

3. THE GOVERNMENT'S POVERTY REDUCTION PROGRAM

A. Historical Perspective

While poverty has always been an overriding concern in development planning in Nepal, only since the Sixth Plan (1981–1985) has it been explicitly stated as a development objective. During the Seventh Plan period (1986–1990), the Government formulated its Program for the Fulfillment of Basic Needs, the first separate plan for reducing poverty. Incorporating the Seventh Plan as one of its integral components, this ambitious long-term program envisaged elimination of poverty in Nepal over a 15-year period. However, it was later abandoned during the period of political upheaval.

Poverty alleviation was one of the major objectives of the Eighth Plan (1993–1997), the first national plan formulated after restoration of multi-party democracy in 1991. The Ninth Plan (1998–2002) adopted poverty alleviation as its sole objective, and unlike previous plans, established long-term goals for improving development indicators in all sectors, based on the potential of each for reducing poverty. While the Government has also endorsed and implemented master plans and perspective plans for reducing poverty that relate to individual sectors and subsectors, thus far these sectoral-level plans have not been integrated well with the national plan.

One of the goals of the Ninth Plan is to lower poverty incidence from 42% to 32% by the end of the Plan period in 2002, with a long-term goal of reducing this to 10% within the coming 2 decades. In addition to these targets, several other variables relating to “human poverty” (literacy, infant mortality, maternal mortality, and average life expectancy at birth) as opposed to “income poverty” have been identified, and target levels for each of these have been set.

The Ninth Plan intends to reduce poverty via

- (i) sustained and broad-based growth,
- (ii) development of rural infrastructure and social priority sectors, and
- (iii) specific programs targeting the poor.

The Ninth Plan is to employ a two-pronged strategy in using the above vehicles to reduce poverty incidence. First, the “moderately” poor, which constitute roughly 60% of the poor population, are to be integrated into the mainstream of economic development. Second, specific programs will deliver targeted assistance to the other 40% of the poor population, which comprises the “extremely poor” who face serious obstacles such as lack of assets that prevent them from participating in the mainstream of economic development due to geography, ethnicity, or cultural factors.

In addition to separately targeting these two groups of low-income households, the Ninth Plan includes other components that will benefit the poor, the two most important being maintaining macroeconomic stability and restructuring government finances to increase the flow of resources to the social sectors. Macroeconomic stability is essential for stimulating investment, without which growth and poverty reduction are not possible, and for keeping inflation rates low. A low inflation rate is an essential component of any poverty reduction effort in Nepal, since the nominal incomes of the poor generally fail to keep pace with price increases during periods of rapid inflation. On

the other hand, increasing the flow of resources to the social sectors directly increases the magnitude of the poverty reduction effort.

The Ninth Plan visualizes the annual population growth rate falling from its current level of 2.37% to 1.5% over the coming 2 decades. Complementing this will be changes in the nature of growth brought about by the Ninth Plan that will make growth “pro-poor”, meaning that growth will be of a type that integrates the poor into the mainstream of economic development. Since employment forms a major link between economic growth and poverty reduction, during the Ninth Plan period, the unemployment and underemployment rates of 4% and 35%, respectively, reported by the NLSS are to be reduced substantially via sectoral programs and employment-creation programs. Since 83% of poor households derive their livelihood from agriculture, highest priority will be given to employment creation in that sector.

The strategy for accelerating growth in agricultural output and productivity during the Ninth Plan period derives from the Agriculture Perspective Plan (APP), which was formulated in 1995. A long-term plan covering a 20-year time horizon, the objective of the APP is to raise the annual rate of growth of agricultural output from less than 3%, which prevailed during the previous 2 decades, up to 4% during the Ninth Plan period, and ultimately to 5% by the end of the 20-year planning period. This growth, which is to be achieved in a regionally balanced manner, will be driven by improved productivity overall, and specialization in regional comparative advantage, with the Terai producing basic food staples, and the Hills and Mountains specializing in high-value commercial crops and livestock products.

The Ninth Plan recognizes that not only must growth be made “pro-poor”, but that it must be made sustainable if the Government’s long-range poverty reduction goals are to be achieved. It thus sees the simultaneous achievement of economic growth, social justice, and ecological sustainability as being key to poverty reduction in the long term. Thus, the Plan sees accountable, democratic systems and market-oriented economic structures that avow social and ecological responsibility as being necessary for sustained growth. A capable state administering an appropriate regulatory framework is a precondition for the new development paradigm for Nepal envisaged in the Ninth Plan.

B. Poverty Reduction Strategy

In addition to the Ninth Plan, the Government’s commitment to poverty reduction was further reinforced by its presentations at the Nepal Development Forum meeting in Paris in April 2000. In order to further clarify the manner in which these broad statements are to be translated into concrete progress in poverty reduction via explicit programs and policy measures, and also to provide a general framework for poverty reduction within which all stakeholders can act in a coordinated way, the Government mandated NPC to prepare a poverty reduction strategy (PRS).

Given the significant number of stakeholders involved in the poverty reduction process in Nepal, the PRS is to be evolved through an extended participatory process, which will include consultations with both the public and aid community, as well as coordination among a significant number of government agencies. It will thus take some time to formulate the full-fledged version of the PRS. As a first step, NPC has prepared an interim PRS (IPRS). This chapter summarizes the salient aspects of the IPRS, and

uses the conceptual framework presented in Chapter 2 to suggest how the IPRS may be further refined within the context of gradual evolution of the IPRS into a full-fledged PRS.

1. Objective and Approach of the Government's IPRS

The major objective of the IPRS is to formulate a 3-year, time-bound action plan for poverty reduction in Nepal. It consists of two components: (i) a macroeconomic framework, and (ii) a policy matrix comprising specific actions for accelerating economic growth and reducing poverty. Policy commitments and targets relating to years beyond the 3-year time horizon are tentative, in that they may be revised as the IPRS evolves into a full-fledged PRS.

The approach used in developing the IPRS was to formulate a workable poverty reduction strategy on the basis of the results of the poverty situation analysis (summarized in Chapter 1), as well as public consultations and focus group discussions. The rationale for this approach was that the PRS should have as its foundation not only the economic analysis of poverty, but the cultural, ethnic, socioeconomic, institutional, and even political factors that relate to poverty as well. Thus, in addition to the perspective of central government institutions and aid agencies, the views of local government institutions, nongovernment organizations (NGOs), community-based organizations (CBOs), political parties, social leaders, and the poor themselves were taken into account in formulating the IPRS.

In formulating the IPRS, NPC constituted an Experts' Group under the coordination of NPC's Vice Chairman, the membership of which comprised representatives of various government agencies, NGOs, CBOs, the private sector, academia, and the members of the National Poverty Alleviation Advisory Committee.

The IPRS identified the following proximate causes of poverty:

- (i) slow overall economic growth in the face of relatively rapid population growth;
- (ii) weak redistributive capacity and institutional capacity overall on the part of the Government;
- (iii) lack of significant spillover effects of nonagricultural growth on the rural poor;
- (iv) low productivity and slow growth of output in the agriculture sector; and
- (v) weak social and economic infrastructure (health, education, drinking water, transport, energy, problems relating to landownership and land quality), leading to inadequate access of poor households to the means for escaping poverty.

2. Major Features of the IPRS

Employment Creation. In an attempt to achieve broad-based growth through employment promotion and improved productivity, the agriculture sector is given top priority in the Ninth Plan and IPRS. Employment creation necessary for lowering the rates of unemployment and underemployment of 4% and 35%, respectively, estimated by the NLSS is to be achieved via sectoral programs in both the agriculture and nonagriculture sectors. In the nonagriculture sector, expansion of tourism and labor-intensive manufacturing (e.g., garments and carpets) will be particularly emphasized. In the agriculture sector, employment creation is to be achieved via implementation of the APP, which focuses on increasing productivity and specialization in activities that accord with regional comparative advantage.

Macroeconomic Policies for Supporting Poverty Reduction. Nepal began its move toward an open, market-oriented economy in the mid-1980s with the partial deregulation of interest rates and lowering of barriers to entry for joint-venture banks. Since then, the momentum of economic reform has increased substantially. The Government has introduced numerous reforms that have lowered the fiscal deficit, thereby reducing borrowing costs and allowing a redirecting of public expenditure into priority social sectors. Key reforms accomplished thus far include a foreign exchange rate increasingly determined by market forces, full convertibility in the current account, a trade policy that has increasingly abandoned import substitution in favor of export promotion, a credit policy that specifically targets rural areas, and a shift in the focus of revenue mobilization from customs duties to a value-added tax and other sources.

As a means of providing an overall economic environment that can support acceleration of poverty reduction, the national economy will move further yet toward openness and market orientation. This will allow continued emphasis on priority social sectors, as well as specific interventions to counterbalance any adverse impact on the poor arising from economic reform. The IPRS sees maintaining macroeconomic stability within the above context as being the key to the Government's poverty reduction efforts.

Priority in Public Expenditure to Social Sectors. Following the World Summit on Social Development in 1995, Nepal adopted a policy of investing in the social sectors as per the 20/20 Compact. To fulfill this commitment, 20% of government expenditure as well as 20% of foreign development assistance must go to designated "social priority sectors". These include subsectors likely to benefit the poor most, such as providing primary health care facilities for all, reducing malnutrition and adult illiteracy, and establishing or upgrading facilities for primary education and rural drinking water. While actual achievement has fallen well short of the 20/20 goal, the share of expenditure going to the social sectors overall has increased from 22% in 1992 to 36% in 2000, although the rate of growth in expenditure going to the agriculture sector has declined.

This increase in the share of the social sectors in the public expenditure is reflected in expenditure per capita on social sectors as well, which rose by nearly 33% within a span of 4 years from \$9.09 in 1992/93 to \$11.90 in 1997/98. However, per capita expenditure on the social priority sectors increased only marginally from \$5.20 in 1994/95 to \$5.46 in 1998/99.

The positive developments in spending on the social sectors described above notwithstanding, that portion of expenditure on social sectors that is most likely to

benefit the poor is not rising in relative terms. This problem is further compounded by the fact that the budget allocations for the various sectors do not always result in disbursements, and that the ratio of allocations to disbursements is not the same for all sectors.

As for foreign assistance, the broad trend is similar to that discussed above for overall public expenditure. The share of foreign assistance going to the social priority sectors has declined in recent years, recovering only in 1999/2000. The major share of total aid disbursement has gone to infrastructure, followed closely by agriculture. Although quite recently the second largest share of foreign assistance has gone to the social sectors, the share of the social priority sectors remains well below the level stipulated in the 20/20 Compact.

Further, despite the improving trend in spending on the social sectors overall described earlier, in absolute terms, inadequate funding remains a major barrier to providing and delivering quality social services that would facilitate poverty reduction. Per capita public expenditures on social sectors are low in absolute terms, and have remained so due to rapid population growth. This impacts the quality of what services are provided. For example, educational institutions exhaust nearly all of their budgets on salaries and administrative costs, and health posts lacking adequate medical supplies are unable to provide quality services, particularly in remote, rural areas where these are essential to poverty reduction.

Overall, the share of the social sectors in public expenditure of approximately 28% is well below the international norm of 40%. However, the problem is not only a level of expenditure that is insufficient in absolute terms, but also inefficiency in utilizing the amounts that are allocated to the social sectors. Weak absorptive capacity on the part of the government institutions responsible for translating these expenditures into reduction in poverty incidence likewise forms a significant constraint to the efficient use of these funds.

Transfer Programs and Subsidies in Support of Poverty Reduction. Though several transfer and subsidy schemes are used to finance universities, hospitals, and some public enterprises, only a few directly impact the poor. These are a transport subsidy for chemical fertilizer administered via a direct grant to district development committees in selected remote areas where fertilizer transport costs are inordinately high, a transport subsidy for food distribution in remote and food-deficit districts, an interest subsidy for credit, and a capital subsidy for small-scale irrigation, mini-micro hydroelectric schemes, and biogas plants used for generating electricity.

Poverty Alleviation Fund. Since the early 1990s, various targeted and sectoral poverty alleviation programs have been implemented by the Government. However, the majority of these programs, which were centrally planned and implemented, ignored community preferences. This, together with weak program coordination and lack of monitoring and evaluation mechanisms, caused the impact of these programs to fall well short of that envisioned. To correct these problems, the Government has established a Poverty Alleviation Fund (PAF) for the purpose of initiating and implementing various sectoral as well as targeted poverty reduction programs that will be implemented via a coordinated and integrated approach that are envisioned to correct the problems described above. The PAF will especially focus on safety nets for the vast majority of the poor.

The PAF is to be an umbrella fund, not an implementing agency itself, which will mobilize both government and aid community resources for integrating poverty reduction programs. It is to be established under a special act, thus ensuring its autonomy and allowing it to function independently. A system for monitoring, reporting, and overall accountability relating to the use of funds will also be established at the central level. The PAF will be exclusively responsive to the needs of the poor, and will acquire the support of local agencies, NGOs, and CBOs. It will operate as a body for mobilizing resources—both internal and external—that concentrate on prioritized poverty reduction efforts and vulnerable groups.

Program Management and Monitoring and Evaluation. **In the past, implementation of some of the Government's poverty reduction programs have suffered from lack of coordination between the various line ministries, which are responsible for all sectoral programs, and the Ministry of Local Development, which is responsible for managing and implementing target-oriented programs. For example, construction of roads for improving access to rural agriculture (as stipulated in the APP) have experienced coordination problems in the nexus between the Roads Department and the Ministry of Local Development, both of which have some degree of responsibility for rural road construction.**

In light of the above, the Government's putting into place at the central level an effective mechanism for monitoring and evaluating poverty reduction programs, with a view to correcting any implementation problems encountered, will be the key factor in achieving the objectives of such programs. To be effective, this mechanism must involve the local level in the monitoring and evaluation process.

C. Constraints to Poverty Reduction

1. Weak Legal and Regulatory Functions

The Government's decision to move from a more centrally-directed economy to one that is more open and market-oriented does not necessarily imply a shift toward absence of—or even an overall reduction in—legal and regulatory functions. Indeed, the open, market-oriented economies that have enjoyed high rates of economic growth are often those that have made extensive use of legal and regulatory functions to ensure a stable, predictable environment in order to maximize the contribution to economic growth of private sector initiatives. In the context of Nepal's current position, it is these very legal and regulatory functions that need to be strengthened the most for the impact of poverty-reducing reforms, policies, and programs to achieve the goals intended. An important distinction between strengthening *functions* as opposed to strengthening the government agencies responsible for carrying them out needs to be drawn. This is so because upgrading the abilities of staff via training programs or improving the physical facilities of government agencies does not necessarily result in strengthening the legal or regulatory functions that a particular agency is responsible for carrying out.

The legal and regulatory functions that need to be strengthened the most in Nepal are those that support operation of competitive market forces rather than rent-seeking behavior. The efficient operation of these functions has yet to take full form.

Such legal lacuna relate particularly to enforcement of contracts, systems, and procedures that allow assets to be collateralized (e.g., clear title to land) and seized in the case of bankruptcy proceedings, and labor law. In the case of land use, legal provisions that restrict

the productive uses to which land may be put, and a land tax structure that encourages keeping land idle and unproductive need to be revised in a way that will allow the land resource to make maximum contribution to economic growth. Overall, there is concern that enforcement agencies are inadequate and poorly equipped, both in terms of authority and facilities.

2. Weak Overall Institutional Capacity

Institutional capacity encompasses an entire gamut of development activities—from planning to implementation to monitoring and evaluation. Ensuring competition, enforcing decisions, and coordinating different agencies both vertically and horizontally involves a host of legal and institutional frameworks. In view of the change in the Government's role from implementing authoritative norms to facilitating transparent systems and procedures, there is an immediate need for a change in mindset as well. But, instead, weak and unmotivated administration at all levels, and overcentralization of development activities with little delegation have incapacitated Nepal's government agencies. Increased politicization has further eroded the institutional strength of the Government. Obviously, all of these factors impede efficient operation of government agencies, whose role it is to provide an enabling environment in which the private sector can expand productive activities and employment opportunities.

In all sectors, the Government is limited in its ability to conceptualize, operationalize, monitor, and evaluate its own programs, and in learning from its experience. All of these attributes negatively impact the quality of services delivered. A compounding factor is that government administrative and management capacity decreases exponentially with distance from urban centers, further lowering the quality of service delivery in rural areas where it is critical to poverty reduction.

3. Weak Redistributive Capacity

The Government's capacity for redistributing either new or existing assets is extremely limited. In the case of existing assets (mainly land), the Government is handicapped by lack of any vision of land reform, as evidenced by its lack of follow-up action following the 1964 Land Reform Act. As for new assets, the Government is limited first by its inability to raise sufficient internal funds (Nepal has one of the lowest ratios of internal revenue generation to GDP at about 12%), and second, by its inability to allocate the internal funds that it does raise to priority social sectors such as primary and adult education, and basic health.

4. Weak Implementation of APP

While the APP provides a strong basis for planning and implementing agricultural development programs, there remain concerns with respect to its implementation. First, despite the fact that agriculture is taken as the lead sector in the Ninth Plan, it is not clear to what extent the plans for the nonagriculture sectors will produce a sectoral development pattern that supports and complement agriculture as the lead sector. Since no analytical framework was used to establish the nature of intersectoral linkages, the sectoral plans were formulated more or less independently of one another. It is therefore not unlikely that other sectors may not able to extend the necessary support to agriculture for it to function as the lead sector.