.5-14.5
Government securities							
National savings certificates							
Treasury bills (3 month) 1/	9.0-15.5	9.0-13.25	9.0-13.25	9.0-13.25	8.5-13.25	8.5-13.25	8.5-13.25
Treasury bills (1 year)	10.9	10.2	3.5	2.3	4.6	4.9	3.4
Development bonds	...	9.0-12.0	5.9-7.3	4.7-7.0	5.5-7.3	5.1	5.1
25-year special bonds	3.0-12.0	3.0-12.0	3.0-12.0	3.0-12.0	3.0-10.5	3.0-10.5	3.0-8.5
20-year special bonds	3.0	3.0	3.0	3.0	...	...	...
Special loan	5.0	5.0	5.0	5.0	5.0	5.0	5.1
Special loan	1.0-13.0	1.0-13.0	1.0-13.0	1.0-9.5	1.0-9.5	1.0-9.5	1.0-9.0

Source: Data provided by the Nepalese authorities.

1/ Annual weighted average.

Table 21. Nepal: Monetary Survey, 1996/97–2001/02

	1996/97	1997/98	1998/99	1999/2000	2000/01	2001/02 <sup>1/</sup>
(In millions of Nepalese rupees, end of period)						
Net foreign assets	40,191	55,573	65,028	80,468	87,891	85,631
Assets	49,367	66,114	77,611	94,856	105,279	104,574
Liabilities	9,176	10,542	12,583	14,388	17,388	18,943
Net domestic assets	63,530	70,890	87,772	105,653	126,856	138,807
Domestic credit	98,272	112,820	130,973	154,350	183,450	193,547
Public sector	28,182	29,819	32,625	36,400	46,993	51,116
Government (net)	26,584	28,761	31,058	34,592	44,770	48,966
Nonfinancial public enterprises	1,598	1,059	1,567	1,808	2,223	2,151
Private sector 2/	70,090	83,001	98,348	117,950	136,457	142,431
Other items (net)	-34,742	-41,930	-43,200	-48,682	-56,594	-54,740
Broad money	103,720	126,463	152,800	186,121	214,654	224,438
Narrow money	38,460	45,164	51,062	60,980	70,777	79,787
Quasi-money	65,260	81,299	101,738	125,141	143,877	144,651
(Annual percentage change)						
Net domestic assets	15.6	11.6	23.8	20.4	20.1	13.7
Domestic credit	13.4	14.8	16.1	17.8	18.9	9.2
Public sector	5.0	5.8	9.4	11.6	29.1	18.3
Private sector 2/	17.3	18.4	18.5	19.9	15.7	6.3
Broad money	11.9	21.9	20.8	21.8	15.3	7.6
Narrow money	5.4	17.4	13.1	19.4	16.1	14.4
Quasi-money	16.2	24.6	25.1	23.0	15.0	4.2
(12-month change in percent)						
Net foreign assets	2.7	9.7	7.5	10.1	3.9	-0.4
Net domestic assets	9.3	12.3	13.3	11.7	11.4	8.0
Domestic credit	12.6	14.0	14.4	15.3	15.6	7.8
Public sector	1.4	1.6	2.2	2.5	5.7	3.8
Private sector 2/	11.1	12.4	12.1	3.4	9.9	4.1
Memorandum items:						
Velocity (GDP/M2)	2.70	2.38	2.24	2.04	1.91	1.90
Money multiplier	2.53	2.75	2.93	3.05	3.03	2.97

Source: Data provided by the Nepalese authorities.

1/ As of June 2002.

2/ Includes credit to financial public enterprises.

Table 22. Nepal: Assets and Liabilities of Nepal Rastra Bank, 1996/97-2001/02

	1996/97	1997/98	1998/99	1999/2000	2000/01	2001/02 <sup>1/</sup>
	(In millions of Nepalese rupees, end of period)					
Net foreign assets						
Assets	34,474	46,354	52,608	65,270	74,965	81,425
Liabilities	36,910	48,393	54,139	66,634	62,859	82,012
	2,436	2,040	1,531	1,363	1,178	586
Net domestic assets	6,554	-358	-382	-4,267	-4,199	-5,901
Claims on public sector	18,846	18,487	18,407	16,423	19,384	19,782
Government (net)	18,838	18,480	18,399	16,415	19,377	19,775
Claims 2/	18,838	18,480	18,399	16,415	19,377	19,775
Deposits	...	...	...	...	...	...
Nonfinancial public enterprises	8	8	8	8	8	8
Claims on private sector 3/	2,977	2,801	3,011	3,723	5,030	3,808
Claims on commercial banks	7	6	6	45	6	259
Other items (net)	-15,275	-21,651	-21,805	-24,246	-28,618	-29,750
Reserve money	41,027	45,996	52,225	61,003	70,767	75,524
Currency outside banks	27,334	30,893	34,984	42,299	48,495	55,639
Currency held by banks	2,837	2,890	3,310	3,351	4,117	4,025
Bankers' deposits	9,273	10,543	11,858	12,187	15,985	13,134
Private sector deposits	1,584	1,670	2,073	2,473	2,170	2,726
	(12-month change in percent of reserve money at start of period)					
Net foreign assets	8.5	29.0	13.6	24.1	15.9	9.1
Net domestic assets	7.4	-16.8	-0.1	-7.4	0.1	-2.4
Reserve money	15.9	12.1	13.5	16.8	16.0	44.6
Memorandum items:						
Currency/deposits ratio	35.8	32.3	29.7	29.3	29.2	33.0
Reserves/deposits ratio	16.2	14.3	13.1	11.6	12.3	10.3

Source: Data provided by the Nepalese authorities.

1/ As of June 2002.

2/ Includes Treasury IMF account.

3/ Includes claims on financial public enterprises.

Table 23. Nepal: Assets and Liabilities of Commercial Banks, 1996/97–2001/02

(In millions of Nepalese rupees, end of period)

	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02 <sup>1/</sup>
Reserves	12,110	13,433	15,168	16,388	20,102	17,160
Foreign assets	12,457	17,721	23,473	28,208	30,047	22,563
Claims on Government	7,746	10,281	12,659	18,177	25,393	29,191
Claims on nonfinancial public enterprises	1,590	1,051	1,559	1,801	2,216	2,143
Claims on financial public enterprises 2/	305	505	598	1,045	1,372	2,033
Claims on business and individual	66,808	79,695	94,739	113,182	130,056	136,590
Assets = Liabilities	101,016	122,686	148,196	178,695	209,185	209,679
Demand deposits	9,543	12,601	14,005	16,364	20,112	21,423
Savings deposits	28,857	35,470	48,114	63,364	77,602	80,384
Fixed deposits	34,536	44,022	51,612	59,774	64,178	61,794
Margin deposits	1,867	1,807	2,011	2,003	2,098	2,473
Foreign liabilities 3/	6,739	8,502	11,052	13,025	17,214	18,357
Borrowing from the central bank	7	6	5	45	6	259
Other items (net)	19,467	20,278	21,395	24,225	27,976	24,990
Memorandum item:						
Priority sector lending in percent of total domestic credit	12.0	12.1	13.2	13.0	...	...

Source: Data provided by the Nepalese authorities.

1/ As of June 2002.

2/ Excludes loanable fund of ADBN.

3/ Includes foreign currency deposits.

Table 24. Nepal: Assets and Liabilities of Finance Companies, 1997/98–2001/02

(End of Period)

	1997/98		1998/99		1999/00		2000/01		2001/02 <sup>1/</sup>	
	Nrs millions	Percent	Nrs millions	Percent	Nrs millions	Percent	Nrs millions	Percent	Nrs millions	Percent
Cash	39	0.5	110	1.0	95	0.7	140	0.9	60	0.3
Bank balance	406	4.8	1,023	9.6	1,640	12.6	1,909	12.2	1,711	9.8
Investment	2,065	24.6	1,262	11.9	1,129	8.6	1,268	8.1	1,466	8.4
<i>Of which : government securities</i>	1,750	20.8	932	8.8	843	6.5	837	5.4	898	5.2
Loans and advances	5,391	64.1	7,219	67.9	9,058	69.4	10,865	69.7	12,063	69.4
Term loans	2,177	25.9	3,105	29.2	4,234	32.4	4,704	30.2	5,268	30.3
Housing loans	1,567	18.6	2,004	18.8	2,342	18.0	2,965	19.0	3,148	18.1
Hire purchases	953	11.3	1,304	12.3	1,639	12.6	2,152	13.8	2,564	14.8
Fixed deposit receipt loans	225	2.7	498	4.7	475	3.6	464	3.0	431	2.5
Leasing	310	3.7	260	2.4	235	1.8	278	1.8	397	2.3
Other	159	1.9	47	0.4	133	1.0	302	1.9	254	1.5
Other	503	6.0	1,019	9.6	1,133	8.7	1,615	10.4	2,071	11.9
Assets = Liabilities	8,404	100.0	10,633	100.0	13,055	100.0	15,597	100.0	17,370	100.0
Deposits	6,275	74.7	8,033	75.5	9,744	74.6	11,654	74.7	12,908	74.3
Paid-up capital	727	8.7	838	7.9	945	7.2	1,221	7.8	1,386	8.0
Borrowings	228	2.7	83	0.8	176	1.3	215	1.4	227	1.3
Reserve 2/	227	2.7	305	2.9	497	3.8	647.0	4.1	678	3.9
Other	947	11.3	1,374	12.9	1,693	13.1	2,060	13.2	2,172	12.5
Memorandum items:										
Capital adequacy ratio (in percent)	15.2		14.2		17.7		17.6		13.2	
Loan/deposit ratio (in percent)	85.9		89.9		93.0		93.2		93.5	
Number of finance companies	44		45		46		48		52	

Source: Nepal Rastra Bank.

1/ As of April 2002.

2/ Including loan loss provision.

Table 25. Nepal: Income Statements of Rastriya Banijya Bank and Nepal Bank Limited, 1995/96–2000/01

(In millions of Nepalese rupees)

	1996/97	1997/98	1998/99	1999/00	2000/01
<b>Rastriya Banijya Bank</b>					
Interest income 1/	3,090	2,963	3,333	3,251	2,834
Less: interest payments	1,830	2,112	2,579	2,725	2,568
Net interest income	1,260	851	754	526	265
Overhead expenses 2/	639	700	753	891	1,186
Provision	503	480	225	1,081	1,804
Total	1,142	1,180	978	1,971	2,991
Operating profit	118	-329	-224	-1,446	-2,726
Other income 3/	297	406	351	369	298
Net profit	415	77	127	-1,077	-2,428
<b>Nepal Bank Limited</b>					
Interest income 1/	2,426	2,693	2,221	2,516	2,362
Less: interest payments	1,515	1,907	2,286	2,022	1,874
Net interest income	911	786	-65	493	488
Overhead expenses 2/	788	944	808	1,095	872
Provision	254	400	936	1,325	1,091
Total	1,042	1,344	1,744	2,420	1,963
Operating profit	-131	-558	-1,809	-1,927	-1,475
Other income 3/	260	574	383	383	401
Net profit	129	16	-1,426	-1,543	-1,074

Sources: Rastriya Banijya Bank; and Nepal Bank Limited.

1/ Interest income from loan and investments.

2/ Provision for staff bonus and taxes and other expenditure.

3/ Other service charges and incomes.

Table 26. Nepal: Outstanding Bank Credit to Major Public Enterprises, 1995/96–2001/02

(In millions of Nepalese rupees, end of period)

	1995/96	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02
Principal	5,448	6,603	7,008	8,815	9,947	9,691	9,847
Financial institutions	4,249	5,430	6,169	7,544	8,497	8,009	8,141
Agricultural Development Bank	2,993	3,751	4,295	5,588	6,538	7,443	7,466
Nepal Industrial Development Corporation	895	1,184	1,263	1,197	1,110	15	15
Rural Development Banks	317	408	521	632	679	493	602
Other	44	87	90	127	169	58	58
Nonfinancial public enterprises	1,199	1,173	839	1,271	1,451	1,682	1,706
Agricultural Input Corporation	383	320	16	242	0	56	0
Agricultural Tools Factory	97	182	176	150	232	1	1
Janak Educational Material Center	45	8	30	58	93	55	97
Cottage Industrial and Handicraft Emporium	85	17	10	5	6	9	9
Himal Cement Company	17	19	25	27	27	29	29
Janakpur Cigarette Factory	134	146	145	121	123	76	130
Nepal Food Corporation	195	317	266	427	485	389	403
Raghupati Jute Mill	40	10	0	0	0	-	0
Royal Nepal Airline Corporation	1	8	3	86	117	611	601
Hetauda Leather Factory	29	2	3	3	2	29	2
Tobacco Development Corporation	51	0	0	0	0	-	0
Nepal Coal Limited	34	5	0	0	1	1	1
Other	88	139	165	152	365	426	433
Overdue interest	761	426	221	301	365	535	207
Financial institutions	2	2	2	4	6	1	3
Nonfinancial public enterprises	759	424	219	297	359	534	204
Total outstanding credit	6,209	7,029	7,229	9,116	10,312	10,225	10,054

Source: Data provided by the Nepalese authorities.



Table 27. Nepal: Nonperforming Bank Loans of Public Enterprises, 1997/98–2000/01

(In millions of Nepalese rupees, end of period)

	1997/98			1998/99			1999/2000			2000/01		
	Principal	Interest	Total	Principal	Interest	Total	Principal	Interest	Total	Principal	Interest	Total
Nepal Food Corporation	10	4	14	7	4	11	7	5	12	0	0	0
Nepal Transportation Corporation	19	20	39	20	28	48	19	27	46	0	0	0
Himal Cement Company	0	0	0	2	0	2	0	0	0	0	0	0
Bhaktapur Tile and Brick Corporation	3	2	5	3	2	5	2	3	5	3	4	7
Rice Exporting Companies	13	90	102	3	32	35	3	32	35	3	32	35
Cottage Industrial and Handicraft Emporium	93	87	180	0	136	136	0	136	136	0	136	136
National Trading Ltd.	0	0	0	0	0	0	0	0	1	0	0	0
Agricultural Tools Factory	0	0	0	0	0	0	137	8	145	0	0	0
Hetadua Leather Factory	2	19	21	3	25	28	2	28	30	2	33	35
Hetadua Clothes Factory	0	0	0	30	2	32	37	8	45	37	15	52
<b>Total</b>	<b>140</b>	<b>222</b>	<b>361</b>	<b>68</b>	<b>229</b>	<b>297</b>	<b>207</b>	<b>247</b>	<b>454</b>	<b>45</b>	<b>220</b>	<b>265</b>

Source: Data provided by the Nepalese authorities.

Table 28. Nepal: Summary of Government Operations 1997/98-2002/03 <sup>1/</sup>

	1997/98	1998/99	1999/00	2000/01	2001/02		2002/03
					Budget	Est. <sup>2/</sup>	Budget <sup>2/</sup>
(In billions of Nepalese rupees)							
Total revenue and grants	37.1	39.3	46.4	53.6	72.2	57.3	70.2
Total revenue	31.7	35.0	40.7	46.8	58.1	48.6	55.6
Tax revenue	25.9	28.8	33.2	38.9	47.2	40.4	45.9
Nontax revenue	5.8	6.3	7.6	8.0	10.9	8.2	9.7
Grants	5.4	4.3	5.7	6.8	14.1	8.7	14.6
Total expenditure	50.2	52.8	59.8	72.1	90.1	74.3	86.2
Current <sup>3/</sup>	27.7	32.0	36.5	45.8	53.0	52.7	61.1
Capital and net lending <sup>3/</sup>	22.5	20.8	23.3	26.3	37.1	21.6	25.1
Overall balance before grants	-18.5	-17.8	-19.0	-25.3	-32.0	-25.7	-30.6
Overall balance after grants	-13.1	-13.5	-13.3	-18.5	-17.9	-17.0	-16.1
Financing	13.1	13.5	13.3	18.5	17.9	17.0	16.1
Net foreign loans	11.5	8.7	10.0	7.5	10.6	5.9	6.4
Gross disbursements	14.2	11.9	13.7	12.0	16.4	10.9	12.4
Amortization	2.7	3.2	3.7	4.5	5.8	5.0	6.0
Net domestic financing	1.6	4.8	3.4	11.0	7.3	11.1	9.7
Net NRB financing	0.2	-0.1	-2.1	3.0	...	2.3	...
Net commercial bank	2.5	2.4	5.5	7.2	...	5.4	...
Net nonbank	-1.1	2.5	-0.1	0.7	...	3.4	...
(In percent of GDP)							
Total revenue	10.5	10.2	10.7	11.4	12.8	11.4	11.9
Tax revenue	8.6	8.4	8.7	9.5	10.4	9.4	9.8
Nontax revenue	1.9	1.8	2.0	1.9	2.4	1.9	2.1
Grants	1.8	1.3	1.5	1.6	3.1	2.0	3.1
Total expenditure	16.7	15.4	15.7	17.6	19.8	17.4	18.4
Current <sup>3/</sup>	9.2	9.3	9.6	11.2	11.6	12.3	13.0
Capital and net lending <sup>3/</sup>	7.6	6.1	6.1	6.4	8.1	5.0	5.4
Overall balance before grants	-6.3	-5.2	-5.0	-6.2	-7.0	-6.0	-6.5
Overall balance after grants	-4.5	-3.9	-3.5	-4.5	-3.9	-4.0	-3.4
Financing	4.4	3.9	3.5	4.5	3.9	4.0	3.4
Net foreign loans	3.8	2.5	2.6	1.8	2.3	1.4	1.4
Gross disbursements	4.7	3.5	3.6	2.9	3.6	2.6	2.6
Amortization	0.9	0.9	1.0	1.1	1.3	1.2	1.3
Net domestic financing	0.5	1.4	0.9	2.7	1.6	2.6	2.1
Central bank financing	0.1	0.0	-0.6	0.7	...	0.5	...
Commercial Bank financing	0.8	0.7	1.5	1.8	...	1.3	...
Nonbank financing	-0.4	0.7	0.0	0.2	...	0.8	...
Memorandum items:							
Public savings (percent of GDP)	1.3	0.9	1.1	0.2	1.1	-1.0	-1.2
Regular expenditure (percent of GDP) <sup>3/</sup>	7.8	7.7	7.7	9.0	9.2	10.3	10.5
Development expenditure (percent of GDP) <sup>3/</sup>	8.9	7.7	8.0	8.5	10.6	7.1	7.9
Nominal GDP (billions of Nrs)	301	342	380	410	455	428	469

Sources: Data provided by the Nepalese authorities; and Fund staff estimates.

1/ Fiscal years start on July 16. Table confined to central government operations as contained in the budget.

2/ Based on the Budget Speech, delivered on July 8, 2002. However, expenditures in the estimate in 2001/02 reflects staff estimate as the detailed expenditure items were not available at the time of the 2002/03 budget speech.

3/ Current and capital and net lending expenditures are based on new economic classification provided by the authorities and staff estimates. The traditional presentation is in terms of regular and development expenditures.

Table 29. Nepal: Central Government Revenue, 1997/98-2002/03

	1997/98	1998/99	1999/00	2000/01	2001/02		2002/03
					Budget	Est. <sup>1/</sup>	Budget <sup>1/</sup>
(In millions of Nepalese rupees)							
Total revenue (HMG)	32,941	37,251	42,894	48,894	60,251	50,515	57,150
Less principal repayment of loans	1,248	2,242	2,183	2,057	2,153	1,919	1,547
Total revenue <sup>2/</sup>	31,687	35,008	40,711	46,837	58,099	48,596	55,603
Tax revenue	25,937	28,751	33,152	38,865	47,170	40,397	45,928
Taxes on income and profits	4,898	6,170	7,421	9,114	11,140	9,248	9,863
Taxes on property	1,112	1,125	1,134	616	1,300	929	1,101
House and land registration	1,001	1,002	1,011	608	1,300	928	1,100
Taxes on goods and services	11,425	11,938	13,784	16,583	20,300	16,580	19,205
Value-added tax	7,123	7,882	9,855	12,048	14,750	11,890	13,730
Excise taxes	2,886	2,953	3,128	3,771	4,880	3,787	4,725
Other	1,416	1,103	801	765	670	903	750
Taxes on international trade	8,502	9,518	10,813	12,552	14,430	13,641	15,760
Import taxes	7,174	7,920	9,009	10,569	12,034	11,149	12,610
Indian excise refund	1,102	1,206	1,332	1,456	1,780	1,511	1,680
Export taxes	217	378	432	493	601	961	1,207
Other	9	14	40	34	15	20	263
Nontax revenue <sup>2/</sup>	5,750	6,257	7,559	7,971	10,929	8,199	9,675
Charges, fees, fines, etc.	1,246	1,446	1,747	1,931	2,157	1,879	2,556
Sales of goods and services	1,339	1,036	1,068	1,184	1,414	1,052	1,239
Dividends	1,311	1,783	2,507	2,336	3,405	2,676	2,885
Royalty and fixed asset sales	565	202	563	950	1,114	651	877
Interest receipts	1,213	1,686	1,568	1,440	1,639	860	1,066
Miscellaneous	76	103	104	131	1,200	1,080	1,053
(In percent of GDP)							
Total revenue	10.5	10.2	10.7	11.4	12.8	11.4	11.9
Tax revenue	8.6	8.4	8.7	9.5	10.4	9.4	9.8
Taxes on income and profits	1.6	1.8	2.0	2.2	2.4	2.2	2.1
Taxes on property	0.4	0.3	0.3	0.2	0.3	0.2	0.2
Taxes on goods and services	3.8	3.5	3.6	4.0	4.5	3.9	4.1
Value-added tax	2.4	2.3	2.6	2.9	3.2	2.8	2.9
Excise taxes	1.0	0.9	0.8	0.9	1.1	0.9	1.0
Other	0.5	0.3	0.2	0.2	0.1	0.2	0.2
Taxes on international trade	2.8	2.8	2.8	3.1	3.2	3.2	3.4
Nontax revenue	1.9	1.8	2.0	1.9	2.4	1.9	2.1
Memorandum item:							
Nominal GDP (billions of Nrs)	301	342	380	410	455	428	469

Source: Data provided by the Nepalese authorities.

1/ Based on the budget speech, delivered on July 8, 2002.

2/ Adjusted by taking out of non-tax revenue the principal repayments from corporations (classified as negative capital spending).

Table 30. Nepal: Central Government Expenditure by Economic Classification, 1997/98–2002/03

	1997/98	1998/99	1999/00	2000/01	2001/02		2002/03
					Budget	Est. <sup>1/</sup>	Budget
(In millions of Nepalese rupees)							
Total expenditure	50,200	52,763	59,754	72,087	90,123	74,289	86,236
Current expenditure	27,652	31,944	36,456	45,837	53,013	52,689	61,120
Goods and services	20,483	23,726	26,547	35,428	40,923	41,467	47,089
Wages, salaries, and benefits	16,532	18,142	19,775	28,506	28,614	31,606	30,124
Core civil service	6,937	7,124	7,701	11,312	10,274	10,375	9,730
Police salaries	2,320	2,578	2,842	4,050	4,293	5,093	4,993
Defense salaries	2,083	2,459	2,872	3,607	3,619	4,619	4,432
Teacher salaries	5,192	5,982	6,360	9,537	10,429	11,520	10,968
Retirement facilities	957	1,189	1,314	2,054	2,418	3,318	2,558
Other goods and services	2,994	4,395	5,458	4,869	9,892	6,543	14,407
Of which : contingency	87	84	969	162	3,862	100	7,370
Interest payments	3,752	4,080	4,820	4,698	6,597	5,720	8,006
Domestic debt	2,435	2,531	3,180	2,997	3,671	3,897	5,428
Foreign debt	1,317	1,549	1,640	1,701	2,926	1,823	2,578
Subsidies and transfers	3,417	4,138	5,089	5,712	5,493	5,502	6,025
Capital expenditure	19,356	19,017	19,358	21,188	29,953	16,700	19,741
Acquisition of fixed assets	12,876	13,288	13,130	14,447	18,768	10,500	11,425
Purchase of stocks	1,913	1,556	1,315	1,109	2,284	1,200	1,351
Capital transfers (grants)	4,566	4,173	4,913	5,632	8,901	5,000	6,965
Lending minus repayments	3,192	1,802	3,940	5,062	7,156	4,900	5,376
Investment in loans	4,440	4,044	6,123	7,119	9,309	6,819	6,923
Less repayment of loans (income)	1,248	2,242	2,183	2,057	2,153	1,919	1,547
(In percent of GDP)							
Total expenditure	16.7	15.4	15.7	17.6	19.8	17.4	18.4
Current expenditure	9.2	9.3	9.6	11.2	11.6	12.3	13.0
Goods and services	6.8	6.9	7.0	8.6	9.0	9.7	10.0
Wages, salaries, and benefits	5.5	5.3	5.2	6.9	6.3	7.4	6.4
Retirement facilities	0.3	0.3	0.3	0.5	0.5	0.8	0.5
Other goods and services	1.0	1.3	1.4	1.2	2.2	1.5	3.1
Interest payments	1.2	1.2	1.3	1.1	1.4	1.3	1.7
Domestic debt	0.8	0.7	0.8	0.7	0.8	0.9	1.2
Foreign debt	0.4	0.5	0.4	0.4	0.6	0.4	0.5
Subsidies and transfers	1.1	1.2	1.3	1.4	1.2	1.3	1.3
Capital Expenditure	6.4	5.6	5.1	5.2	6.6	3.9	4.2
Acquisition of fixed assets	4.3	3.9	3.5	3.5	4.1	2.5	2.4
Purchase of stocks	0.6	0.5	0.3	0.3	0.5	0.3	0.3
Capital transfers (grants)	1.5	1.2	1.3	1.4	2.0	1.2	1.5
Lending minus repayments	1.1	0.5	1.0	1.2	1.6	1.1	1.1
Investment in loans	1.5	1.2	1.6	1.7	2.0	1.6	1.5
Less repayment of loans (income)	0.4	0.7	0.6	0.5	0.5	0.4	0.3
Memorandum items:							
Regular expenditure (millions of Nrs) 2/	23,317	26,473	29,311	37,079	41,805	44,079	49,104
Development expenditure (millions of Nrs) 3/	26,884	26,290	30,443	35,009	48,318	30,210	37,132
Nominal GDP (billions of Nrs.)	301	342	380	410	455	428	469

Sources: Data provided by the Nepalese authorities; and Fund staff estimates.

1/ Staff estimates.

2/ Regular expenditure adjusted by subtracting payment of amortization on domestic and foreign loans.

3/ Development expenditure adjusted by adding net lending (or subtracting the payment of principal from corporations).

Table 31. Nepal: Central Government Expenditure by Functional Classification, 1997/98–2002/03

	1997/98	1998/99	1999/00	2000/01	2001/02		2002/03
					Budget	Est. <sup>1/</sup>	Budget
(In millions of Nepalese rupees)							
Total expenditure	50,200	52,763	59,754	72,087	90,123	74,289	86,236
Regular expenditure	23,317	26,473	29,311	37,079	41,805	44,079	49,104
Social services	7,066	7,876	8,881	10,692	13,534	13,454	14,130
Education	5,731	6,004	6,717	8,226	10,429	10,413	10,968
Health	1,049	1,137	1,325	1,547	2,228	2,115	2,151
Other	286	735	839	919	877	926	1,011
Economic services	2,036	2,321	2,411	2,533	3,111	2,965	3,260
Agriculture related	388	431	469	544	662	575	774
Forestry	540	732	791	829	940	965	1,007
Infrastructure	808	863	891	924	1,195	1,055	1,132
Other	300	295	260	236	314	370	347
Defense	2,583	2,995	3,482	3,813	4,521	5,785	7,228
Interest payments	3,752	4,080	4,820	4,698	6,597	5,720	8,006
General administration	3,930	4,532	5,454	8,027	8,774	10,961	11,225
Other	3,950	4,669	4,262	7,315	5,268	5,194	5,255
Development expenditure	26,884	26,290	30,443	35,009	48,318	30,210	37,132
Social services	10,730	9,668	12,202	12,873	18,757	11,108	16,860
Education	2,362	1,641	2,574	2,784	3,503	2,402	3,318
Health	2,712	1,677	2,127	1,972	3,007	1,702	2,748
Drinking water	1,683	1,900	2,423	2,407	3,993	2,077	3,773
Other	3,973	4,450	5,079	5,709	8,254	4,927	7,020
Economic services	16,154	16,622	18,241	22,136	29,561	19,102	20,273
Agriculture related	4,830	4,905	5,653	6,624	9,188	5,716	5,413
Infrastructure	10,809	11,398	11,350	12,779	17,039	11,028	12,800
Other	515	319	1,238	2,732	3,334	2,358	2,060
(In percent of GDP)							
Total expenditure	16.7	15.4	15.7	17.6	19.8	17.4	18.4
Social services	5.9	5.1	5.6	5.7	7.1	5.7	6.6
Of which : Education	2.7	2.2	2.4	2.7	3.1	3.0	3.0
Health	1.3	0.8	0.9	0.9	1.1	0.9	1.0
Drinking water	0.6	0.6	0.6	0.6	0.9	0.5	0.8
Economic services	6.0	5.5	5.4	6.0	7.2	5.2	5.0
Of which : Agriculture related	1.7	1.6	1.6	1.7	2.2	1.5	1.3
Infrastructure	3.9	3.6	3.2	3.3	4.0	2.8	3.0
Defense	0.9	0.9	0.9	0.9	1.0	1.4	1.5
Interest payments	1.2	1.2	1.3	1.1	1.4	1.3	1.7
General administration	1.3	1.3	1.4	2.0	1.9	2.6	2.4
Other	1.3	1.4	1.1	1.8	1.2	1.2	1.1
(In percent of total expenditure)							
Social services	35.4	33.3	35.3	32.7	35.8	33.1	35.9
Of which : Education	16.1	14.5	15.5	15.3	15.5	17.3	16.6
Health	7.5	5.3	5.8	4.9	5.8	5.1	5.7
Drinking water	3.4	3.6	4.1	3.3	4.4	2.8	4.4
Economic services	36.2	35.9	34.6	34.2	36.3	29.7	27.3
Of which : Agriculture related	10.4	10.1	10.2	9.9	10.9	8.5	7.2
Infrastructure	23.1	23.2	20.5	19.0	20.2	16.3	16.2
Defense	5.1	5.7	5.8	5.3	5.0	7.8	8.4
Interest payments	7.5	7.7	8.1	6.5	7.3	7.7	9.3
General administration	7.8	8.6	9.1	11.1	9.7	14.8	13.0
Other	7.9	8.8	7.1	10.1	5.8	7.0	6.1

Sources: Data provided by the Nepalese authorities; and Fund staff estimates.

1/ Staff estimates.

Table 32. Nepal: Summary of the Tax System  
(As of July 17, 2002)

Tax	Nature of Tax	Exemptions and Deductions	Tax Rates	
<b>1. Taxes on income and profits</b>				
1.1 Taxes on business income	Levied on net income from public, private, and joint-venture enterprises.	<b>Deductions:</b> a. All costs incurred during the year; by the person; and in the production of income from the business. b. Donation. c. Retirement contribution. d. Up to 5 percent reserve allowance in case of commercial banks as per the instruction of the NRB.	<i>Business type</i> Normal Special industry: <sup>1/</sup> Employing 600+ Nepali Operating remote areas for ten years Other Financial institutions	<i>Tax rates (In percent)</i> 25  18 14-16 20 30
1.2 Taxes on employment income	Levied on net income from individual's remuneration from the employment of the individual during the year.	<b>Deductions:</b> a. Donation b. Retirement contribution.  <b>Exemption threshold:</b> Single Nrs 65,000 Married Nrs 85,000	<i>Income bracket</i> Below Nrs 75,000 Above Nrs 75,000	<i>Tax rates (In percent)</i> 15 25
1.3 Taxes on investment income	Levied on profits and gains from investment, including dividend, interest, rent, royalty, and retirement payment.	<b>Deductions:</b> Same as prescribed in the above business income.  <b>Exemptions:</b> a. Final withholding payments. b. Amounts included in calculating the taxpayers' income from any business or employment.  <b>General exemptions:<sup>2/</sup></b> a. amounts derived by a person entitled to privileges under a bilateral or a multilateral treaty concluded between the Nepalese government and a foreign country; b. amounts derived by an individual from employment in the public service of the foreign government; c. amounts derived from public funds of the foreign country by an individual who is not a citizen of Nepal; d. amounts derived by an individual who is not a	<i>Income type</i> Interest, other retirement payment, rent Interest to individuals on deposits Retirement payment from approved source Dividend, gains from investment insurance or gains from other unapproved source	<i>Tax rates (In percent)</i> 15 6 6 10

Table 32. Nepal: Summary of the Tax System (continued)

(As of July 17, 2002)

Tax	Nature of Tax	Exemptions and Deductions	Tax Rates																		
		<p>citizen of Nepal from employment by the Nepalese government;</p> <p>e. allowances paid by the Nepalese government to widows, elder citizens, or disabled individuals;</p> <p>f. amounts derived by way of gift, bequest, or scholarship;</p> <p>g. amounts derived by an exempt organization by way of (i) gift, or (ii) other contributions;</p> <p>h. an agricultural income;</p> <p>i. incomes and dividends derived by cooperative societies;</p> <p>j. income of an approved retirement fund; and</p> <p>k. pension received by retired army or police service of foreign countries, paid by the public fund of that country.</p>																			
<b>2. Taxes on property</b>																					
2.1 <i>Tax on rural land</i>	Levied on the size of an individual's land holdings. The tax rates vary with the location and type of the soil.	There is full or partial remission of the land revenue tax in the presence of a drought or other natural calamity.	For holdings of less than 1 hectare, Nrs 0.6 to 10 per hectare. For larger holdings, Nrs 2.6 to 105 per hectare.																		
2.2 <i>Taxes on urban houses and land</i>	Levied on the property value.	Property values of up to Nrs 1 million are exempted.	<table border="0"> <thead> <tr> <th data-bbox="1339 971 1482 992"><i>Property value</i></th> <th data-bbox="1612 971 1797 992"><i>Marginal tax rates</i></th> </tr> </thead> <tbody> <tr> <td data-bbox="1339 997 1482 1018">Next 1 million</td> <td data-bbox="1612 997 1713 1018">Nrs 300</td> </tr> <tr> <td data-bbox="1339 1023 1482 1044">Next 3 millions</td> <td data-bbox="1612 1023 1751 1044">0.05 percent</td> </tr> <tr> <td data-bbox="1339 1049 1482 1070">Next 5 millions</td> <td data-bbox="1612 1049 1751 1070">0.25 percent</td> </tr> <tr> <td data-bbox="1339 1075 1482 1096">Next 10 millions</td> <td data-bbox="1612 1075 1751 1096">0.50 percent</td> </tr> <tr> <td data-bbox="1339 1101 1440 1122">Remaining</td> <td data-bbox="1612 1101 1751 1122">1.50 percent</td> </tr> </tbody> </table>	<i>Property value</i>	<i>Marginal tax rates</i>	Next 1 million	Nrs 300	Next 3 millions	0.05 percent	Next 5 millions	0.25 percent	Next 10 millions	0.50 percent	Remaining	1.50 percent						
<i>Property value</i>	<i>Marginal tax rates</i>																				
Next 1 million	Nrs 300																				
Next 3 millions	0.05 percent																				
Next 5 millions	0.25 percent																				
Next 10 millions	0.50 percent																				
Remaining	1.50 percent																				
2.3 <i>Registration fees</i>	Levied on the value of property at the time of sale, gifts, or on partition.		<table border="0"> <thead> <tr> <th colspan="2" data-bbox="1499 1166 1629 1187"><b>Urban Areas</b></th> </tr> <tr> <th colspan="2" data-bbox="1499 1192 1629 1213"><b>Sales deeds</b></th> </tr> </thead> <tbody> <tr> <td data-bbox="1339 1218 1608 1239">Gifts within third generation</td> <td data-bbox="1650 1218 1734 1239">2 percent</td> </tr> <tr> <td data-bbox="1339 1243 1608 1265">Gifts out of third generation</td> <td data-bbox="1650 1243 1734 1265">10 percent</td> </tr> <tr> <td data-bbox="1339 1269 1388 1291">Sales</td> <td data-bbox="1650 1269 1734 1291">6 percent</td> </tr> <tr> <th colspan="2" data-bbox="1499 1333 1692 1354"><b>Non-urban Areas</b></th> </tr> <tr> <td data-bbox="1339 1359 1608 1380">Gifts within third generation</td> <td data-bbox="1650 1359 1734 1380">1 percent</td> </tr> <tr> <td data-bbox="1339 1385 1608 1406">Gifts out of third generation</td> <td data-bbox="1650 1385 1734 1406">5 percent</td> </tr> <tr> <td data-bbox="1339 1411 1388 1432">Sales</td> <td data-bbox="1650 1411 1734 1432">3 percent</td> </tr> </tbody> </table>	<b>Urban Areas</b>		<b>Sales deeds</b>		Gifts within third generation	2 percent	Gifts out of third generation	10 percent	Sales	6 percent	<b>Non-urban Areas</b>		Gifts within third generation	1 percent	Gifts out of third generation	5 percent	Sales	3 percent
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Gifts out of third generation	5 percent																				
Sales	3 percent																				

Table 32. Nepal: Summary of the Tax System (continued)  
(As of July 17, 2002)

Tax	Nature of Tax	Exemptions and Deductions	Tax Rates	
			Partition Deeds <i>Value of property</i>	<i>Tax</i>
			0-50,000	Nil
			50,001-200,000	Nrs 200
			200,001-500,000	Nrs 1,000
			500,001-1,000,000	Nrs 3,000
			1,000,001-5,000,000	0.25 percent
			5,000,001-10,000,000	0.50 percent
			Above 10,000,001	0.75 percent
<b>3. Taxes on goods and services</b>				
3.1 <i>Value-added tax</i>	Levied on goods and services at all stages of production and distribution.	<p><b>Exemption threshold:</b> Nrs 2 million</p> <p><b>Exemptions:</b> Exports, inputs used in the production of exports, and foreign aid projects.</p> <p>Equipment for agricultural, fishery, and industrial activities; domestically produced cotton fabric, cotton textiles, and other textiles; cotton thread; woolen yarn; carpets; jute products; gold ornaments; unprocessed; aero planes, helicopters, fire fighters, and ambulances; battery operated three-wheeler; printed material; vaccines; food and medicine for animals; equipment for processing waste and for investment in alternative energy sources. Unprocessed mustard oil, primary agricultural products.</p> <p>Additional goods exempted from VAT in the 2000/01 budget were sarees made of cotton and artificial fibres; organic tea.</p>	10 percent	
3.2 <i>Excise taxes</i>	Levied on some goods; the high-yielding are those on cigarettes and liquor.	Liquor industries based on fruits receive a five-year exemption, with an additional three-year extension for locating in remote areas.	<p><b>Specific taxes</b></p> <p><i>Cigarettes</i></p> <p>Nonfiltered cigarettes</p> <p>Filtered cigarettes by length</p> <p>Short</p> <p>Medium (70 mm to 75 mm)</p> <p>Medium (75 mm to 85 mm)</p>	<p><i>Per 1,000 cigarettes</i></p> <p>Nrs 125</p> <p>Nrs 300</p> <p>Nrs 385</p> <p>Nrs 530</p>



Table 32. Nepal: Summary of the Tax System (continued)  
(As of July 17, 2002)

Tax	Nature of Tax	Exemptions and Deductions	Tax Rates	
			Long (above 85 mm)	Nrs 710
			<i>Liquor types</i>	<i>Per L.P. liter</i>
			Whisky	Nrs 275
			Vodka	Nrs 160
			Low-quality liquor	Nrs 50
			Beer	Nrs 38
			<i>Ad valorem taxes</i>	
3.3 <i>Tourism fee</i>	Levied on tourism services.		Pick-ups	15 percent
3.4 <i>Motor vehicle tax</i>	An annual tax based on the size of the vehicle and whether it is for own use or rented.		2 percent	
			<i>Size of vehicle</i>	<i>Annual tax rates</i>
				<i>For gasoline-fueled vehicles</i> <i>For diesel engine vehicles</i>
			Cars, jeeps, and vans	
			up to 1,300 cc	Nrs 6,500    Nrs 10,000
			1,301 cc to 2,000 cc	Nrs 8,500    Nrs 13,750
			2,001 cc to 2,900 cc	Nrs 10,000    Nrs 17,500
			2,901 cc to 4,000 cc	Nrs 12,300    Nrs 23,000
			Above 4,001 cc	Nrs 15,000    Nrs 28,000
<b>4. Taxes on international trade</b>				
4.1 <i>Import duties</i>	Levied on c.i.f. import values.	<b>Exemptions:</b> Imports by the government, educational institutions, and foreign aid projects. Equipment for agricultural and fishery activities, food and medicine for animals, inputs for the textile industry and for computers, medicine from India.	<i>Commodity Groups</i>	<i>Basic Duty Rates (In percent)</i>
			Roughly:	
			Raw material and machinery	2.5-15 <sup>3</sup>
			Semi-processed materials	15-25
			Fully processed materials	15-25
			Consumer items	10 and 40
			Luxury items	80 and 130
		<b>Deductions:</b> 50 percent on industrial machinery, 80 percent on aluminum, copper, and brass in block or plates. Rebates of 10-20 percent on imports from India and Tibet and, 5 percent on imports from most favored countries.		

Table 32. Nepal: Summary of the Tax System (continued)  
(As of July 17, 2002)

Tax	Nature of Tax	Exemptions and Deductions	Tax Rates
			Development tax that replaced the octroi tax. 1.5
4.2 <i>Export duties</i>	Levied on a limited range of exports	Half percent service duty on exports	A combination of ad valorem and specific tax rates apply.

<sup>1</sup> As defined in section 3 of the Industrial Enterprises Act, 1992, but not including cigarettes, bidi, cigar, chewing tobacco, khaini, or other goods of a similar nature using tobacco as the basic raw material, or alcohol, beer, or other goods of a similar nature.

<sup>2</sup> Applicable to all income heads.

<sup>3</sup> Slab rates of 1 and 2 percent are created by exemptions.

Table 33. Nepal: Profits and Losses of Selected Nonfinancial Public Enterprises, 1996/97–2001/02<sup>1/</sup>

	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02 <sup>2/</sup>
(In millions of Nepalese rupees, end of period)						
Agricultural Input Corporation	-217	-71	-266	14	-62	-112
Nepal Drinking Water Corporation	39	24	-24	-48	-80	-114
Hetauda Cement Company	11	0	17	-27	-117	-11
Janakpur Cigarette Factory	-71	-34	-3	20	60	30
Nepal Electricity Authority	26	356	356	817	-71	514
Nepal Food Corporation	0	-12	42	26	209	372
Nepal Oil Corporation	-520	-295	1,055	1014	256	72
Nepal Telecommunication Corporation (NTC)	1,177	1,857	2,045	2,028	2147	1731
Royal Nepal Airline Corporation	-121	9	-55	14	-993	-197
Others	-1,468	-586	-141	-400	-2,649	196
Total excluding NTC	-2,322	-609	981	1,430	-3,447	750
Total including NTC	-1,145	1,248	3,026	3,458	-1,301	2,482
(In percent of GDP)						
Agricultural Input Corporation	-0.1	0.0	-0.1	0.0	0.0	0.0
Nepal Drinking Water Corporation	0.0	0.0	0.0	0.0	0.0	0.0
Hetauda Cement Industry Ltd.	0.0	0.0	0.0	0.0	0.0	0.0
Janakpur Cigarette Factory Ltd.	0.0	0.0	0.0	0.0	0.0	0.0
Nepal Electricity Authority	0.0	0.1	0.1	0.2	0.0	0.1
Nepal Food Corporation	0.0	0.0	0.0	0.0	0.1	0.1
Nepal Oil Corporation	-0.2	-0.1	0.3	0.3	0.1	0.0
Nepal Telecommunication Corporation (NTC)	0.4	0.6	0.6	0.5	0.5	0.4
Royal Nepal Airline Corporation	0.0	0.0	0.0	0.0	-0.2	0.0
Others	-0.5	-0.2	0.0	-0.1	-0.6	0.0
Total excluding NTC	-0.9	-0.2	0.3	0.4	-0.8	0.2
Total including NTC	-0.4	0.4	0.9	0.9	-0.3	0.6
Memorandum items:						
Number of profit-making enterprises	19	15	14	20	19	22
Number of loss-making enterprises	16	20	21	15	18	15
Total number of employees <sup>3/</sup>	36,295	32,693	35,578	47,178	45,721	...

Source: Data provided by the Nepalese authorities.

1/ Profits after income tax and bonus.

2/ From Targets and Performances of Public Enterprises, MoF, 2002. Data for 2001/02 are preliminary.

3/ Includes contractual, temporary, and part-time employees.

Table 34. Nepal: Interest and Dividend Payments of Public Enterprises to Government, 1997/98–2001/02

(In millions of Nepalese rupees)

	1997/98			1998/99			1999/00			2000/01			2001/02 <sup>1/</sup>		
	Interest	Dividend	Total	Interest	Dividend	Total	Interest	Dividend	Total	Interest	Dividend	Total	Interest	Dividend	Total
Agricultural Development Bank	29	0	29	34	0	34	29	0	29	444	0	444	82	0	82
Agricultural Inputs Corporation	0	0	0	0	0	0	...	...	...	...	...	...	...	...	...
Cottage Handicraft Emporium	0	0	0	0	0	0	...	...	...	0	1	1	...	...	...
Credit Guarantec Corporation	0	1	1	0	1	1	0	1	1	0	2	2	0	2	2
Hetauda Cement Factory	57	0	57	38	0	38	20	0	20	...	...	...	8	0	8
National Insurance Co.	...	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Nepal Drinking Water Corporation	6	0	6	...	...	...	...	...	...	67	0	67	43	0	43
Nepal Electricity Authority	424	0	424	70	0	70	481	0	481	1,149	0	1,149	1,250	0	1,250
Nepal Industrial Development Corporation	...	...	...	0	20	20	133	0	133	57	0	57	...	...	...
Nepal Rastra Bank	10	1,300	1,310	...	1,300	1,300	...	1,500	1,500	...	2,000	2,000	...	2,250	2,250
Nepal Transport Corporation	0	0	0	0	0	0	...	...	...	...	...	...	...	...	...
Royal Nepal Airlines	0	0	0	0	0	0	...	...	...	...	...	...	...	...	...
Salt Trading Corp.	0	1	1	...	...	...	...	...	...	...	...	...	...	...	...
Securities Exchange Centre	0	0	0	0	0	0	...	...	...	...	...	...	...	...	...
Others	331	4	335	278	148	426	...	...	...	...	...	...	...	...	...
Total	857	1,306	2,163	420	1,469	1,889	663	1,501	2,164	1,717	2,003	3,720	1,382	2,252	3,634

Sources: Data provided by the authorities; and *Targets and Performances of Public Enterprises*, MoF, 2002.

1/ Preliminary.

Table 35. Nepal: Summary of the Privatization Process

Enterprise Name	Value in Millions of U.S. Dollars	Number of employees	Form of Privatization	Date of Privatization
<i>I. Privatized enterprises</i>				
1. Bhrikuti Pulp and Paper Factory	3.4	1,321	Share sale	October 1992
2. Harisiddhi Bricks and Tiles Factory	3.2	595	Share sale	October 1992
3. Leatherage Bansbari Tannery and Shoes Factory	0.4	55	Share sale	November 1992
4. Nepal Film Development Company	1.0	99	Share sale	November 1993
5. Balaju Textiles Industry Ltd.	0.3	165	Share sale	December 1993
6. Raw Hide Collection and Development Company	0.1	...	Share sale	December 1993
7. Nepal Jute Development and Trading Company	...	...	Liquidated in 1993	
8. Nepal Lube Oil Limited	0.5	101	Share sale	June 1994
9. Bitumen and Barrel Industries Ltd.	0.2	58	Share sale	June 1994
10. Tobacco Development Company	...	...	Liquidated in 1994	
11. Nepal Foundry Industry	0.2	65	Share sale	March 1996
12. Ragupati Jute Mills	1.2	114	Share sale	August 1996
13. Biratnagar Jute Mills	...	2,000	Leased	December 1996
14. Agriculture Tools Factory Ltd.	1.4	287	Share sale: 5 percent to employees, 65 percent to one private-sector party, and 30 percent retained.	May 1997
15. Bhaktapur Brick Factory Ltd. 7/	3.0	...	Leased	August 1997 1/
16. Nepal Bank Ltd. 2/	3.3	...	Government share reduced to 41 percent.	February 1997
<i>II. Public sector enterprises being privatized</i>				
1. Nepal Tea Development Corporation 3/	4	2,000	Share sale: 5 percent to employees, 30 percent to general public, and 65 percent to one private-sector party.	March 1998, completion delayed
2. Himal Cement Company 4/	1.5-2	905	Share sale	May 1998, completion delayed
3. Butwal Power Company	25-30	300	Share sale: 2-3 percent to employees, 2-3 percent to United Mission to Nepal, 75 percent to one private-sector party, and 20 percent retained.	Jan. 10, 1999 completion delayed

Table 35. Nepal: Summary of the Privatization Process (Continued)

Enterprise Name	Value in millions of U.S. dollars	Number of employees	Form of Privatization	Date of Privatization
III. <i>Public sector enterprises to be privatized</i> 5/				
<i>Financial institutions</i>				
	-72.1			
1. Rastriya Banijya Bank 6/	-72.8	5,743	Process of contracting out started	
2. Rastriya Beema Sansthan (insurance company)	-	308	Not yet decided	
3. Nepal Housing and Finance Company	0.7	19	Not yet decided	
<i>Nonfinancial Institutions</i>				
	192.4	15,826		
4. Nepal Telecommunication Corporation	191.2	5,224	Not yet decided	
5. Royal Nepal Airline Corporation	-11.0	1,788	Not yet decided	
6. Dairy Development Corporation (Pokhara Unit) 7/	5.3	1,158	Not yet decided.	
7. Nepal Rosin and Turpentine 7/	0.6	605	Not yet decided	
8. Lumbini Sugar Factory 7/	1.6	1,109	Not yet decided	
9. Janakpur Cigarette	2.0	1,806	Not yet decided	
10. Nepal Transport Corporation	0.6	865	Closed	
11. Industrial District Management Ltd.	1.5	271	Not yet decided	
12. Agriculture Lime Industry	-0.1	107	Not yet decided	
13. Agriculture Project Service Center	-0.4	171	Closed	
14. Herbs Production and Processing Center 7/	-0.5	177	Not yet decided	
15. Hetauda Textile Industry 7/	-0.6	934	Privatization process has been started	
16. Morang Sugar Mills	...	...	Not yet decided	
17. Birendra International Conference Center	...	...	Not yet decided	
18. Nepal Orind Magnesite Industry	-31.6	258	Closed	
19. Butwal Spinning Mills	...	...	Process of contracting out started	
20. Udayapur Cement Factory	33.1	640	Not yet decided	
21. Hetauda Cement Factory 7/	0.7	884	Not yet decided	
22. Cotton Development Board	...	...	Not yet decided	

Source: Ministry of Finance.

1/ The government repossessed the company, as the lessee failed to operate the company satisfactorily. A legal settlement is pending.

2/ A sale of 10 percent of the shares reduced government participation to 41 percent in February 1997.

3/ Offers received in 1999, and associated payments, were not considered satisfactory. A proposal for privatization is being considered by MoF and MoI.

4/ The preferred bidder could not meet financial commitment and negotiations to be finalized with second preferred bidder in February pending compromise on severance pay awards to administrative staff that are to be made redundant.

5/ Net worth estimates for end-2000/2001, as reported in *Targets and Performances of Public Enterprises FY 2000/2001-2002/2003* published by the Ministry of Finance in July 2002. The conversion from Nepalese rupees to U.S. dollars was done at the rate of Nrs 78.68=US \$ 1.

6/ A share issue is planned through brokers in 2000. Selection of broker and percentage to be determined.

7/ Under review in privatization cell.