ASIAN DEVELOPMENT BANK PPA: NEP 23085

# PROGRAM PERFORMANCE AUDIT REPORT

# ON THE

# INDUSTRIAL SECTOR PROGRAM
# (Loan 1229-NEP [SF])

# IN

# NEPAL

November 2002

## CURRENCY EQUIVALENTS

Currency Unit – Nepalese rupee/s (NRe/NRs)

| | | At Appraisal (March 1993) | At Project Completion (October 1998) | At Operations Evaluation (December 2001) |
|---|---|---|---|---|
| NRe1.00 | = | $0.019940 | $0.017536 | $0.013127 |
| $1.00 | = | NRs50.150 | NRs57.025 | NRs76.176 |

## ABBREVIATIONS

| | | |
|---|---|---|
| ADB | – | Asian Development Bank |
| ASYCUDA | – | Automated System of Custom Data |
| BWH | – | bonded warehouse |
| CSI | – | cottage and small industry |
| DDS | – | duty drawback scheme |
| DOC | – | Department of Customs |
| DOI | – | Department of Industry |
| EPR | – | Environmental Protection Regulation |
| ESAF | – | Enhanced Structural Adjustment Facility |
| GDP | – | gross domestic product |
| GFCF | – | gross fixed capital formation |
| IDM | – | Industrial District Management |
| IMF | – | International Monetary Fund |
| IPCR | – | Industrial Pollution Control Regulations |
| ISP | – | Industrial Sector Program |
| MOC | – | Ministry of Commerce |
| MOF | – | Ministry of Finance |
| MOI | – | Ministry of Industry |
| MOPE | – | Ministry of Population and Environment |
| NBSM | – | Nepal Bureau of Standards and Metrology |
| NPC | – | National Planning Commission |
| NRB | – | Nepal Rastra Bank |
| NRM | – | Nepal Resident Mission |
| OEM | – | Operations Evaluation Mission |
| OGL | – | open general licensing |
| PCR | – | program completion report |
| SDR | – | special drawing rights |
| TA | – | technical assistance |
| TPIA | – | trend, progress, and impact assessment |

## NOTES

(i) The fiscal year (FY) of the Government ends on 15 July. FY before a calendar year denotes the year in which the FY ends. For example, FY2002 begins on 16 July 2001 and ends on 15 July 2002.

(ii) In this report, "$" refers to US dollars.

**Operations Evaluation Department, PE-608**

## CONTENTS

## BASIC DATA
## Industrial Sector Program (Loan 1229-NEP[SF])

**Program Preparation/Institution Building**

| TA No. | TA Name | Type | Person-Months | Amount ($) | Approval Date |
|---|---|---|---|---|---|
| 1654 | Industrial Sector Program | PPTA | 11.6 | 187,000 | 10 Jan 1992 |
| 1872 | Monitoring, Impact Assessment, and Management of Policy Reforms[1] | ADTA | 23.6 | 286,000 | 27 Apr 1993 |
| 1873 | Improvement of Customs Valuation[1] | ADTA | 3.0 | 149,000 | 27 Apr 1993 |

**KEY PROGRAM DATA ($million)**

| | | As per ADB Loan Documents | Actual |
|---|---|---|---|
| Total Program Cost | | 20.58 | 20.74 |
| Foreign Exchange Cost | | 20.58 | 20.74 |
| ADB Loan Amount/Utilization | | 20.58 | 20.74 |
| | SDR million | 15.00 | 15.00 |
| ADB Loan Amount/Cancellation | | | 0.00 |
| | SDR million | | 0.00 |

| KEY DATES | Expected | Actual |
|---|---|---|
| Fact-Finding | | 21 Jun–1 July 1992 |
| Pre-appraisal | | 27 Sep–2 Oct 1992 |
| Appraisal | | 7–14 Dec 1992 |
| Loan Negotiations | | 22–30 Mar 1993 |
| Board Approval | | 27 Apr 1993 |
| Loan Agreement | | 3 May 1993 |
| Loan Effectiveness | 31 Aug 1993 | 22 Jun 1993 |
| First Tranche Disbursement | 31 Aug 1993 | 14 July 1993 |
| Second Tranche Disbursement | July 1994 | 5 Dec 1997 |
| Program Completion | 31 Dec 1995 | 12 Dec 1997 |
| Loan Closing | 31 Dec 1995 | 12 Dec 1997 |
| Months (effectiveness to completion) | 28 | 54 |

**BORROWER** Kingdom of Nepal

**EXECUTING AGENCY** Ministry of Finance

**MISSION DATA**

| Type of Mission | No. of Missions | Person-days |
|---|---|---|
| Appraisal | 1 | 16 |
| Country Consultation | 1 | 5 |
| Review | 3 | 20 |
| Operations Evaluation[2] | 1 | 42 |

ADB = Asian Development Bank, ADTA = advisory technical assistance, PPTA = project preparatory technical assistance, SDR = special drawing rights, TA = technical assistance.

[1] Technical assistance grant attached to the loan.

[2] The mission comprised A. Qureshi, Principal Evaluation Specialist (Mission leader); A. Ibrahim, Evaluation Specialist; and T. Heap, International consultant.

## EXECUTIVE SUMMARY

After the advent of democracy in the Kingdom of Nepal in 1991, the Government initiated a program of structural reforms for economic progress, supported by an Enhanced Structural Adjustment Facility (ESAF) from the International Monetary Fund. ESAF sought to ease controls on exchange and allow partial convertibility of the Nepalese rupee, thus creating an environment that would expand trade and investment, and an opportunity for complementary reforms in the industrial sector. In response to this opportunity, and to build on the continuing dialogue with the Government on the industrial sector, the Asian Development Bank (ADB) approved an Industrial Sector Program (ISP) in April 1993 for $20.6 million.

ISP was designed to support an agenda of policy and institutional reforms to enhance, on a sustainable basis, the efficiency of Nepal's industrial sector. It reinforced specific components of ESAF. The ISP objective conformed to the Government's priorities and ADB's country operational strategy. The ISP design focused on issues like rationalizing the tariff structure, easing import controls, liberalizing export regulations, and improving export incentives. ISP also sought to streamline customs procedures and industrial regulations and incentives, and to strengthen sector institutions. But its design did not delve deeply enough into the structure of Nepal's industrial sector. Nor did ISP target specific policy measures to improve the efficiency of particular subsectors, such as cottage and small industries, which offered a significant potential for pro-poor growth.

ISP implementation began before the ADB loan approval. Thereafter, 23 policy actions were to be taken within 28 months of loan effectiveness, including 10 actions before second tranche release. That was too ambitious. Implementation got delayed considerably, and was less than complete. Accordingly, the second loan tranche was released almost 3.5 years behind schedule. The delay was attributable to an overly broad policy agenda, frequent changes of government, and both an optimistic assessment of the implementation capacity of, and insufficient ownership building among, some government agencies.

ISP addressed some of the fundamental problems that impeded industrial sector development, especially high tariffs and multiple tariff bands, restrictive trade regulations, an outdated customs valuation system, investment restrictions, and weak interagency coordination. Policy and institutional reforms helped reduce costs of imports and exports, modernized customs valuation, made industrial inputs available at internationally competitive prices, and encouraged competition by lowering barriers to entry of small-scale producers and exporters. Nepal is now one of the most open economies in the South Asian subregion, with an average tariff rate of less than 10%, and deregulated industrial licensing.

ISP has had a substantial and visible overall impact on Nepal's industry and trade. Attributing the improvement in macroeconomic indicators exclusively to ISP is difficult, but industrial output, foreign trade, and private investments have increased substantially since ISP implementation. ISP also helped diversify the commodity base of Nepal's exports, while increasing their overall value.

ISP reforms have resulted in new institutional mechanisms to facilitate investments, customs valuation, and bonded warehousing. Organizational arrangements to monitor and control industrial pollution are also in place.

ISP has had less impact in areas like improvement of export incentives through reform of the duty drawback system, and equalizing the cost of land use between industries located inside and outside of industrial estates. There has been no significant impact in control of industrial pollution, despite relevant laws and regulations initiated since 1997.

Two technical assistance (TA) grants were attached to ISP. One grant provided advisory services to improve customs valuation, which resulted in successful implementation of the Automated System of Custom Data. The other TA grant was to build capacity for monitoring and evaluation of trends and progress in the implementation of reforms, and for the periodic reporting on their progress during the program period. This TA largely failed, because the consultants performed poorly.

Most of the major ISP reform measures were completed, although after considerable delay. The ISP design was relevant, but some aspects could have been better. Overall, ISP was efficacious, substantially achieving its objective. Although quantitative measurement is difficult, ISP appears to have improved the efficiency of revenue collection through indirect taxes, and to have reduced the cost of imports and exports. But ISP is assessed as less efficient because of slow implementation and, thus, delayed impact.

The Government remains firmly committed to maintain and build on the ISP reforms. Sustainability of the reforms and their impact is assessed as likely. ISP contributed significantly to capacity building of the main implementing agencies, although more work is necessary. On the whole, ISP is rated as successful.

The ISP experience confirms that macroeconomic adjustments, while necessary, were not sufficient to realize fully the potential for productivity and growth of Nepal's industrial sector. ISP relied almost exclusively on macroeconomic reforms. Future ADB assistance to Nepal's industrial sector should focus on cottage and small industries, and support diversification of export products and markets.

A few important lessons became obvious during ISP implementation. ISP called for completion of too many actions within a limited time, without adequately considering constraints on the capacities of implementing agencies. Furthermore, implementation involved too many agencies, some of which were not directly concerned with ISP actions. Lines of responsibility were not always clear for implementing some policies. Thus, coordination among the implementing agencies was not always smooth. Future programs should be more sharply focused, provide adequate time for implementation, and be preceded by sufficient ownership-building, especially among prospective implementation agencies.

Some important outstanding issues need to be addressed. First is the extension of regulations for pollution control across all industries, whether new or existing, and their strengthened enforcement. Second, governance of the Customs Department should be improved by streamlining of procedures and capacity building in the use of the Automated System of Custom Data. Another issue is leveling of the playing field between industries located inside and outside the industrial estates by raising rental rates that industrial estates charge to market level, and changing laws and rules to allow liens on fixed assets embedded in leased land. There is potential for ADB TA in all of these areas. Finally, the Government should provide continuing and adequate funding to ensure that the duty drawback system operates efficiently.

# I. BACKGROUND

## A. Rationale

1. The 1991 advent of democracy in Nepal, after a 30-year gap, brought a commitment to economic progress. This required prudent financial management, accompanied by structural reforms. Government efforts to bring about these changes were supported by the International Monetary Fund (IMF) through the Enhanced Structural Adjustment Facility (ESAF), covering the fiscal years (FYs) 1993–1995. Within this context, the Government decided in 1993 to allow free conversion of the Nepalese rupee on trade accounts. To increase the profitability of exporters, 100% convertibility of foreign currency earnings at market exchange rate was also allowed. Such policies established an environment that enabled expanded trade and investment, both domestic and foreign, and provided an opportunity for complementary reforms in the industrial sector.

2. The Industrial Sector Program (ISP) supported an agenda of policy and institutional reforms to enhance the efficiency of Nepal's industrial sector on a sustainable basis as the country moved to a more open market economy. It sought to build on the continuing dialogue between the Asian Development Bank (ADB) and the Government on the industrial sector, and to fine tune and reinforce specific components of the ESAF. The program loan modality was considered appropriate, as ISP formed an important component of the overall agenda for structural adjustment of the economy, and because experience suggested that project lending succeeded only in a sound policy environment backed by adequate institutional capacities.

## B. Formulation

3. The dialogue between ADB and the Government on the industrial sector began in 1984 when ADB provided technical assistance (TA) for a sector study,[1] which resulted in the Industrial Enterprise Act in 1987. A second sector study,[2] completed in March 1991, was followed by initiation of a range of policy and structural reforms, supported by ESAF, in monetary and fiscal policies; exchange rates; trade, industry, agriculture, and financial sectors; public resource management; and privatization. Within this overall framework, the Government sought ADB assistance to address problems facing the industrial sector. Although the areas of reforms had been broadly identified in the earlier sector studies, a program preparatory TA[3] implemented from April to June 1992 helped design the package and sequencing of the reforms that ADB would support.

4. The first stage of ISP reforms had already been initiated in March 1992 with easing of quantitative restrictions on imports, and allowing partial convertibility of the Nepalese rupee on trade accounts. A number of other reform measures, whose implementation was required before the first tranche of the ADB loan could be disbursed, were initiated before ISP approval (para. 23). These included moves toward a more open trade regime by rationalizing and lowering the tariff structure and reducing quantitative restrictions, promoting exports by liberalizing export regulations, improving export incentives and simplifying customs procedures, deregulating the industrial sector through elimination of licensing, and liberalizing foreign investment. The fact-finding mission for ISP was fielded in June and July 1992. In December 1992, an appraisal mission assessed the appropriateness of the proposed measures, confirmed

[1] TA 620–NEP: *Industrial Sector Study,* for $241,000, approved on 22 August 1984.
[2] TA 1047–NEP: *Second Industrial Sector Study,* for $525,000, approved on 19 October 1988.
[3] TA 1654–NEP: *Industrial Sector Program* , for $187,000, approved on 10 January 1992.

their adequacy as the basis for ADB assistance, and reached understanding with the Government on ISP objectives and scope. This was followed by ADB's approval of the ISP loan in April 1993.[4]

## C. Objectives and Scope

5. The principal objective was to create a policy environment that would increase industrial sector efficiency on a sustainable basis. To that end, ISP focused on seven main areas of policy and regulatory reform (Appendix 1):

(i) Rationalization of Tariff Structure: improving tariff classification, eliminating tariff discrimination among different importers, and reducing basic and additional tariff rates.

(ii) Liberalization of Import Controls: reducing quantitative restrictions on imports and enlarging the open general licensing (OGL) system to cover most imports.

(iii) Liberalization of Export Regulations: eliminating export duties and freeing export prices.

(iv) Improvement of Export Incentives: extending and simplifying the bonded warehouse (BWH) facility[5], and improving the duty drawback scheme (DDS).[6]

(v) Improvement of Customs Procedures: introducing a new customs valuation system, and streamlining customs procedures.

(vi) Streamlining of Industrial Regulations and Incentives: eliminating industrial licenses, liberalizing domestic and foreign investment, rationalizing industrial incentives, and reforming the excise duty and sales tax system.

(vii) Strengthening of Sector Institutions: improving coordination among various ministries and departments, and establishing institutions to control and monitor industrial pollution.

6. These reforms were expected to contribute to employment generation, income growth, and improved balance of payments, and to lead to greater reliance on market forces and increased participation of the private sector in industrial development after the envisaged trade liberalization, export promotion, and industry deregulation. ISP also focused on strengthening two institutions concerned with the formulation and implementation of trade and industrial policy: the Ministry of Industry (MOI) and the Department of Customs (DOC), and streamlining procedures for their effective operation.

## D. Financing Arrangements

7. ADB allocated SDR15 million (equivalent at the time of approval to $20.58 million)[7] to finance ISP. The loan was released in two equal tranches, in July 1993, and December 1997,

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[4] Loan 1229–NEP(SF): *Industrial Sector Program,* for $20.58 million, approved on 27 April 1993.
[5] BWH facility allows a manufacturer duty-free use of imported raw materials for manufacture of export products. At the time of ISP formulation, BWH facility was available only to the garment industry.
[6] DDS allows exporters to claim refund of import duty paid on inputs used for production of export products.

after implementation of the agreed reform measures specified in respective tranche conditions. The second tranche release was delayed by 41 months because of late compliance with tranche conditions, mainly due to political uncertainties, frequent changes in government, and constraints on implementation capacity (para. 29).

## E. Donor Coordination

8. Coordination with IMF was an important feature of ISP. The ESAF objectives included sustained higher rates of output growth and price stability over the medium term. Fiscal and monetary policies were tightened to achieve macroeconomic stability, while various growth-enhancing structural reforms were pursued to promote private sector activities, and to better integrate Nepal's economy with the world economy. Reforms focused on the exchange and trade system, public resource management (including the tax system), public enterprise reform, civil service reform, financial sector liberalization, and improved sectoral policies.

9. ESAF was scheduled to end in October 1995. As the Government failed to meet the agreed macroeconomic targets and complied only partially with ESAF conditionalities, only half of ESAF funds (SDR16.8 million) was disbursed. By the time of IMF's last Article IV consultation, in February 1997, all macroeconomic benchmarks were met, even though the necessary structural reforms and policy measures were still ongoing. Because ISP reinforced specific components of ESAF, whose implementation had been delayed, disbursement under the ISP loan followed the same pattern with the final tranche released on 5 December 1997, almost 3.5 years behind schedule (although factors internal to ISP design and implementation also contributed to the delay, paras. 10 and 29). ISP was preceded by two Structural Adjustment Credits that the World Bank provided, covering the period from FY1988 to FY1990 ($50 million for agriculture sector reform) and FY1990 to FY1993 ($60 million for financial sector reform).

## F. Program Completion Report Findings

10. A program completion report (PCR) was prepared at ADB headquarters in October 1998, with assistance from the Nepal Resident Mission (NRM). The PCR highlighted three lessons. First, before designing a program, the political climate and the resources[8] of the country concerned must be carefully assessed. The seven areas of reform, requiring 49 policy actions, were considered too many for a country like Nepal. Second, weak governments have difficulty implementing politically sensitive reforms within a relatively short time span. The 28-month period from loan effectiveness to scheduled loan closing was deemed insufficient for the Government to implement the ISP reform agenda. Third, the implementation responsibilities of the 10 ministries and departments involved should have been specified more clearly. These were considered the main reasons for the 3.5 year delay in implementation.

11. The PCR noted five areas where performance was less than satisfactory: (i) providing adequate resources for DDS; (ii) awarding duty drawback within 60 days of the date of application; (iii) monitoring industrial pollution; (iv) raising rents at the industrial estates to market rates; and (v) submitting trend, progress, and impact assessment (TPIA) reports, which MOI was to prepare after periodic consultations with the private sector and concerned government agencies. The PCR noted the need for ADB to continue policy dialogue to ensure

[7] The loan was relatively small in comparison with total foreign aid commitments and disbursements in the year of its approval (10%) and during the planned program period (3%).

[8] The PCR appears to use the word "resources" in the sense of implementation capacity.

that one of the remaining conditionalities—raising the rents at the industrial estates to comparable market rates—was complied with fully. The PCR rated ISP as generally successful,[9] while acknowledging the implementation delay.

## G. Operations Evaluation

12. The evaluation presented in this report focuses on pertinent aspects of ISP, and presents the findings and assessment of the Operations Evaluation Mission (OEM) that visited Nepal in November/December 2001, on ISP's effectiveness in achieving its objectives and generating the desired benefits, and the sustainability of industrial reforms (see Appendix 1 for the evaluation framework). The report is based on a review of ADB's internal records, including the PCR and the report and recommendation of the President, the data that OEM collected in the field; and discussions with concerned ADB staff, executing and implementing agencies of the Government, representatives of multilateral institutions, and civil society and the private sector.

13. While most of the OEM findings are consistent with the PCR conclusions, the former differ from the position stated in the PCR on the status of actions in three areas. The first is related to industrial pollution standards, regulations, and monitoring. ISP called for the industrial pollution control measures to cover both existing and new industries, but as of December 2001, standards had been legislated only for new plants in five industries that were heavy polluters in terms of industrial effluents discharged to inland surface waters. Even for this reduced scope, regular monitoring capacity is lacking, and is generally limited to ad hoc surveys, often in response to public complaints. Also, the study on implementation of a pollution tax called for by ISP was not done. The PCR assessed these three policy measures as being complied with. OEM, however, considers the first two as only partially complied with (both were conditions for the second tranche release), and the third as not complied with.

14. The second area where the PCR and this evaluation diverge is related to another second tranche release condition: increasing rents at the industrial estates to comparable market rates. The PCR accepted substantial compliance, based on information that the Government had increased rents by 50% in both 1994 and 1996. But the data provided to OEM by the Industrial District Management (IDM), the organization responsible for managing industrial estates in Nepal, shows that the rents remained constant from 1992 to 1997, when they were raised by 40%. The gross domestic product (GDP) deflator increased at a higher rate of 45.8% during the period from FY1993 to FY1997. Thus, this single increase during ISP implementation did not even maintain the real rental levels, which were significantly lower than market rates before ISP approval. Therefore, the OEM considers that the Government did not comply with this condition.

15. The third area of divergence is on TPIA reports, which were required to be prepared in consultation with government agencies and the private sector, and submitted to ADB semi-annually for 5 years. The PCR acknowledged receipt of only 3 of the 10 TPIA reports, but OEM has been able to locate only two of them. The first one, submitted in December 1995, did not include an impact assessment. The second, covering the June–December 1996 period, was submitted to ADB in September 1997. Although more detailed than the first, it contained mostly published statistics, and included neither an analysis of the impact of reform measures on the industrial sector, nor progress of ISP. The PCR rated this condition as substantially complied with, but OEM considers compliance partial, at best.

[9] Using the previous three-category rating system (generally successful, partly successful, and unsuccessful).

## II. IMPLEMENTATION EXPERIENCE AND RESULTS

### A. Effectiveness of Design

16. The program design generally conformed to government priorities. The Government's Eighth Five–Year Plan, covering FY1993–FY1998, clearly mandated a new direction that would make participation of the private sector more important in the development process, while giving all levels of government a facilitating role. This was in sharp contrast with the role of government envisaged in the previous plan, which emphasized intervention and control. The key strategies included the promotion and diversification of exports, and reform of public administration. Thus the industrial sector, which had been the main engine of Nepal's past export growth, was a natural candidate for policy attention in the context of further expanding exports.

17. The ISP design was consistent with its objectives, and with ADB's country operational strategy[10] that recognized the long-term potential for industrial development in Nepal's economy. The principal objective was to move to a more open economy, and establish a policy environment that would increase the industry sector's efficiency and international competitiveness on a sustainable basis. ISP essentially focused on some of the broader issues affecting the sector rather than targeting particular industries or subsectors. Industry-level initiatives were left to the ingenuity of the private sector. ISP also did not address efficiency issues in public enterprises. The objective of increasing sector efficiency could have been better served by more specific and sector-targeted measures, such as establishing a training institute for carpet design, and providing technical expertise, particularly to the cottage and small industry (CSI) subsector. The ISP design could have focused on CSIs to harness their strength for greater impact, considering that they accounted for 65% of Nepal's total exports, 70% of total industrial output, and 85% of industrial sector employment.

18. ISP supported greater reliance on market forces, but did not sufficiently consider the Trade and Transit Treaty with India, through which Nepal mirrors India's trade policies. Thus, while the treaty favors Nepal in trade with India, it also limits Nepal's trade with third countries because Indian export incentives have reduced the competitiveness of Nepalese exports of comparable products to third countries.

19. ISP tried to encourage exports by eliminating export duties and reducing the cost of export business. This was seen as crucial to the development of Nepal's fledgling economy, particularly to generation of greatly needed foreign exchange. At the time of program formulation, however, different sponsors seem to have given conflicting advice to the Ministry of Finance (MOF). The policy framework supported through ESAF emphasized fiscal prudence to reduce inflation and protect external competitiveness, but the export incentives foreseen in ISP would lower government revenue. However, there is now improved coordination and cooperation among development partners, so confusion seems unlikely in the future.

20. ISP was too broad, involving 49 policy actions, and the 28–month period allocated to implement those policies was too short, considering Nepal's implementation capacity. The coordination group established to facilitate implementation included too many agencies some of which, such as the National Planning Commission (NPC) and the Nepal Rastra Bank (NRB, the central bank), had only a small role in implementing the reforms. Some implementing agencies claimed they had not been involved in program formulation, an indication of weak ownership. The Government feels strongly that the program design lacked coherence in that it sought to

[10] The Operational Strategy for Nepal, February 1993.

achieve disparate policy objectives.[11] The Government view is that the component on industrial pollution control was inconsistent with the overall objective of enhancing industrial sector efficiency. It appears that the Government has not sufficiently committed itself to linking the goal of sustainable economic development with the need to control industrial pollution. The Government believes that a "pro poor" development strategy cannot be realized if the environmental pollution agenda supersedes the objective of industrial development.

21. Finally, the design failed to identify key performance indicators to assess and monitor the impacts of the policy reforms during ISP implementation, or after its completion. This task was left to the consultants engaged under one of the TAs attached to the ADB loan (para. 36). The lack of performance indicators in the TPIA framework is considered a design deficiency.

### B. Implementation of Policy Reforms

22. Program implementation was to be completed within 28 months after the loan effectiveness date, i.e., by December 1995. But implementation was partial, and delayed considerably. Accordingly, disbursement of the second tranche, which was to take place within 11 months from loan effectiveness, did not occur until 5 December 1997—almost 3.5 years behind schedule, and after four extensions to the original loan closing date of 31 December 1995.

23. A significant part of ISP was implemented before its approval (Appendix 1). The Government reported that 26 policy actions had been completed, concerning liberalization of import controls and export regulations, improvement of export incentives, and streamlining of industrial regulations and incentives. Notable among the policy actions were: elimination of tariff discrimination among different types of imports, importers, and end-uses; equalization of tariff protection by reducing certain tariff rates, as well as reducing rates of additional tariffs to reflect the true prices of imports from India and other countries; reduction of quantitative restrictions, convertibility of the Nepalese rupee on trade accounts, and substantial replacement of import license auctions with the open general licensing (OGL) system; abolishment of export licenses, except for essential agricultural commodities; broadening the use of BWHs and simplification of relative procedures; liberalization of industrial licensing regulations, provision of legal framework for foreign investment, and establishment of a one window committee to facilitate foreign and domestic investment; and the phased reduction in the number of excisable items from 52 to 11.

24. Several of these actions, however, failed to produce the desired results. First, in export regulations, the floor price for carpet exports was not eliminated, and DDS remained (and still largely remains) cumbersome. Second, although the Government granted export processing zone status (i.e. duty exemption) to firms exporting 90% or more of their output, in practice, no firm has been awarded this status. Yet the BWH scheme remains in use. Third, despite several experiments in instruments, modalities, and procedures, DDS has not worked effectively. The Government has not allocated sufficient budget to quickly meet obligations for duty refunds,[12] but DDS may function better in the future, now that the Government has decided to fully refund the accepted duty drawback claims by issuing interest-bearing bonds.[13] Fourth, policy actions on control of industrial pollution are far from complete, although progress has been in the right

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[11] The Government considered inclusion, as a policy action, of the need to raise rental levels for industrial land to market value as conflicting with established industrial incentives, and not addressing a major economic distortion.

[12] By one estimate that the private sector provided to OEM, pending DDS claims amounted to more than NRs800 million in December 2001.

[13] Private sector stakeholders, however, complained about the low interest rate of 5% paid on the bonds, compared with 12% cost of capital.

direction. Environmental standards for new industries were issued only recently, but existing industries remain largely outside the regime of pollution control (para. 13). Furthermore, monitoring and enforcement have not yet been adequately addressed, since the general approach to pollution control embodied in the Environmental Protection Regulation (EPR) emphasizes industry consultation and public participation, rather than a strict penalty-based enforcement regime as embodied in the Industrial Pollution Control Regulations (IPCR) recommended by ADB TA consultants.[14] Finally, although rental rates in industrial estates have been raised, they remain substantially lower than comparable market rates (para. 26). One reason that the tenants have resisted rental increases—more than 15% every 2 years since 1999—is that they cannot offer fixed assets as collateral for bank credit, because IDM holds the land titles.[15]

25. Changes in DDS have not significantly increased the use of this facility, nor reduced the backlog of claims for refund of import duty. This is despite the increase in claim payments from NRs0.4 million in FY1993 to NRs25.0 million in FY1997, and NRs153.0 million in FY2001 (Table 1). But such payments have been small, as a percentage of related government tax revenue: 0.1% in FY1998, rising to 0.5% in FY2001.

**Table 1: Duty Drawback Approved by One Window Committee**
(NRs million)

| **Item** | **Fiscal Year** | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | **1993** | **1994** | **1995** | **1996** | **1997** | **1998** | **1999** | **2000** | **2001** |
| Custom Duty | 0.4 | | 5.1 | 13.6 | 25.0 | 22.6 | 50.3 | 82.2 | 153.0 |
| Premium | 0.2 | | 0.0 | | | | | | |
| Excise Duty | | | 0.0 | | | | | | |
| Sales Tax | | | 1.0 | | | | | | |
| Total | 0.6 | 10.1 | 6.2 | 20.6 | 25.0 | 22.6 | 50.3 | 82.2 | 153.0 |
| **Total Number of Decisions** | **120** | **742** | **719** | **722** | **482** | **129** | **316** | **367** | **432** |

Source: Industrial Statistics, Department of Industries, 2001.

26. Table 2 shows rental rates for Balaju Industrial Estate in Kathmandu, which mirror rates in other main estates. As noted in para. 14, the single increase in rental rates during the program period did not even maintain the real rental levels, which were already significantly below market rates. Over the longer period from FY1993 to FY2002, the overall increase in nominal rental levels was 85%, equivalent to a 13% increase in real terms. Nevertheless, industrial estate rentals still remain considerably lower than market rates.

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14 Fines incorporated in the EPR are minimal: NRs50,000–NRs100,000 compared with NRs100,000 per day under IPCR.

15 Inadequate infrastructure on industrial estates, particularly utility services, such as electricity and water, was also cited.

**Table 2: Industrial Estate Rental Levels: Balaju Estate**

| Fiscal Years | Rental Levels (NRs)[a] Land | Shed | Warehouse | Increase (%) | Equivalent GDP Deflator (%) |
|---|---|---|---|---|---|
| 1993 | 1,800 | 1.20 | 1.60 | | |
| 1994 | 1,800 | 1.20 | 1.60 | | |
| 1995 | 1,800 | 1.20 | 1.60 | | |
| 1996 | 1,800 | 1.20 | 1.60 | | |
| 1997 | 1,800 | 1.20 | 1.60 | | |
| 1998 | 2,520 | 1.68 | 2.24 | 40.0 | 45.8 |
| 1999 | 2,520 | 1.68 | 2.24 | | |
| 2000 | 2,898 | 1.93 | 2.58 | 15.0 | 1.1 |
| 2001 | 2,898 | 1.93 | 2.58 | | |
| 2002 | 3,333 | 2.22 | 2.97 | 15.0 | 13.4 |
| **Increase from FY1993 to FY2002** | | | | **85.2** | **72.2** |

[a] Land: per ropani (5,476 sq.ft.) per annum; Shed: per sq.ft. per month; Warehouse: per sq.ft. per month.
Source: Industrial District Management.

27. Of the remaining 23 policy actions, 10 were agreed to be completed before the second tranche release. The Government considered that all these actions had been complied with (although with the 3.5 year delay), except for the raising of rental rates on industrial estates. However, OEM has concluded that compliance was less than complete in terms of expected outcomes. First, it is not clear whether the 1994 survey of duty drawbacks actually confirmed that export-oriented industries with backward linkages were able to benefit from a simpler DDS. Second, as mentioned earlier, the industrial pollution control measures taken so far are only partial. Furthermore, although the EPR was approved in July 1997, its full enforcement is still not possible, because compliance plans for pollution control in existing industries remain in the development phase.

28. Performance was also mixed in implementation of 13 policy actions that were not tied to the second tranche. Notable were actions on liberalization of import control, streamlining of industrial licensing, establishment of guidelines for environmental impact assessment and initial environment examination, and a study on the implementation of a pollution tax. Export incentives such as DDS do not work effectively because procedures are complex and time consuming, and budget allocations are lacking. A passbook system was recently introduced to simplify the duty refund process, but its efficacy has not been tested. In particular, CSIs are virtually unable to benefit from DDS, because those that export mostly source their imported raw materials domestically. Purchase costs include import duty as well as the value added tax, so the CSIs are entitled to duty drawback—but in practice, they do not benefit from DDS because they have limited knowledge of the procedures involved. Furthermore, although export duties have been withdrawn on many products, the private sector views the 0.50% service charge on exports, and the 0.75% withholding tax on export revenues, as similar to export tariffs. Also, as mentioned earlier, the monitoring and control of industrial pollution remains weak. Finally, the envisioned institutional strengthening of DOC and MOI, on a sustainable basis, was only partial. In particular, the TA provided to MOI for this purpose was not effective because the consultants' performance was inadequate (para. 36).

29. In summary, ISP implementation was delayed considerably and some issues, like comprehensive industrial pollution control, are still being addressed. Implementation was slow

mainly because frequent changes of government[16] delayed passage of policy changes and associated legislation, and created an atmosphere of uncertainty among senior civil servants as to the Government's commitment to the reform package. Implementation was also delayed because of inadequate capacity among the concerned departments and agencies; ineffective coordination and frequent personnel changes in those agencies; the ambitious nature of ISP relative to the 28–month implementation period; and unsatisfactory performance of the TA consultants who helped the Government monitor and assess the impact of reforms.

## C. Management of Program

### 1. By Government

30. Program implementation required coordination of all ministries concerned . MOF had the overall responsibility of ensuring that policies adopted and actions taken before the loan became effective would continue; and that all other policies and actions would be implemented. Coordination between MOF, the designated Executing Agency, and NPC, NRB, Department of Industry (DOI), Ministry of Commerce (MOC), DOC, and other ministries and departments concerned was managed through a high-level program coordination committee, chaired by Secretary, MOF. Given its complexity and the number of agencies involved, ISP could have been implemented more efficiently had a suitably staffed program implementation unit helped the coordination committee.

31. Organizational arrangements in Nepal are complex and difficult because of the intertwined responsibilities of ministries, which are predominantly policy-related, and related departments and agencies, which are mainly concerned with operational matters. MOF and DOC actions were required for tariff structure reforms (seven policy action areas), liberalization of import control (five policy action areas), liberalization of export controls (four policy actions), and improvement of customs procedures (three policy actions). These reforms proceeded smoothly, mainly because DOC was organizationally responsible to MOF. Implementation of improvements in customs procedures was delayed, because the frequent changes of government slowed the legislative process and DOC's capacity was limited. The improvement of export incentives (13 policy action areas) and streamlining of industrial regulations (17 policy action areas) predominantly involved MOI, DOI, MOC, MOF, Ministry of Population and Environment (MOPE), Nepal Bureau of Standards and Metrology (NBSM), IDM, Inland Revenue Department[17], and DOC. The complexity of working across areas of responsibility and reporting lines of many ministries and departments caused late and incomplete implementation in these policy action areas, particularly in DDS and industrial pollution control. Success in reform implementation and harmonized departmental responsibilities across ministerial boundaries seems to be directly related. The reforms are also implemented better when the implementing department and ministry are in a line relationship, as with tariff rationalization and improvement of customs procedures.

32. The Government's monitoring, and reporting on, ISP implementation was insufficient. A number of key agencies lacked qualified staff and administrative capacity, including DOC, DOI, NBSM, MOPE, and MOI's Planning and Monitoring Unit. Those agencies preferred to continue with ad hoc incentives to preferred industries. Furthermore, MOI found it difficult to meet the reporting requirements, and TA consultants did not help them adequately.

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[16] The government changed four times during the envisaged 28-month implementation period.
[17] Created through merger, during ISP, of the Department of Excise Duty and the Department of Sales and Tax.

33. Despite the substantial delay in implementation, the Government has generally maintained the policy reforms that ISP envisaged. There has been no significant policy reform reversal.

### 2. By ADB

34. NRM monitored ISP implementation from 1993 to late 1995, when monitoring was shifted to headquarters. Three missions from headquarters were fielded from February 1996 to May 1997 to review implementation progress and conduct policy dialogue with government representatives on delayed reforms. In addition, a country consultation mission from ADB headquarters reviewed the compliance status of second tranche conditions in May 1994. Apart from these missions, NRM staff regularly monitored implementation progress and continued policy dialogue with the Government to expedite ISP and ensure there was no policy reversal. No government PCR was found by OEM; it is believed none was prepared, even though it was required by the Loan Agreement.[18] No formal PCR mission was fielded; the PCR was prepared, with NRM assistance, at ADB headquarters in October 1998.

35. Program monitoring was less rigorous than it should have been, given the cautionary remarks made during Board consideration of ISP, particularly regarding Nepal's inadequate institutional capacity. The first formal review mission was conducted over 7 days in February 1996, and the first extension of the loan closing date, from 31 December 1995 to 30 June 1996, was approved after that mission. The next review mission was conducted over 4 days in October 1996, followed by the second extension of the loan closing date, to 31 December 1996. The final review mission was conducted over 9 days in April 1997, and resulted in the third extension of the closing date, to 15 June 1997.[19] ADB records indicate that the delays were largely because of the Government's failure to implement the agreed reform actions, despite continual NRM follow-up. More rigorous follow-up and more frequent review missions might have reduced such delays.

### 3. Effectiveness of Technical Assistance

36. ISP was accompanied by two TAs, with a combined input of 9 person-months of international and 18 person-months of domestic consulting services. The first TA[20] was to establish the TPIA system, help MOI prepare semiannual TPIA reports, and design a proper mechanism for coordination among various government agencies as well as the private sector. The consultants—both international and domestic—performed poorly, failing to meet the requirements of their terms of reference, and taking 2.5 years to complete the final report. The team leader was not available to conduct a seminar scheduled after submission of the draft final report, even though it had been agreed in the consultants' contract. A new team leader was brought in, but he was not familiar with the draft final report, and conducted the required seminar only 2.5 years after its completion. The TA was, therefore, ineffective in developing TPIA capacity in MOI, as well as in establishing formal coordination mechanisms on monitoring and evaluation of reforms. Thus by late 2001, MOI had completed only 3 of the 10 semiannual TPIA reports required for ISP—and those reports lacked substance.

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[18] Loan Agreement LAS:NEP 23085 between Kingdom of Nepal and Asian Development Bank, Schedule 5, Item I (F), Program Completion Report (para. 6).

[19] The fourth and final extension of the loan closing date, to 31 October 1997, did not require fielding of a mission. The loan account was, however, kept open until 12 December 1997 to allow eligible payments.

[20] TA 1872–NEP: *Monitoring, Impact Assessment, and Management of Policy Reforms*, for $286,000, approved on 27 April 1993.

37. The second TA,[21] to improve the customs valuation system, was implemented successfully. The TA was completed and its final report submitted on time, in March 1994. The report recommended revising customs legislation to adopt the valuation system of the General Agreement on Tariffs and Trade, based on the transaction value, thereby reducing the discretion of customs officers. DOC accepted the consultant's recommendations, and amended the Customs Act in November 1997. The delay in legislation was because of several changes of government during FY1994–FY1997. The consultants trained DOC staff and helped in the successful launching of the Automated System of Custom Data (ASYCUDA).

## D. Assessment of Program Results

38. ISP was designed to increase the private sector's role in a market-based economy, and to develop an outward-looking and internationally competitive industrial sector. A review of growth in the manufacturing sector, and in manufacturing exports, shows emergence of positive trends that may have largely been caused by ISP reforms.[22] The manufacturing production index (Table 3) during the period from FY1988 (5 years before the ISP policy actions) to FY2001 (4 years after ISP completion) showed an average annual growth of 9.0%, using FY1987 as the base year. The annual growth significantly accelerated in the post-ISP period (15.4% during FY1997–FY2001 versus 6.1% in FY1988–FY1993 and 6.5% in FY1993–FY1997). The trends for individual product categories, however, varied markedly with half of the manufacturing subsectors experiencing decelerating growth.[23]

39. Growth was healthy in the export of manufactured goods over the period from FY1988 to FY2001 (Table 4), but the growth pattern was less clear for the pre-ISP, ISP, and post-ISP periods, and results varied markedly for individual product categories. Notably, the average annual growth rate of total exports decelerated during ISP implementation (probably reflecting the lagged effect of ISP) but recovered substantially in the post-ISP period, though remaining below the pre-ISP annual growth rates. But in absolute value, the average annual increase improved significantly in the post-ISP period.

40. The industrial production and trade trends reflect the positive impacts of tariff reforms (improvement of tariff classification, elimination of tariff discrimination, reduction and equalization of basic tariff rates across sectors, and additional tariff reductions); other import liberalization measures (reduction of quantitative restrictions and elimination of import licenses); and improvement of customs procedures (transfer of cargo handling to Tribhuvan International Airport, and improved customs valuation system). These tariff reduction measures have resulted in an overall tariff rate of less than 10%—the lowest in South Asia—helping improve efficiency of the industrial sector.

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[21] TA 1873–NEP: *Improvement of Customs Valuation*, for $149,000, approved on 27 April 1993.
[22] See Appendix 2 for key economic statistics.
[23] Whether this was entirely or significantly a result of ISP is difficult to establish.

### Table 3: Production Index of Manufacturing Industries (FY1987=100)

| Item | Weight (%) | Fiscal Year 1988 | 1993 | 1997 | 2001[a] | Annual Growth Rate (%) 1988–1993 | 1993–1997 | 1997–2001 |
|---|---|---|---|---|---|---|---|---|
| Food Manufacturing | 19.3 | 112 | 219 | 309 | 957 | 14.4 | 9.0 | 32.7 |
| Beverage Industries | 3.9 | 148 | 234 | 258 | 316 | 9.6 | 2.5 | 5.2 |
| Tobacco Manufacturing | 20.1 | 107 | 133 | 133 | 118 | 4.5 | 0.0 | -2.9 |
| Manufacture of Textiles | 18.1 | 97 | 93 | 146 | 165 | -0.8 | 11.9 | 3.1 |
| Leather and Leather Products | 2.3 | 51 | 68 | 87 | 26 | 5.9 | 6.4 | -26.1 |
| Footwear Manufacturing | 0.4 | 177 | 680 | 455. | 586 | 30.9 | -9.6 | 6.5 |
| Wood and Wood Products | 2.0 | 63 | 26 | 36 | 45 | -16.2 | 8.5 | 5.7 |
| Paper and Paper Products | 0.9 | 177 | 249 | 499 | 1,516 | 7.1 | 19.0 | 32.0 |
| Manufacture of Other Chemical Products | 6.0 | 99 | 132 | 231. | 338. | 5.9 | 15.0 | 10.0 |
| Manufacture of Rubber Products | 0.6 | 131 | 142 | 99 | 111. | 1.6 | -8.6 | 2.9 |
| Manufacture of Plastics Products | 1.3 | 119 | 215 | 227. | 120. | 12.6 | 1.4 | -14.7 |
| Other Non Metallic Mineral Products | 16.9 | 122 | 121 | 122 | 108. | -0.2 | 0.2 | -3.0 |
| Iron and Steel Based Industries | 3.1 | 74 | 175. | 311. | 394. | 18.8 | 15.5 | 6.1 |
| Manufacture of Cutlery and Hand Tools | 3.2 | 92 | 86 | 56 | 12 | -1.3 | -10.2 | -32.0 |
| Manufacture of Electricals, Industrial Machinery Apparatus, and Appliances | 1.9 | 122 | 90 | 219. | 295. | -5.9 | 24.9 | 6.1 |
| **Overall Index** | **100.0** | **107** | **144** | **185** | **328** | **6.1** | **6.5** | **15.4** |
| Manufacturing GDP: | | | | | | | | |
| at FY1995 prices (NRs million) | | 10,142 | 17,075 | 22,826 | 27,605 | 11.0 | 7.5 | 4.9 |
| at Current prices (NRs million) | | 4,615 | 14,618 | 24,816 | 35,566 | 25.9 | 14.1 | 9.4 |

FY = fiscal year, GDP = gross domestic product.
[a] Provisional
Source: Economic Survey, Ministry of Finance 2002.

### Table 4: Exports by Main Commodity Group

| Item | Fiscal Year (NRs million) 1988 | 1993 | 1997 | 2001 | Annual Growth Rate (%) 1988–1993 | 1993–1997 | 1997–2001 |
|---|---|---|---|---|---|---|---|
| Food and Live Animals | 804 | 1,863 | 2,662 | 4,777 | 18.3 | 9.3 | 15.7 |
| Tobacco and Beverages | 10 | 13 | 15 | 76 | 5.4 | 3.6 | 50.0 |
| Crude Materials and Inedibles | 514 | 532 | 663 | 751 | 0.7 | 5.7 | 3.2 |
| Animals and Vegetable Oils and Fats | 171 | 176 | 313 | 4,102 | 0.6 | 15.5 | 90.3 |
| Chemicals and Drugs | 13 | 29 | 1,353 | 4,042 | 17.4 | 161.4 | 31.5 |
| Classified by Materials | 1,602 | 10,298 | 11,029 | 18,910 | 45.1 | 1.7 | 14.4 |
| Miscellaneous Manufactures [a] | 1,001 | 4,355 | 6,602 | 22,896 | 34.2 | 11.0 | 36.5 |
| Errors and Omissions [b] | | 20 | 26 | 123 | | | |
| **Total Exports** | **4,115** | **17,286** | **22,663** | **55,677** | **33.2** | **7.0** | **25.2** |

[a] Including mineral fuels and lubricants, machinery and transport equipment, and articles not classified.
[b] Represent data inconsistency within the same source.
Source: Economic Survey, Ministry of Finance 2002.

# III. PROGRAM IMPACT

## A. Economic Impact

41. The overall impact of ISP on Nepal's industrial and trade sectors has been positive. That is confirmed by data on manufacturing output and exports, and by favorable feedback from stakeholders. Although macroeconomic trends cannot be linked directly to ISP measures, they can indicate the likely direction of the impacts of policy reforms because of their contributory influences. As shown in Table 5, the growth rates of key industry and trade parameters exceeded GDP growth during the ISP period, from FY1993 to FY1997. Macroeconomic indicators also suggest general sustainability of the reform benefits in the post-ISP period, as the average growth rates of industrial production, total exports, and total imports in FY1993–FY2001 continued to exceed the GDP growth.

**Table 5: Selected National Account Output and Trade Statistics**

| | **Fiscal Year (NRs million)** | | | | **Annual Growth Rate** (%) | |
|---|---|---|---|---|---|---|
| **Item** | **1988** | **1993** | **1997** | **2001** | **1993–1997** | **1993–2001** |
| GDP (FY1995=100) | 148,405 | 188,782 | 233,040 | 280,339 | 5.4 | 5.1 |
| Manufacturing Output | 10,412 | 17,075 | 22,826 | 27,605 | 7.5 | 6.2 |
| Manufacturing Output as % of GDP | 7.0 | 9.0 | 9.8 | 9.9 | | |
| Total Exports (FOB) | 4,115 | 17,286 | 22,663 | 55,677 | 7.0 | 15.7 |
| Total Imports (CIF) | 13,870 | 39,260 | 93,662 | 115,797 | 24.3 | 14.5 |
| **Trade Deficit** | **9,755** | **21,974** | **70,999** | **60,121** | | |

CIF = cost, insurance, and freight, FOB = free on board, GDP = gross domestic product.
Source: Economic Survey, Ministry of Finance 2002.

42. ISP's long-term impact on Nepal's balance of payments is hard to judge at this stage, because the trade reforms have encouraged both imports and exports. Nepal's trade balance deteriorated during the ISP period, but has improved marginally post-ISP, indicating a limited, lagged impact. The trade deficit in the 4-year implementation period increased significantly, from NRs22 billion in FY1993 to NRs71 billion in FY1997. After ISP completion, the trade deficit decreased to NRs52 billion in FY1999, and appears to have subsequently stabilized at about NRs60 billion. Overall, ISP's beneficial impact can be seen in a three-fold increase in the total value of foreign trade over FY1993–FY2001, and a decline in trade deficit as a proportion of total value of trade from 38% in FY1993 to 35% in FY2001.

43. Some diversification of export products has occurred following ISP implementation (Table 6), which is a positive and sustainable impact of the trade sector reforms. This is evident in the decline in the share of the top two export categories—carpets and ready made garments—from 77% of total export value in FY1993 to 65% in FY1997 and 38% in FY2001. A diverse range of new products entered the export arena, including jute products, sacking, oil cake, rice products, and ginger. On the other hand, export concentration by destination country increased with the top three export destinations—Germany, India, and the United States—increasing their share of export value from 79% to 83% during the years of ISP implementation, and to 86% in FY2001.

**Table 6: Selected Export Data**

| Export by Destination | Fiscal Year (NRs million) 1993 | 1997 | 2001 |
|---|---|---|---|
| India | 1,622 | 5,226 | 27,304 |
| USA | — | 5,930 | 14,974 |
| Germany | — | 7,652 | 6,178 |
| Subtotal (Germany, India and USA) | –– | 18,808 | 48,456 |
| Other Countries | — | 3,828 | 8,064 |
| Subtotal (All countries) | 17,267 | 22,636 | 56,520 |
| Errors and Omissions[a] | 19 | 27 | (843) |
| **Total Exports (FOB)** | **17,286** | **22,663** | **55,677** |
| Top Exports by Destinations (Germany, India and USA) % | 79.0 | 83.1 | 85.7 |
| Carpets and Ready Made Garments: | | | |
| Value | 13,261 | 14,759 | 21,717 |
| % of total exports | 76.8 | 65.2 | 38.4 |

–– = not available, FOB = free on board.
[a] Represent inconsistencies between the data on total value of exports published in Economic Survey, 2002 and the data on export by destination obtained from the Trade Promotion Centre.
Sources: Economic Survey, Ministry of Finance, 2002; Nepal Country Assistance Evaluation, World Bank, 1999; and Nepal Overseas Trade Statistics, Trade Promotion Centre, 1999–2001.

44. ISP implementation provided an initial boost to Nepal's traditional export items—carpets, garments, and pashmina[24]—which constituted most of the country's exports. But the trend has reversed in recent years, because of (i) competition from Indian carpets of similar designs; (ii) failure of Nepalese carpets to meet third-country demand for modern designs; (iii) smuggling of Nepalese pashmina to India where it is re-exported to third countries, with the exporters taking advantage of India's export incentives; and (iv) Nepal's narrow export base in general. Increased private sector participation in the economy is reflected in statistics for the private sector component of gross fixed capital formation (GFCF), which grew, at current prices, from 59% in FY1988 to 68% in FY1997 (Table 7). Direct foreign investment as a percentage of GFCF increased from 0.7% in FY1993 to 2.7% in FY1997. After ISP, the private sector component of GFCF gradually declined to pre-program levels, and was 63% in FY1999, and 60% in FY2001. But in absolute terms, the private sector GFCF has continued to grow, although at lower rates in nominal terms.

[24] Pashmina is a type of animal wool produced in Nepal. In this report, the word "pashmina" is used in a generic sense and refers to products made out of this wool.

**Table 7: Selected Capital Formation Data**

| Item | Fiscal Year (NRs million at Current prices) 1988 | 1993 | 1997 | 2001 | Annual Growth Rate (%) 1988–1993 | 1993–1997 | 1997–2001 | 1993–2001 |
|---|---|---|---|---|---|---|---|---|
| GFCF | 13,414 | 37,278 | 60,794 | 78,017 | 22.7 | 13.0 | 6.4 | 9.7 |
| Private Sector | 7,931 | 25,509 | 41,402 | 46,727 | 26.3 | 12.9 | 3.1 | 7.9 |
| Private Sector as % of GFCF | 59.1 | 68.4 | 68.1 | 59.9 | | | | |
| FDI | –– | 261 | 1,621 | –– | –– | 57.9 | –– | –– |
| FDI Net Inflow as % of GFCF | –– | 0.7 | 2.7 | –– | | | | |

–– = not available, FDI = foreign direct investment, GFCF = gross fixed capital formation.
Source: Ministry of Finance, Economic Survey FY2002, National Accounts of Nepal, Central Bureau of Statistics, 2000.

## B. Social Impact

45. ISP's impact on social conditions—poverty reduction and gender issues—is hard to measure. That is partly because much of Nepal's population is engaged in subsistence activities and thus is less affected by developments in the monetized economy. Higher industrial production will in time, through backward linkages, increase opportunities in CSIs, where most of the poor may be employed. ISP may have indirect impacts through increased industrial employment, which rose steadily from 355,058 persons in FY1994 to 392,421 in FY2000, compared with an anticipated temporal displacement of 3,000 workers as estimated in the report and recommendation to the President. But establishing a direct correlation between ISP actions and employment growth is difficult. That is probably why specific beneficiary target groups were not identified in the ISP design.

## C. Institutional Impact

46. Measures taken to strengthen sector institutions included the establishment of new organizational units: the Environment and Industrial Pollution Control Sections in MOI and DOI; the Foreign Investment and Facilities Section in DOI, to serve as full time secretariat to the One Window Committee; the Planning and Monitoring Unit in MOI; and the ASYCUDA implementation unit in DOC. The beneficial impacts of these institutional changes have varied, depending on the success of policy reforms initiated in their respective jurisdictions, as described above. As to Planning and Monitoring Unit of MOI, only three TPIA reports were produced during ISP implementation, and the reports were discontinued after the 1997 loan closing. Institutional consolidation has continued during and after ISP,[25] signaling the Government's resolve to implement sustained institutional and organizational reforms. But as noted elsewhere, these organizational changes have not been accompanied by adequate human and other resources, and there is a need for further capacity building. An upgrading of skills, training, and equipment is needed in technical units, such as the agencies responsible for the monitoring of industrial pollution and enforcement of pollution regulations, and operation of the ASYCUDA system in DOC.

[25] Three ministries were combined to form the Ministry of Industry, Commerce and Supplies in 2000, the Department of Excise Duty and Department of Sales and Tax were merged to form the Inland Revenue Department, and a new Ministry of Population and Environment was established in 1995.

## D. Environmental Impact

47. The impacts of improved pollution control and environmental protection reforms have been limited, and difficult to verify. The Environmental Protection Act and the EPR, both introduced in 1997, are only applied to liquid effluents that new plants discharge into inland waters in five designated industries.[26] Initially, compliance was voluntary, and was made compulsory only in 2000. The monitoring capacity of the responsible agencies (DOI, Department of Cottage and Small Industries, and NBSM) is limited, and the enforcement will and capacity of MOPE is weak and yet untested.

# IV. OVERALL ASSESSMENT

## A. Relevance

48. ISP objectives conformed to the Government's priorities and ADB's country operational strategy. Its design was generally consistent with the objectives. ISP supported a series of policy and institutional reforms to provide a conducive environment for enhancing the efficiency of the industry sector and generating its economically sustainable growth. These reforms constituted an integral part of the Government's overall policy framework, seeking to create greater employment and improve Nepal's balance of payments, relying on market forces, and increasing private sector participation in industrial development. But in hindsight, two aspects of ISP might have been better designed. First, the component on industrial pollution control, although important in the context of sustainable development, was not directly relevant to the main ISP objective, and could have been pursued more effectively as a separate initiative. Second, ISP could have targeted measures to improve the productivity of the CSI subsector, which has considerable potential to contribute to pro-poor growth. But on balance, ISP is assessed as relevant.

## B. Efficacy

49. ISP achieved its purpose substantially. It helped provide a competitive environment to improve the efficiency of the industry sector by liberalizing imports, reducing tariff rates and bands, removing quantitative restrictions, easing regulations on exports and foreign investment, adopting a modern customs valuation system, and streamlining customs procedures. Although ISP addressed the fundamental problems impeding development of the sector, it did not focus policy actions on particular sector segments (e.g., CSIs). ISP performance was not as good as expected, but still was positive, in the improvement of export incentives such as simpler and expanded BWH regulations, and improvements to DDS. ISP faced difficult and politically sensitive issues in areas relating to industrial regulations and incentives (i.e., improved control of industrial pollution, environmental protection, and rationalization of micro incentives), which caused a long delay in their implementation. Nevertheless, the most significant industry sector reforms have proceeded, although slower than expected. All points considered, ISP is assessed as efficacious.

## C. Efficiency

50. Precise quantitative measurement of the efficiency of ISP is difficult. Several measures to reform trade-related policies and procedures have been beneficial, including the introduction

[26] NBSM has developed standards for water effluent discharged to inland waters by new plants in three additional industries (cotton textile, sugar and synthetic fibre) but these are yet to be legislated.

of Harmonized System of Tariff Classification and ASYCUDA, and operation of the One Window Committee. Industry has benefited from those measures in terms of lower import and export costs, and improved availability of industrial inputs at internationally competitive prices. Also, simplification of excise and sales taxes has made tax collection more efficient. But ISP implementation was slow and ineffective in other areas, such as industrial pollution control and export incentives. Overall, ISP was less than efficient.

## D. Sustainability

51. The Government is conscious of the need to maintain and build on the reforms initiated through ISP, which are critical for gaining membership in the World Trade Organization. It has shown a strong record of sustaining most of the trade-related reforms, such as rationalization of tariff structure, liberalization of import controls, and improvement of customs procedures. The Government is committed to retaining the low tariff regime and continuing with progressive improvements in customs procedures and the expanded application of ASYCUDA. Some regression has occurred, however, in the liberalization of export regulations. While export duty was initially eliminated, a 1% export service charge was introduced (it was subsequently reduced to 0.5%). Also, new export taxes were imposed at rates generally in the range of 2–5%. Floor prices have been eliminated for all commodities except carpets. The floor price for carpets was gradually reduced from \$65 per $m^2$ to \$48 per $m^2$. Export incentives have been diluted by continuation of this floor price and the recent introduction of a 0.75% withholding tax on export revenue. Nevertheless, the sustainability of the overall impact of ISP appears likely.

## E. Institutional Development and Other Impacts

52. ISP has contributed significantly to development and capacity building of several departments and organizations concerned with industry and trade sectors. These include the One Window Committee charged with facilitating investment and processing of duty drawback claims, the ASYCUDA implementation unit in DOC, the Environment and Pollution Control Sections in MOI and DOI, and the Planning and Monitoring Unit in MOI. Further capacity building is needed, however, by improving the quality of human resources and providing essential equipment and facilities. ISP generally signaled the Government's resolve to increase competition in industry, thus improving its efficiency. Although ISP did not address poverty issues directly, it is believed to have contributed to poverty reduction by encouraging employment and growth. On the whole, the institutional and other impacts of ISP are considered significant.

## F. Overall Performance

53. Generally, the areas of partial compliance or noncompliance with agreed actions are of relatively low significance in the overall ISP context. Examples are revision of procedures and administrative arrangements to improve export incentives, and studying the implementation of a pollution tax. In the two attached TAs, improving the customs valuation system was successful while capacity building in TPIA was unsuccessful (but that did not adversely affect reform implementation). ISP is rated successful,[27] considering its positive outcomes, sustainability of major reforms, and the limited overall impact of those elements of policy actions that were not fully implemented.

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[27] Using the current four-category rating system (highly successful, successful, partly successful, and unsuccessful).

# V. KEY ISSUES, LESSONS, AND FOLLOW-UP ACTIONS

## A. Key Issues

### 1. Development of Cottage and Small Industries

54. CSIs, a dominant force in Nepal's manufacturing and trade sector, would benefit from carefully focused policy initiatives to improve their efficiency and productivity. Such improvements would yield direct benefits in poverty reduction, gender development, and child labor, because much of the CSI activity consists of home-based manufacture and is a significant source of employment, particularly of women. CSI support could also address issues relating to employment of minors. Ways to encourage growth of CSIs include providing entrepreneurs convenient ways to avail of DDS, and making institutional arrangements to provide business services. Thus, scope is considerable for addressing key economic and social issues through balanced development of CSIs.

### 2. Improvement of Customs Procedures

55. Progress was considerable in improving customs procedures through ISP. Notably, the ASYCUDA system continues to be implemented progressively across DOC. But more capacity building, institutional strengthening, training, and equipment are needed for DOC to gradually reduce the discretion and influence of front-line customs officers. This would improve the governance of DOC, facilitate efficient trade processing, and reduce nonofficial costs to importers and exporters.

### 3. Industrial Pollution Management

56. While progress was made in industrial pollution management (starting from a base of zero) through ISP, there is a continuing need for TA and institutional strengthening in the monitoring and enforcement of industrial pollution standards and regulations. This applies not only to new plants in specified industries, but more important, in extending the standards, monitoring, and enforcement to existing industrial units. The Government should act more decisively in these matters.

### 4. Reporting on Industrial Sector Impact Assessment

57. The failure of MOI to introduce and sustain effective TPIA reporting should be addressed in any future ADB intervention in the industrial sector. In view of the weak capacity for impact assessment analysis in MOI, and the lack of commitment to TPIA reporting, the establishment of an effective system should be a precondition of further loan assistance to the sector. A capacity building TA for establishment of a permanent TPIA unit would help create the monitoring and evaluation capacity within the Government on a sustainable basis and thus facilitate implementation of ongoing reforms and design of future reform programs.

### 5. Property Mortgage Rights for Leasehold Industrial Land

58. Tenants of industrial estates in Nepal have resisted increases in rental rates to market levels. The main reason for this resistance is the tenants' inability to obtain loans by mortgaging fixed assets, because the land titles rest with IDM, and the mortgage law does not provide for liens on plants erected on leasehold land. This appears to be a genuine problem. It impedes

expansion of existing industries on industrial estates, and calls for reforms through amendment of relevant laws and regulations.

### 6. Duplication of Export Promotional Activity

59. After the introduction of export services in 1995, the Government established the Export Promotion Board, which is funded by revenue from export service taxes. There appears to be some duplication between the functions and activities of the Export Promotion Board and the Trade Promotion Centre. This causes confusion in industry and trade circles, and could lead to inefficiency of resource allocation. ADB should encourage the merger of these two organizations to optimize the use of scarce funding for trade promotion.

## B. Lessons

60. The implementation experience of ISP has confirmed a few already well-known lessons. First, ISP included too many actions to be completed within a time frame of only 28 months. This was ambitious but unrealistic, given the constraints on implementation capacity, and the political sensitivity of some reform measures. Similar programs in the future should be more sharply focused, and be preceded by an organized effort to build ownership among all important stakeholders, including political decision makers, bureaucracy, beneficiaries and affectees, the private sector, and the civil society. Furthermore, adequate implementation capacity must be built before reform programs are launched. The ISP design should have incorporated a more significant element of capacity building and training to upgrade the capabilities of DOC, DOI, NBSM, and MOPE.

61. Second, the ISP implementation arrangements relied on a large number of ministries and agencies; some were not involved in ISP formulation. The resulting lack of ownership made it difficult to coordinate implementation, despite the existence of a formal committee mechanism. The efficiency and effectiveness of implementation could have been improved by a suitably staffed program implementation unit to assist the coordination committee for the duration of ISP. Furthermore, the responsibility for implementation of various policy conditions lacked clarity and should have been defined more precisely.

62. Third, the ISP design did not adequately consider the structure of Nepal's industrial sector. Thus, CSIs, perceived to have considerable potential to enhance their contribution to employment generation and poverty reduction, have not benefited from some reform measures and continues to face difficulties, particularly in export incentives. The efficacy of future programs can be improved by more comprehensive sector assessment, and by targeting policy changes on those segments of the sector that promise maximum development impacts.

63. Fourth, experience with ISP confirms that trade reforms are necessary, but such reforms alone are not sufficient for Nepal's industrial sector to realize its potential for productivity and growth. In trade and tariffs, ISP relied almost exclusively on macroeconomic reforms, and did not provide institutional support to address Nepal's well-known needs in the export sector, namely diversification of export products and markets.

64. Finally, it appears in hindsight that ADB's own monitoring and evaluation of programs involving such wide-ranging reforms should be more rigorous than it was with ISP. Furthermore, fielding a PCR mission is necessary when implementation has been delayed significantly and there are difficulties in compliance with loan covenants. Also, when policy impact assessment reporting is incorporated in the program design, the design should include clearly defined key

performance indicators. Tranche conditionality should require regular reporting of impact assessments against the set benchmarks. For this, adequate assistance in institutional strengthening and capacity building should be provided ahead of program implementation. Alternatively, the program design should include adequate implementation TA.

## C. Follow-Up Actions and Recommendations

65. ADB should continue policy dialogue with the Government to ensure compliance with ISP elements that are not yet fully realized. First, the playing field should be leveled for industries located both within and outside the major industrial estates. For that, ADB should support amendments to the relevant laws or regulations to allow liens on the fixed assets embedded in leasehold land. Once this is done, ADB should pursue compliance of the ISP condition that requires increasing rents at the industrial estates to comparable market rates. Second, the Government should strengthen industrial pollution regulation in line with the IPCR that the TA consultants developed, and initiate effective monitoring and enforcement. Third, adequate funding should be provided to settle claims efficiently under DDS, and the system should be made more accessible to CSIs. Finally, capacity building of DOC should be continued to enable it to extend ASYCUDA to all transactions. ADB may consider providing further capacity building TA, particularly in implementing ASYCUDA and strengthening control of industrial pollution. Also, a sector assessment focusing on the issues and constraints that CSIs face, and on efficiency issues in public enterprises, would help further develop the industry sector.

66. Recommended follow-up actions are summarized in Table 8.

**Table 8: Follow-up Actions**

| Action Area | For ADB | For Government |
|---|---|---|
| 1. Leveling the playing field for industries located inside and outside the major industrial estates | 1.1 Continue policy dialogue with the Government. | 1.1 By 30 September 2003, amend laws and/or regulations to allow liens on leasehold land.<br><br>1.2 By 31 December 2003, raise rental rates of major industrial estates to comparable market rates. |
| 2. Industrial pollution control | 2.1 Continue policy dialogue with the Government.<br><br>2.2 Consider technical assistance (TA) for capacity building of concerned agencies and strengthening the enforcement of the pollution control regime. | 2.1 By 30 September 2003, strengthen regulations on industrial pollution in line with the Industrial Pollution Control Regulations developed under TA 1939–NEP.[28] |
| 3. Duty Drawback Scheme (DDS) | 3.1 Continue policy dialogue with the Government. | 3.1 Provide adequate funding to clear the backlog of claims on DDS, and settle new claims within 60 days on a continuing basis. |
| 4. Capacity building of Department of Customs and extension of the Automated System of Custom Data (ASYCUDA) | 4.1 Continue policy dialogue with the Government.<br><br>4.2 Consider capacity building TA to DOC. | 4.1 By 30 June 2004, extend application of ASYCUDA to all transactions. |
| 5. Further development of the industry sector through addressing issues and constraints in cottage and small industries (CSIs) and public enterprises | 5.1 Initiate policy dialogue with Government.<br><br>5.2 Consider TA to support a sector assessment focusing on CSIs and public enterprises. | 5.1 By 31 March 2003, form a Government-private sector team to study issues and constraints facing CSIs. |

[28] TA 1939–NEP: *Formulation of Industrial Pollution Control Regulations,* for $135,000, approved on 25 August 1993.

## EVALUATION FRAMEWORK

| Design Summary | Performance Target/Policy Action | Achievement/Compliance | | Impacts/Outcomes |
|---|---|---|---|---|
| | | During Program Period | After Program Period | |
| **I. Goal and Purpose**<br><br>A. Goal<br>The Industrial sector makes a significant contribution to:<br>(i) Output | A.1.1 Increased contribution of trade sector to GDP growth. | | . | **During the Industrial Sector Program (ISP):** While GDP grew at an average annual rate of 5.4% in constant prices between fiscal years (FYs) 1993 and 1997, the growth rates of exports (7.0%) and imports (24.3%) outpaced GDP growth.<br>**Post ISP:** Over the period from FY1993–FY2001, GDP grew at an average annual rate of 5.1% in constant prices as compared to growth rates of exports (15.8%) and imports (14.5%).<br>**Comment:** Macroeconomic indicators suggest the general sustainability of impacts of the policy reform. |
| (ii) Balance of payments (BOP) and | A.1.2 Improvement in balance of payments. | | | **During ISP:** Trade deficit increased from NRs22.0 billion in FY1993 to NRs71.0 billion in FY1997.<br>**Post ISP:** Trade deficit declined to NRs52.0 billion in FY1999, and has stabilized around NRs60.0 billion in subsequent years.<br>**Comment:** ISP's long-term impact on balance of payments is difficult to judge. But its beneficial impact can be seen in a three-fold increase in the total value of foreign trade during FY1993–FY2001, and a decline in trade deficit as a proportion of total value of foreign trade from 38% in 1993 to 35% in FY2001. |
| (iii) Employment generation. | A.1.3 Increase in industrial employment. | | | **During ISP:** Industrial employment increased from 355,058 persons in FY1994 to 382,845 in FY1997.<br>**Post ISP:** Industrial employment continued to steadily increase to 392,421 in FY2000.<br>**Comment:** Increased employment trend compares well with a temporal displacement of 3,000 workers anticipated in the report and recommendation to the President. |
| B. Purpose<br>Improve the environment for sustained private sector-led growth of trade and industry through policy and regulatory reforms and institutional strengthening of trade and industry sectors. | B.1.4 Increase in industrial production. | | | **During ISP:** Industrial production grew at an average annual rate of 7.5% between FY1993 and FY1997, which exceeded the GDP growth rates.<br>**Post ISP:** Growth of industrial production continued at an average annual rate of 4.9% between FY1997 and FY2001.<br>**Comment:** The overall average growth of industrial production since the start of ISP, i.e. during FY1993–FY2001 (6.2%), has exceeded GDP growth rate (5.1%) over the same period. |

| Design Summary | Performance Target/Policy Action | Achievement/Compliance | | Impacts/Outcomes |
|---|---|---|---|---|
| | | During Program Period | After Program Period | |
| | B.1.5 Growth of industrial investment including foreign direct investment (FDI). | | | **During ISP:** Private sector component of gross fixed capital formation (GFCF) grew from 59% in FY1988 to 68% in FY1997, at an annual average rate of 20% in current prices FDI as a percentage of GFCF grew from 0.7% in FY1993 to 2.7% in FY1997. **Post ISP:** The private sector component of GFCF gradually moved back to pre-ISP levels. But in absolute terms, the private sector GFCF almost doubled from FY1993–FY2001. |
| | B.1.6 Increase in exports and export diversification. | | | **During ISP:** FOB value of exports increased from NRs17.3 billion in FY1993 to NRs22.7 billion in FY1997. Export diversification by commodity declined in the s hare of the top two export categories (carpets and garments) from 77% to 65%. In terms of destination, however, export concentration increased with the top three export destinations (Germany, India and USA) increasing their share of export value from 79% to 83%. **Post ISP:** These trends have continued except that total exports, after peaking at NRs55.7 billion in FY2001, are estimated to have declined to about NRs48 billion in FY2002. The share of two major export categories dropped further to 38% in FY2001, and export concentration by destination increased further with the top three export destinations accounting for 86% of total export value in FY2001. **Comment:** Sustained export product diversification confirms a positive program impact while increased export concentration calls for refine went of export promotions. |

| Design Summary | Performance Target/Policy Action | Achievement/Compliance | | Impacts/Outcomes |
|---|---|---|---|---|
| | | During Program Period[a] | After Program Period | |
| **II. Outputs** | | | | |
| A. Rationalization of Tariff Structure. | A.2.1 Improve tariff Classification. | Tariff classification system changed to Harmonized System of Tariff Classification (HSTC) in July 1992.[b]<br><br>HSTC used for trade statistics from July 1993. | International revisions to 1996 HSTC adopted in 1997. | DOC is committed to continue using and updating HSTC. Trade statistics are firmly established in HSTC terms. |
| | A.2.2 Eliminate tariff discrimination. | Effective July 1992, Government introduced the open general licensing (OGL) system, abolished preferential tariff rates available to industrial importers, and applied uniform tariff rates to goods imported by different categories of importers.[b] | | Current policy is to continue moving toward tariff reduction and maintaining equalized tariffs among various sectors. The average effective tariff rate has been progressively reduced to less than 10%. Stakeholders have reported beneficial impacts of OGL. However, industry has voiced concern on some inconsistencies between tariffs on raw materials and related finished products, which discourage domestic value addition, and discretionary use of the tariff classification system by individual customs officers. |
| | A.2.3 Reduce basic tariff rates to equalize effective protection among various sectors. | Effective July 1992, the number of tariff rates was reduced from 14 to 8, and maximum basic tariff rate was reduced to 30% with the exception of a few items such as alcoholic beverages, cigarettes, perfumes.[b] | The Customs Tariff Schedule for FY2002 lists most common import tariffs as 5%, 10%, 15% and 25% and 40%, and 80-100% for luxury items. The effective average tariff rate was less than 10% in FY2001. | |
| | A.2.4 Reduce additional tariff rates to better reflect true prices of Indian and third country imports. | Additional tariff rates reduced from 15%, 30%, 40%, and 50% to 5%, 10%, 15%, and 20% in July 1992, and 3%, 5%, 8% and 12% in February 1993.[b] | | |
| B. Liberalization of Import Controls. | B.2.1 Reduce quantitative restrictions on imports and replace them with tariffs. | Government abolished the industrial passbook system from March 1992. With the exception of prohibited goods, all goods are freely importable under the OGL system.[b] | | Operation of OGL is firmly entrenched and producing beneficial impacts. |

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| Design Summary | Performance Target/Policy Action | Achievement/Compliance | | Impacts/Outcomes |
|---|---|---|---|---|
| | | During Program Period[a] | After Program Period | |
| | B.2.2 Phase out import license auction and replace it with appropriate tariffs.<br><br>B.2.3 Continuously monitor items subject to import license auction with a view to further reducing the number of such items. | Following the introduction of partial currency convertibility on trade account in March 1992 and full convertibility in February 1993, Government reduced the number of items subject to import license auction from 88 to 12 in July 1992, and to 6 in February 1993.[b] | | The import license system stands effectively abolished for all but prohibited items, such as firearms and narcotics. |
| C. Liberalization of Export Regulations. | C.2.1 Eliminate export duty. | Export licenses and export duties abolished except in respect of a few essential agricultural commodities.[b] | Export taxes re-introduced for selected commodities at rates generally in the range of 2-5%, with the highest at 200% for wood products. Compliance is considered partial. | Re-introduction of export taxes albeit at low rates, is contrary to the reform measures under ISP, which sought to liberalize export regulations. But there is no evidence of substantial negative impacts. |
| | C.2.2 Eliminate export floor prices. | The Government abolished export floor prices for hides and skins, and cardamom in August 1992; reduced export floor prices for carpets from \$65 $m^2$ (washed) and \$61 $m^2$ (unwashed) to \$60 $m^2$ in October 1992; and finally abolished export floor prices for all products[b] (except for carpets, which was retained at \$48 $m^2$ in March 1993). | Export service charge was introduced (1% at first, but reduced progressively to 0.5% after industry pressure). Also, a 0.75% withholding tax, and more recently, a tax on export earnings (albeit at a lower rate than other earnings) was introduced. Export income was made taxable at 40% of an organization's normal tax rate in FY2001, which was raised to 70% in FY2002. Compliance is considered partial. | The cost of doing export business may have initially declined but has subsequently increased somewhat with the re-introduction of export-related taxes. Viewed in light of the reforms supported by the Program, these steps appear regressive. There is strong industry opposition to the continuation of the floor price on carpet exports. |

| Design Summary | Performance Target/Policy Action | Achievement/Compliance | | Impacts/Outcomes |
|---|---|---|---|---|
| | | During Program Period[a] | After Program Period | |
| D. Improvement of Export Incentives. | D.2.1 Simplify and make more user friendly the administration of export incentives. | A One Window Committee was established in Department of Industries (DOI) under Industrial Enterprise Act of1992 to handle various export incentives including drawback of customs duty, excise duty, and sales tax.[b] | | In general, the One Window Committee has been an effective mechanism to facilitate new foreign investment and existing industrial enterprises, though difficulties have been experienced with processing of duty refund applications, largely due to inadequate budget for refund payments. |
| | D.2.2 Review implementation of export incentives and revise procedures and administrative arrangements for improvement every fiscal year. | | | This action was reported as complied within ISP documentation based on actions relating to the bonded warehouse system (see D.2.4 below). No documentary evidence of discreet annual reviews is, however, available. |
| | D.2.3 Award export processing zone (EPZ) status to exporters. | Firms exporting more than 90 percent of their output were given duty and sales tax exemption under the Industrial Enterprise Act 1992.[b] | | EPZ status has not been awarded and the mechanism remains unused. However, a regime of low tariffs, BWH, and duty drawback schemes (DDS) offer practical alternatives to EPZ. |
| | D.2.4 Bonded Warehouse (BWH) Facility: Allow industries other than garments to use the BWH facility and simplify its utilization procedures. | BWH facilities substantially simplified, including the procedure for verification of raw materials used for export production, and extended to all manufacturing industries.[b]<br><br>Effective July 1992, Department of Customs (DOC) began releasing bank guarantees and deposits to cover duties and sales tax upon submission of evidence of export.[b] | | BWH system appears to be little used by new establishments in Nepal and is not mentioned in investment promotion literature. Need for system lessened with tariff reductions.<br><br>Industry stakeholders confirm that BWH system has become simpler, though its utilization by industries other than garments is insignificant because of reduction in import tariffs. |

| Design Summary | Performance Target/Policy Action | Achievement/Compliance | | Impacts/Outcomes |
|---|---|---|---|---|
| | | During Program Period[a] | After Program Period | |
| | D.2.5 Duty Drawback Scheme: Make utilization of DDS easier. | Budget allocation of NRs20 million was made for drawbacks of customs duty, sales tax and excise duty in FY1993.[b] | | Budgetary funding was insufficient to clear the backlog. Private sector stakeholders expressed dissatisfaction with DDS. |
| | D.2.6 Adhere to 60-day rule for duty drawback payments effective FY1996. | The Government announced new procedures and input-output coefficients to be used for the calculation of duty drawback, and made a commitment to settle claims within 60 days. Claims processing was assigned to the One Window Committee.[b] | | Comprehensive data on this measure is not available. However, anecdotal evidence suggests that producers using multiple inputs, such as tanneries, have had wait for up to 109 days to realize their claims. Private sector stakeholders are unhappy about refund processing delays. Government has attempted several revisions to the refund payment procedure (see D.2.8). |
| | D.2.7 Continue to provide adequate budget for DDS. | Duty drawback payments increased from NRs 0.3 million in FY1993 to NRs25 million in FY1997. | Duty drawback payments rose further to NRs 138.9 million in FY2001, equal to 0.5% of related government tax revenue in FY2001 as compared to 0.1% in FY1998. | Budget allocations have increased over the program, with some fluctuation, though adequate funding for full claim processing by One Window Committee has not occurred. By a private sector estimate, the backlog of claims in December 2001 was estimated to be more than NRs800 million. |
| | D.2.8 Review and streamline procedures on a continuing basis, including input-output coefficients. | | Introduction of bank guarantee system in lieu of cash payment of duty (1998), revolving passbook system for credit of duty drawback payments (2001), and duty drawback payments in the form of marketable interest-bearing bonds (proposed for implementation in 2002). | While DDS is being constantly refined it remains a source of significant dissatisfaction of exporters. Improvements implemented so far have not resulted in reducing the backlog. |

| Design Summary | Performance Target/Policy Action | Achievement/Compliance | | Impacts/Outcomes |
|---|---|---|---|---|
| | | During Program Period[a] | After Program Period | |
| | D.2.9 Promote backward linkage of export-oriented industries by relaxing requirements for duty drawback. | Actual importers are allowed to utilize the DDS whether or not they are also actual exporters.[b] | | Cottage and small industries (CSIs) do not appear to be able to access this facility. CSI stakeholders cite the complexity of DDS as the cause of delays in claim payments, though they appear to lack a full understanding of the claims process. |
| | D.2.10 Conduct survey of actual utilization of duty drawback.[c] | The National Productivity and Economic Development Center conducted a survey for MOI on the actual utilization of DDS in June 1994. | | |
| E. Improvement of Customs Procedures. | E.2.1 Move the cargo handling function from Department of Customs (DOC) to airline company or other appropriate agencies.[c] | Cargo handling at Tribhuvan International Airport was transferred to Nepal Transit and Warehouse Corporation in December 1994. | | DOC and private sector stakeholders indicate this has been a beneficial move and cargo-handling services are being provided effectively. |
| | E.2.2 Implement recommendations of the ADB technical assistance (TA) for improvement of customs valuation.[c] | Recommendations of TA 1873 submitted in March 1994, together with an implementation plan for: (i) amendment of the Customs Act to introduce the new valuation system based on transaction value, (ii) training of DOC officials, and (iii) computerization of DOC and its customs houses with Automated System of Customs Data (ASYCUDA). The Customs Act was amended in August 1997. | | Amendment of the Customs Act was delayed due to government changes during the period 1994 to 1997. |

| Design Summary | Performance Target/Policy Action | Achievement/Compliance | | Impacts/Outcomes |
|---|---|---|---|---|
| | | During Program Period[a] | After Program Period | |
| | E.2.3 Implement ASYCUDA. | | ASYCUDA implementation began in January 1998 and system refinements (including software upgrading) have occurred up to 2001. | DOC showed commitment to continuing improvement of the system, and is progressively extending its operation. However, there is an ongoing need for capacity building and training in DOC to fully implement ASYCUDA across all DOC operations and functions. |
| F. Streamlining of Industrial Regulations and Incentives. | F.2.1 Liberalize industrial licensing regulations. | Effective June 1992, industrial licensing was done away with except for industries in defense or public health sectors, and environmentally hazardous industries.[b] | | Industry stakeholders indicate that these policy changes have been beneficial to industrial development. And employment growth (see Section 1 above). |
| | F.2.2 Relax FDI regulations. | Foreign Investment and Technology Transfer Act of 1992 allowed 100 percent foreign ownership (with full repatriation of profits) of industries with fixed assets exceeding NRs20 million.[b] | | |
| | F.2.3 Quick disposal of investment applications. | Since 1994, the One Window Committee, has observing the 30-day rate of dispose of investment applications, both foreign and domestic. | | |
| | F.2.4 Remove restrictions on FDI based on size of enterprises of medium industries.[c] | Restrictions based on the size of enterprises for FDI purposes was removed in January 1996. Instead, a negative list of industries, including tourism and services, was introduced. | | Initial private sector concerns that this policy action would result in CSI firm closures did not eventuate. Its overall impact has been beneficial for the industry sector. |

| Design Summary | Performance Target/Policy Action | Achievement/Compliance | | Impacts/Outcomes |
|---|---|---|---|---|
| | | During Program Period[a] | After Program Period | |
| | | A Foreign Investment and Facilities Section was established in DOI to serve as a full-time secretariat of the One-Window Committee to facilitate both FDI and domestic investment. The Industrial Enterprise Act of 1992 mandated disposal of license applications within 30 days.[b] The requirement to comply with the 30-day rule was strengthened in 1995. | | The One Window Committee has proved to be an effective mechanism to facilitate new FDI and expansion of existing industrial enterprises. |
| | F.2.5 Improve industrial pollution control and arrangements for environmental protection. | An Environment Section and an Industrial Pollution Control Section were established within DOI in November 1992.[b] | Training and technical skills development initiatives have been taken, and industry consultations and monitoring activities have begun. | The commitment of MOI, DOI and MOPE appears sound but further capacity building, monitoring equipment, and stronger legislative support is necessary for effective pollution control and environmental management in the industrial sector. |
| | F.2.6 Establish appropriate industrial pollution standards to be applied to existing and new industries, formulate a mechanism for monitoring industrial pollution, and enforcing compliance with such environmental standards.[c] | ADB TA[d] provided pollution control standards based on relevant international experience, which were not adopted because the Government desired to apply standards based on Nepal-specific measurements. The Nepal Bureau of Standards and Metrology (NBSM) developed pollution standards for new plants in 5 industries.[e] These standards were embodied in the Environment Protection Regulation (EPR) of 1997 but were not strictly enforced. | The standards for new plants in the designated industries were made mandatory effective 2000. Similar standards were specified for new plants in four additional industries,[f] but have not yet been formally adopted. Monitoring capacity within the departments concerned remains limited. Danish International Development Assistance (DANIDA) is providing significant technical support to improve the monitoring and compliance function. | These measures have had limited impact. The development and enactment of pollution control standards has been slow and limited to only new plants in five industries that impact the environment significantly, and then only in relation to effluents. No enforcement has begun, however, and reliance is placed on industry consultation and community pressure. No standards for solid waste, air, or noise pollution have yet been specified. |

| Design Summary | Performance Target/Policy Action | Achievement/Compliance During Program Period[a] | Achievement/Compliance After Program Period | Impacts/Outcomes |
|---|---|---|---|---|
| | F.2.7 Enact Industrial Pollution Control Regulations (IPCR).[c] | Draft IPCR was finalized in November 1994, and incorporated appropriate industrial pollution standards to be applied to existing and new industries. However, these were not legislated. In 1995, MOPE was given the mandate to draft an environment protection bill. This bill was enacted in October 1996. | | Since 1997, there has not been any significant formulation of environmental policy and legislation (the responsibility of MOPE). The law and regulations on industrial pollution control are inadequate and not enforced effectively. |
| | F.2.8 Establish appropriate guidelines for environmental impact assessment (EIA) and initial environmental examination (IEE) before 31 December 1993. | Guidelines were published in the official Gazette on 6 November 1995. | EIA and IEE made mandatory for registration of each new foreign investment and necessary guidelines prepared. | While progress has been made, this has been slow and the monitoring and compliance aspects are weak, largely due to capacity constraints. |
| | F.2.9 Prepare and complete a study on the implementation of a pollution tax before 31 December 1994. | A pollution tax was incorporated in the 1994 draft IPCR, though it was not included in the EPR. ADB TA funds earmarked for this purpose were not utilized. | The Program Completion Report (PCR) considers this action to have been completed. However, no study is on record. | The concept of a pollution tax is not accepted under present Government approach to industrial pollution control. Fines incorporated in EPR are minimal (NRs50,000–100,000 as compared to NRs100,000 per day under IPCR). The general approach under EPR relies on industry consultation and public participation. |
| | F.2.10 Monitor industrial pollution. | | The industrial pollution control sections of DOI and DCSI receive training and additional equipment under a 5-year DANIDA support program, but regular monitoring activity is still limited. | Monitoring capacity in all agencies is limited (DOI, DCSI, MOPE and NBSM). Only ad hoc monitoring of new plants covered by the limited standards issued so far has occurred. There is a rising community concern over industrial pollution, and community based pressure is expected to continue to increase (including legal challenges). |

| Design Summary | Performance Target/Policy Action | Achievement/Compliance | | Impacts/Outcomes |
|---|---|---|---|---|
| | | During Program Period[a] | After Program Period | |
| | F.2.11 Raise the rents at industrial estates to comparable market rates.[c] | Land, shed and warehouse rents were raised 40% in 1997 but in real terms they declined marginally. | Rental rates were raised 15% each in FY1999 and FY2000. During this time, the GDP deflator increased 18.7%. Government and estate lessees have reached agreement to raise rents by 15% every two years up to 2010. | The rental rates remain significantly below market rates, to the disadvantage of industries located outside industrial estates. Government experienced considerable opposition to raising rental levels from industries and trade unions, as well as to a planned privatization of the industrial estates in FY1997. This may be partly because the relevant laws and regulations do not permit mortgage of fixed assets built on leased land. |
| | F.2.12 Revise current system of tax holidays and exemptions accorded to industry sector.[c] | The Government amended the Industrial Enterprises Act 1992 to reduce the tax holidays and tax rebates to priority sectors and industries. The amendment was approved by Parliament on 22 August 1997. | | Industrial stakeholders hold the view that these policy reforms have not had significant impacts, given Nepal's remote location and limited raw material resources. |
| | F.2.13 Improve excise duty and sales tax systems: (i) substantially reduce the number of excisable items, (ii) merge excise duty on other items with sales tax.[c] | In July 1992, the Government reduced the number of items subject to excise duty from 52 to 38 (and to 11 in July 1993). Excise duty on other items was merged with the sales tax in 1993. The procedure of excise duty payment was simplified by replacing the excise inspector with the self-removal system in July 1992.[b] A value added tax (VAT) replaced these taxes in FY 1996. | | VAT collections have widened the tax catchment and VAT revenue has exceeded overall revenue from the taxes it has replaced (see below). Industry stakeholders have generally approved of the simplifications involved with these reforms leading to a single VAT, though there is concern that VAT rates are too high. |
| | F.2.14 Broaden the sales tax base. | The Government replaced the multi-rate structure of sales tax (5% to 40%) with a two-tier rate structure (10% and 20%). This was further simplified to 15% in July 1996 and reduced to 10% in July 1997, replacing separate sales, entertainment, hotel and contract taxes. | | |

| Design Summary | Performance Target/Policy Action | Achievement/Compliance During Program Period[a] | Achievement/Compliance After Program Period | Impacts/Outcomes |
|---|---|---|---|---|
| G. Strengthening of Sector Institutions. | G.2.1 Effective implementation of policy reform measures and improved coordination between various ministries and departments concerned with the implementation of trade and industrial policy. | MOI was reorganized and a Planning and Monitoring Unit was established within DOI.[b] A Project Coordination Committee was formed to improve coordination between various ministries and departments, though it met irregularly during the Program period. | | ISP implementation was slow and ineffective in some areas, particularly in the Planning and Monitoring Unit. Limited institutional strengthening and capacity building was also implemented in DOC and NBSM. As a result, the activities of Industrial Pollution Control Section of DOI remained largely ineffective. |
| | G.2.2 Constantly monitor implementation of trade and industrial policies and prepare semi-annual trend, progress and impact assessment (TPIA) reports in consultation with government agencies and as the private sector. | Planning and Monitoring Unit was slow in preparing TPIA reports and submitted few reports to Bank during life of the Program. The first TPIA report was provided in December 1995 and was deficient in impact assessment. The second TPIA report, covering the June-December 1996 period, was submitted to ADB in September 1997. | | Planning and Monitoring Unit has since been disbanded and the systems and equipment to prepare TPIA reports remain unused. Although the Government did not submit its formal PCR, it ascribed poor impact assessment to unsatisfactory performance of ADB TA[g] consultants. ADB's own PCR rated consultants' performance as unsatisfactory (see below). |

| Design Summary | Performance Target/Policy Action | Achievement/Compliance |
|---|---|---|
| **III. Inputs** | | |
| A. Program loan of $20.74 million. | A.3.1 Compliance with the conditions for the release of first and second tranches of the Industrial Sector Program Loan of ADB. | Tranches 1 and 2 released. The PCR lists 21 key policy measures and determined all tranche conditions were complied with (16) or substantially complied (5). For details, see Section II above. |
| B. TA 1872-NEP: Monitoring, Impact Assessment, and Management of Policy Reforms. | B.3.1 Monitor progress of policy reforms. | The consultants failed to establish TPIA reporting system and produce semi-annual TPIA reports in the initial TA phase (FYs1994-1995). A short seminar presentation was made in January 1996. The seminar was brief, lacked substance, failed to analyze and assess the impacts of policy reform, and used old data. The international consultant that delivered the presentation, and ultimately the final report, was not the person who conducted the first phase, and was thus not familiar with the TA background. TA report was submitted in April 1997. |
| | B.3.2 Analyze program impact on economy and the industrial sector. | Under this TA, the performance of both international and domestic consultants was poor. They did not meet the requirements of the terms of reference (TORs) and took too long to complete the assignment (2.5 years as against 1 year provided for originally). The TA did not achieve its objective, namely to help the Government in (i) monitoring the progress of the policy reforms and in analyzing their impact on the economy in general and the industrial sector in particular; and (ii) designing proper coordination mechanisms among various Government agencies as well as between the private sector and Government. In short, the TA made little impact. |
| C. TA 1873-NEP: Improvement of Customs Valuation. | C.3.1 Improve valuation practices of DOC, leading to successful launching of the ASYCUDA project. | TA report submitted in March 1994 recommended the revision of the customs legislation for adoption of the valuation system of GATT, based on transaction value. DOC started implementing these recommendations, namely the amendment of the Customs Act for a valuation system based on transaction value, training of DOC staff, and computerization of DOC and its customs houses with ASYCUDA. A follow-on ADB TA[h] assisted in improving Government efficiency and effectiveness of customs operations, and increasing the yield of customs revenue, and capacity building of DOC. The TA was implemented from September 1996 to February 1999, and consolidated the gains of the first TA. |

ADB = Asian Development Bank, DCSI = Department of Cottage and Small Industries, DOC = Department of Customs, DOI = Department of Industry, EIA = environmental impact assessment, FOB = free on board, GDP = gross domestic product, MOI = Ministry of Industry, MOPE = Ministry of Population and Environment.

[a] Program period is taken to end with the loan closing date.

[b] Action completed before Board consideration.

[c] Second tranche condition.

[d] TA 1939-NEP: *Formulation of Industrial Pollution Control Regulations*.

[e] Tanneries, wool processing, fermentation, oil and ghee, and pulp and paper.

[f] Dairy, cotton textile, sugar, and synthetic fiber industries.

[g] TA 1872-NEP: *Monitoring, Impact Assessment and Management of Policy Reforms.*

[h] TA 2459-NEP: *Efficiency Enhancement of Customs Operations.*

## NEPAL: KEY ECONOMIC STATISTICS

### Table A2.1: Gross Domestic Product[a]
### (NRs million and Percent)

| Item | FY1991 | FY1992 | FY1993 | FY1994 | FY1995 | FY1996 | FY1997 | FY1998 | FY1999 | FY2000 | FY2001[b] | FY2002[c] |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Nominal GDP (Current prices)** | **116,127** | **144,933** | **165,368** | **191,596** | **209,974** | **239,388** | **269,570** | **289,798** | **330,018** | **366,284** | **393,473** | **410,493** |
| Agriculture | 55,368 | 65,156 | 70,090 | 80,589 | 85,569 | 96,896 | 108,785 | 112,495 | 132,373 | 144,644 | 149,040 | 156,384 |
| Non-Agriculture | 60,759 | 79,777 | 95,278 | 111,007 | 124,405 | 142,492 | 160,785 | 177,303 | 197,645 | 221,640 | 244,433 | 254,109 |
| **Real GDP (Constant 1994/95 prices)** | **174,909** | **183,371** | **188,782** | **204,397** | **209,975** | **221,930** | **233,040** | **240,816** | **251,789** | **267,473** | **280,339** | **282,574** |
| Agriculture | 81,320 | 80,392 | 79,631 | 86,356 | 85,569 | 88,830 | 92,706 | 93,496 | 96,183 | 100,856 | 105,227 | 107,037 |
| Non-Agriculture | 93,589 | 102,979 | 109,151 | 118,041 | 124,406 | 133,100 | 140,334 | 147,320 | 155,606 | 166,617 | 175,112 | 175,537 |
| **GDP Deflator (FY1995=100)** | **66** | **79** | **88** | **94** | **100** | **108** | **116** | **120** | **131** | **137** | **140** | **145** |
| Agriculture | 68 | 81 | 88 | 93 | 100 | 109 | 117 | 120 | 138 | 143 | 142 | 146 |
| Non-Agriculture | 65 | 77 | 87 | 94 | 100 | 108 | 115 | 120 | 127 | 133 | 140 | 145 |
| | | | | | | **Change Over Previous Year (%)** | | | | | | |
| **Nominal GDP (Current prices)** | **16.5** | **24.8** | **14.1** | **15.9** | **9.6** | **14.0** | **12.6** | **7.5** | **13.9** | **11.0** | **7.4** | **4.3** |
| Agriculture | 9.7 | 17.7 | 7.6 | 15.0 | 6.2 | 13.2 | 12.3 | 3.4 | 17.7 | 9.3 | 3.0 | 4.9 |
| Non-Agriculture | 23.4 | 31.3 | 19.4 | 16.5 | 12.1 | 14.5 | 12.8 | 10.3 | 11.5 | 12.1 | 10.3 | 4.0 |
| **Real GDP (Constant 1994/95 prices)** | **6.7** | **4.8** | **3.0** | **8.3** | **2.7** | **5.7** | **5.0** | **3.3** | **4.6** | **6.2** | **4.8** | **0.8** |
| Agriculture | 2.3 | -1.1 | -0.9 | 8.4 | -0.9 | 3.8 | 4.4 | 0.9 | 2.9 | 4.9 | 4.3 | 1.7 |
| Non-Agriculture | 10.9 | 10.0 | 6.0 | 8.1 | 5.4 | 7.0 | 5.4 | 5.0 | 5.6 | 7.1 | 5.1 | 0.2 |

FY = fiscal year, GDP = gross domestic product.
[a] The figures are presented at GDP factor cost (before deduction of bank service charges).
[b] Revised estimate.
[c] Preliminary estimate.
Source: Ministry of Finance, Economic Survey FY2002.

## NEPAL: KEY ECONOMIC STATISTICS

### Table A2.2: Gross Domestic Product at Current Prices by Industrial Origin

(NRs million at Current prices)

| Item | FY1991 | FY1992 | FY1993 | FY1994 | FY1995 | FY1996 | FY1997 | FY1998 | FY1999 | FY2000 | FY2001[a] | FY2002[b] |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Agriculture, Fisheries, and Forestry | 55,368 | 65,156 | 70,090 | 80,589 | 85,569 | 96,896 | 108,785 | 112,495 | 132,373 | 144,644 | 149,040 | 156,384 |
| Mining and Quarrying | 575 | 795 | 921 | 990 | 1,117 | 1,342 | 1,495 | 1,553 | 1,685 | 1,815 | 1,981 | 2,091 |
| Manufacturing | 7,894 | 12,822 | 14,618 | 17,861 | 19,555 | 22,466 | 24,816 | 26,987 | 30,337 | 33,550 | 35,566 | 34,616 |
| Electricity, Gas, and Water | 815 | 1,241 | 1,543 | 2,163 | 2,862 | 3,598 | 4,457 | 4,383 | 4,632 | 5,942 | 6,989 | 9,339 |
| Construction | 11,078 | 14,769 | 17,318 | 19,621 | 23,093 | 26,093 | 29,263 | 30,483 | 33,262 | 37,373 | 39,571 | 43,984 |
| Trade, Restaurants, and Hotels | 12,902 | 16,563 | 19,260 | 22,497 | 24,326 | 28,317 | 30,551 | 33,687 | 39,313 | 42,895 | 45,381 | 42,817 |
| Transport, Communications, and Storage | 6,560 | 8,558 | 10,819 | 12,625 | 13,995 | 15,898 | 19,315 | 22,598 | 24,631 | 29,336 | 33,050 | 34,800 |
| Finance and Real Estate | 10,944 | 13,241 | 15,684 | 18,122 | 20,533 | 23,521 | 27,157 | 29,778 | 33,203 | 36,919 | 41,835 | 43,636 |
| Community and Social Services | 9,991 | 11,788 | 15,115 | 17,128 | 18,924 | 21,257 | 23,731 | 27,834 | 30,582 | 33,810 | 40,060 | 42,826 |
| Total GDP at Factor Cost | 116,127 | 144,933 | 165,368 | 191,596 | 209,974 | 239,388 | 269,570 | 289,798 | 330,018 | 366,284 | 393,473 | 410,493 |
| Less: Imputed Value of Banking Service | 2,289 | 2,933 | 3,578 | 4,473 | 5,060 | 5,932 | 7,009 | 7,896 | 9,438 | 10,708 | 11,912 | 12,269 |
| Total GDP at Factor Cost excluding Imputed Banking Services | 113,838 | 142,000 | 161,790 | 187,123 | 204,914 | 233,456 | 262,561 | 281,902 | 320,580 | 355,576 | 381,561 | 398,224 |
| Net Indirect Taxes | 6,532 | 7,487 | 9,702 | 12,149 | 14,261 | 15,457 | 17,952 | 18,943 | 21,456 | 23,945 | 28,633 | 29,809 |
| GDP at Producers' Prices | 120,370 | 149,487 | 171,492 | 199,272 | 219,175 | 248,913 | 280,513 | 300,845 | 342,036 | 379,521 | 410,194 | 428,033 |

FY = fiscal year, GDP = gross domestic product.

[a] Revised estimate.

[b] Preliminary estimate.

Source: Ministry of Finance, Economic Survey FY2002.

## NEPAL: KEY ECONOMIC STATISTICS

### Table A2.3: Gross Domestic Product at Constant Prices by Industrial Origin
(NRs million at FY1995 prices)

| Item | FY1991 | FY1992 | FY1993 | FY1994 | FY1995 | FY1996 | FY1997 | FY1998 | FY1999 | FY2000 | FY2001[a] | FY2002[b] |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Agriculture, Fisheries, and Forestry | 81,320 | 80,392 | 79,631 | 86,356 | 85,569 | 88,830 | 92,706 | 93,496 | 96,183 | 100,856 | 105,227 | 107,037 |
| Mining and Quarrying | 922 | 996 | 1,018 | 1,080 | 1,117 | 1,262 | 1,348 | 1,365 | 1,416 | 1,480 | 1,538 | 1,581 |
| Manufacturing | 12,179 | 16,076 | 17,075 | 19,179 | 19,555 | 21,322 | 22,826 | 23,607 | 24,856 | 26,646 | 27,605 | 25,981 |
| Electricity, Gas, and Water | 2,481 | 2,649 | 2,406 | 2,553 | 2,862 | 3,414 | 3,475 | 3,331 | 3,520 | 4,025 | 4,344 | 4,993 |
| Construction | 18,285 | 19,695 | 20,474 | 21,765 | 23,093 | 24,733 | 26,372 | 26,953 | 28,786 | 31,544 | 31,815 | 33,375 |
| Trade, Restaurants, and Hotel | 18,701 | 19,828 | 21,130 | 22,947 | 24,326 | 25,424 | 26,458 | 27,981 | 29,069 | 31,036 | 31,888 | 29,840 |
| Transport, Communications, and Storage | 9,910 | 10,772 | 11,597 | 12,653 | 13,995 | 14,759 | 15,902 | 17,186 | 18,355 | 19,644 | 20,856 | 21,006 |
| Finance and Real Estate | 16,647 | 17,519 | 18,522 | 19,684 | 20,534 | 22,096 | 23,136 | 24,494 | 25,719 | 27,026 | 28,064 | 28,831 |
| Community and Social Services | 14,464 | 15,444 | 16,929 | 18,180 | 18,924 | 20,090 | 20,817 | 22,403 | 23,885 | 25,216 | 29,002 | 29,930 |
| Total GDP at Factor Cost | 174,909 | 183,371 | 188,782 | 204,397 | 209,975 | 221,930 | 233,040 | 240,816 | 251,789 | 267,473 | 280,339 | 282,574 |
| Less: Imputed Value of Banking Service | 3,277 | 3,519 | 3,892 | 4,518 | 5,060 | 5,616 | 5,703 | 6,181 | 6,610 | 7,230 | 7,831 | 7,839 |
| Total GDP at Factor Cost excluding Imputed Banking Services | 171,632 | 179,852 | 184,890 | 199,879 | 204,915 | 216,314 | 227,337 | 234,635 | 245,179 | 260,243 | 272,508 | 274,735 |
| Net Indirect Taxes | 9,346 | 8,979 | 10,541 | 12,287 | 14,261 | 14,561 | 15,684 | 15,537 | 16,240 | 17,508 | 18,631 | 18,860 |
| GDP at Producers' Prices | 180,978 | 188,831 | 195,431 | 212,166 | 219,176 | 230,875 | 243,021 | 250,172 | 261,419 | 277,751 | 291,139 | 293,595 |

FY = fiscal year, GDP = gross domestic product.

[a] Revised estimate.

[b] Preliminary estimate.

Source: Ministry of Finance, Economic Survey FY2002.

## NEPAL: KEY ECONOMIC STATISTICS

### Table A2.4: National Accounts Summary
(NRs million at Current prices)

| Item | FY1991 | FY1992 | FY1993 | FY1994 | FY1995 | FY1996 | FY1997 | FY1998 | FY1999 | FY2000 | FY2001[a] | FY2002[b] |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| GDP at Producers' Prices | 120,370 | 149,487 | 171,474 | 199,272 | 219,175 | 248,913 | 280,513 | 300,845 | 342,036 | 379,521 | 410,194 | 428,033 |
| Plus Import of Goods and NFS | 27,785 | 39,321 | 47,429 | 62,972 | 75,850 | 88,996 | 105,775 | 101,949 | 101,648 | 123,055 | 131,403 | 123,143 |
| Total Resources Available = Uses | 148,155 | 188,808 | 218,903 | 262,244 | 295,025 | 337,909 | 386,288 | 402,794 | 443,684 | 502,576 | 541,597 | 551,176 |
| Total Consumption | 108,856 | 133,280 | 148,302 | 170,052 | 186,710 | 214,487 | 241,351 | 259,407 | 295,473 | 322,526 | 350,080 | 371,495 |
| Private | 97,771 | 121,372 | 133,402 | 154,065 | 166,443 | 191,469 | 216,364 | 231,392 | 264,944 | 287,947 | 309,107 | 326,108 |
| Public | 11,085 | 11,908 | 14,900 | 15,987 | 20,267 | 23,018 | 24,987 | 28,015 | 30,529 | 34,579 | 40,973 | 45,387 |
| Total Investment | 25,074 | 31,619 | 39,653 | 44,644 | 55,231 | 68,017 | 71,084 | 74,728 | 70,061 | 91,690 | 99,497 | 101,130 |
| Gross Fixed Capital Formation | 22,780 | 29,277 | 37,278 | 42,032 | 48,370 | 56,081 | 60,794 | 65,375 | 65,269 | 73,314 | 78,017 | 84,165 |
| Private | 14,097 | 18,945 | 25,509 | 28,652 | 33,300 | 38,457 | 41,402 | 42,802 | 41,381 | 46,878 | 46,727 | 52,456 |
| Public | 8,683 | 10,331 | 11,769 | 13,380 | 15,070 | 17,624 | 19,392 | 22,573 | 23,888 | 26,436 | 31,290 | 31,709 |
| Change in Stocks | 2,294 | 2,342 | 2,375 | 2,612 | 6,861 | 11,936 | 10,290 | 9,353 | 4,792 | 18,376 | 21,480 | 16,965 |
| Export of Goods and NFS | 14,226 | 23,909 | 30,948 | 47,548 | 53,084 | 55,405 | 73,853 | 68,659 | 78,150 | 88,360 | 91,821 | 77,796 |
| Errors and Omissions[c] | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 199 | 755 |
| Memorandum Item: | | | | | | | | | | | | |
| Gross Domestic Savings | 11,514 | 16,207 | 23,172 | 29,220 | 32,465 | 34,426 | 39,162 | 41,438 | 46,563 | 56,995 | 60,114 | 56,538 |
| Net Factor Income | 2,147 | 2,715 | 3,231 | 3,863 | 4,817 | 3,566 | 4,660 | 6,025 | 10,881 | 11,806 | 14,715 | 16,522 |
| Net Current Transfer | 218 | 482 | 581 | 495 | 819 | 900 | 1,009 | 1,158 | 1,205 | 1,319 | 1,456 | 1,664 |
| Gross National Savings | 13,879 | 19,404 | 26,984 | 33,578 | 38,101 | 38,892 | 44,831 | 48,620 | 58,648 | 70,120 | 76,285 | 74,724 |
| Gross National Product | 122,517 | 152,202 | 174,705 | 203,135 | 223,992 | 252,479 | 285,173 | 306,870 | 352,917 | 392,646 | 426,365 | 446,219 |

FY = fiscal year, GDP = gross domestic product, NFS = Non factor services.
[a] Revised estimate.
[b] Preliminary estimate.
[c] Represent data inconsistency within the same source.
Source: Ministry of Finance, Economic Survey FY2002.

## NEPAL: KEY ECONOMIC STATISTICS

### Table A2.5: Balance of Payments Summary
(NRs million)

| Item | FY1991 | FY1992 | FY1993 | FY1994 | FY1995 | FY1996 | FY1997 | FY1998 | FY1999 | FY2000 | FY2001[a] | FY2002[b] |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Trade Balance** | **(15,852)** | **(18,261)** | **(21,974)** | **(32,313)** | **(46,060)** | **(54,658)** | **(70,999)** | **(61,614)** | **(52,002)** | **(58,780)** | **(60,121)** | **(59,314)** |
| Export, FOB | 7,403 | 13,726 | 17,286 | 19,316 | 17,680 | 19,913 | 22,663 | 27,540 | 35,693 | 49,845 | 55,677 | 47,560 |
| Import, CIF | 23,256 | 31,987 | 39,260 | 51,629 | 63,740 | 74,571 | 93,662 | 89,154 | 87,695 | 108,624 | 115,797 | 106,873 |
| **Services, Net** | **2,692** | **3,893** | **5,064** | **17,477** | **23,565** | **20,923** | **39,361** | **29,128** | **30,201** | **26,446** | **22,239** | **9,070** |
| Receipts | 7,679 | 11,757 | 14,943 | 30,000 | 37,479 | 37,179 | 53,181 | 43,496 | 45,967 | 43,085 | 41,615 | 28,817 |
| Travel | 3,588 | 5,017 | 5,966 | 8,252 | 8,973 | 9,521 | 8,523 | 9,882 | 12,168 | 12,074 | 11,717 | 8,654 |
| Investment Income | 857 | 1,123 | 1,519 | 1,769 | 2,075 | 1,686 | 1,990 | 2,377 | 3,510 | 4,569 | 5,471 | 4,297 |
| Others | 3,235 | 5,617 | 7,458 | 19,980 | 26,430 | 25,972 | 42,667 | 31,237 | 30,289 | 26,442 | 24,427 | 15,866 |
| Payments | 4,988 | 7,864 | 9,878 | 12,524 | 13,913 | 16,256 | 13,820 | 14,368 | 15,766 | 16,639 | 19,376 | 19,748 |
| **Transfers, Net** | **3,661** | **4,294** | **6,937** | **6,809** | **10,709** | **12,193** | **15,130** | **17,298** | **22,036** | **23,368** | **26,928** | **30,520** |
| Receipts | 4,041 | 4,490 | 7,076 | 7,004 | 11,227 | 12,766 | 16,347 | 19,065 | 23,168 | 25,267 | 28,360 | 32,491 |
| Private Remittances | 2,128 | 2,317 | 2,994 | 3,469 | 5,064 | 4,284 | 5,595 | 6,988 | 10,315 | 12,662 | 15,903 | 20,951 |
| Official Grants | 1,694 | 1,690 | 3,499 | 3,040 | 5,339 | 7,583 | 9,743 | 10,920 | 11,648 | 11,286 | 11,001 | 9,839 |
| Indian Excise Refund | 188 | 422 | 562 | 494 | 819 | 900 | 1,009 | 1,158 | 1,205 | 1,319 | 1,456 | 1,701 |
| Others | 30 | 62 | 21 | 1 | 6 | — | — | — | — | — | — | — |
| Payments | 379 | 196 | 138 | 195 | 518 | 573 | 1,217 | 1,767 | 1,131 | 1,899 | 1,433 | 1,971 |
| **Current Account Balance** | **(9,500)** | **(10,074)** | **(9,972)** | **(8,027)** | **(11,786)** | **(21,542)** | **(16,508)** | **(15,188)** | **235** | **(8,966)** | **(10,954)** | **(19,724)** |
| Official Capital, Net | 6,300 | 7,326 | 5,474 | 10,723 | 8,805 | 7,401 | 8,390 | 10,370 | 9,101 | 8,485 | 6,976 | 2,964 |
| Foreign Loans | 7,154 | 8,710 | 6,960 | 12,975 | 11,396 | 10,285 | 11,233 | 14,236 | 13,264 | 12,548 | 11,715 | 8,040 |
| Amortization | (854) | (1,384) | (1,486) | (2,251) | (2,591) | (2,884) | (2,843) | (3,867) | (4,164) | (4,063) | (4,738) | (5,077) |
| Foreign Direct Investment | — | — | — | — | — | 388 | 1,621 | 685 | 578 | — | — | — |
| Miscellaneous Capital, Net | 7,332 | 6,142 | 12,238 | 3,587 | 2,668 | 12,673 | 9,699 | 15,100 | (74) | 14,928 | 9,199 | 14,269 |
| **Change in Reserves, Net** | **4,132** | **3,394** | **7,740** | **6,283** | **(314)** | **(1,081)** | **3,202** | **10,966** | **9,840** | **14,448** | **5,221** | **(2,491)** |

— = not available, CIF = cost, insurance, and freight, FOB = free on board.
[a] Revised estimate.
[b] Preliminary estimate.
Source: Ministry of Finance, Economic Survey FY2002.

## NEPAL: KEY ECONOMIC STATISTICS

### Table A2.6: Status of the Industrial Districts, FY2002

| Industrial District | Total Employed in ID (no.) | Employment by Industries (no.) | Sheds Constructed by Industrialists (no.) | Buildings Constructed by ID (no.) | Sheds Rented to Industrialists (no.) |
|---|---|---|---|---|---|
| Balaju Industrial Estate | 3,445 | 2,527 | 73 | 49 | 49 |
| Hetauda Industrial Estate | 4,669 | 3,214 | 378 | 15 | 15 |
| Patan Industrial Estate | 2,060 | 2,313 | 154 | 49 | 49 |
| Nepalgunj Industrial Estate | 519 | 721 | 30 | 20 | 20 |
| Dharan Industrial Estate | 433 | 519 | 38 | 16 | 16 |
| Pokhara Industrial Estate | 1,257 | 1,722 | 148 | 13 | 13 |
| Butwal Industrial Estate | 1,499 | 1,500 | 87 | 8 | 8 |
| Bhaktapur Industrial Estate | 627 | 709 | 44 | 12 | 12 |
| Birenda Nagar Industrial Estate | 28 | 47 | 0 | 6 | 6 |
| Dhankuta Industrial Estate | 1 | 1 | 0 | 0 | 0 |
| Rajbiraj Industrial Estate | 49 | 66 | 0 | 10 | 10 |
| Total | 14,587 | 13,339 | 952 | 198 | 198 |

FY = fiscal year, ID = industrial district, no. = number.
Source: Ministry of Finance, Economic Survey FY 2002.