

# Economic Outlook Recap

*Insights, Trends, and Key Highlights  
January – December 2024*

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January 2024

## *Analyzing various economic indicators, it appears contradictory to conclude whether the Nepalese economy is shrinking!*

<i>Despite the perception of reduced imports, the average import trend shows an increase.</i>	<i>Similarly, while there's a belief remittance inflow may fall, the average remittance trend indicates growth.</i>	<i>Contrary to the notion of decreased in government revenue, the average revenue trend shows an increase.</i>	<i>Moreover, despite assumptions of reduced government spending, the average spending trend suggests otherwise.</i>	<i>Although the interest rate is perceived to be at its peak, the average interest rate trend is actually decreasing.</i>	<i>Additionally, although there's a perception of reduced forex reserves, the average reserve trend indicates growth.</i>	<i>It is said that NPA level of BFIs are increasing if you look from NRB prospective BFIs are more prudent and are becoming more transparent.</i>	<i>It is said industrial capacity utilization is low, however it is argued that industries are over capitalizes.</i>	<i>It is said that loan growth is slow indicating low confidence, however it is observed that borrowers are over leverage.</i>
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*Considering these conflicting observations, it is challenging to determine whether the Nepalese economy is experiencing growth or contraction.*

# Outlook 2024

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*In the aftermath of the COVID-19 pandemic, Nepal faced a challenging credit crunch scenario in 2023. Despite these difficulties, there's a positive outlook on the horizon. The country's economic revival is underway, and although growth expectations dipped below historical averages, there's optimism for a robust recovery. The initial sense of pessimism is giving way to resilience and adaptability, with the potential for substantial economic progress.*

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*While challenges persist, there's a concerted effort to overcome them. The consequences of the financial crisis are being addressed through strategic measures, fostering an environment conducive to investment, innovation, and overall economic development. The nation is on a trajectory to rebound from the setbacks experienced in the wake of the pandemic.*

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*Despite the lingering effects on domestic demand, economic activities, and market confidence, there are positive signs of gradual improvement. Government revenue, including VAT collections, is expected to see an upturn as economic conditions stabilize. Although there are rising obligations related to social security and administrative payments, prudent financial management is being implemented to navigate these challenges successfully.*

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*While economic analysts acknowledge the potential for continued economic headwinds, there's a prevailing belief that Nepal is well-positioned to weather these conditions. Strategic monetary and fiscal policies are being carefully considered to ensure stability and support the ongoing economic recovery. The nation's resilience and proactive measures instill confidence in a brighter economic future.*

# 2024 “Optimistic outlook while exercising prudence”

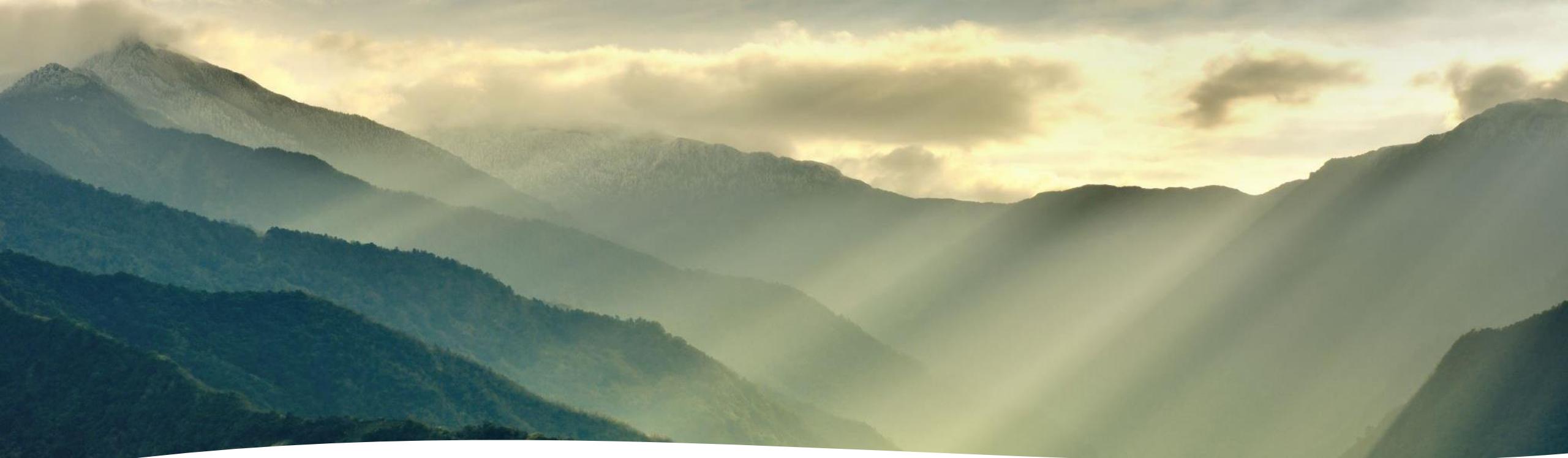
Positive developments are emerging for Nepal, propelled by proactive measures implemented by the central bank to address financial stability risks and achieve primary objectives. The Nepal Rastra Bank (NRB) acknowledges the intricate relationship between monetary policy and financial stability, emphasizing the need for coherent policy actions to prevent undue strain on the financial system. This commitment underscores a dedication to fostering a positive and secure financial environment.

Recent economic indicators for January 2024 demonstrate encouraging signs of improvement in consumer spending compared to previous quarters. Retail sales, particularly in interest rate-sensitive sectors like motor vehicles, have rebounded, indicating a favorable impact of the NRB's accommodating monetary policy.

While the recent arrest of some businessmen and bureaucrats has understandably caused concern within the business community,. Transparent communication of the rationale behind such actions is crucial to allay uncertainties. Upholding the rule of law is paramount, with the presumption of innocence until proven guilty being fundamental.

By promoting transparency and accountability, confidence in the stability and fairness of the legal system can be upheld within the business community. While acknowledging potential impacts on economic activity, trust in the economy's resilience to navigate through challenges is essential. Moreover, positive developments are evident in both manufacturing and non-manufacturing activities among businesses. With moderate long-term interest rates, overall improvements in financial conditions are expected to support household and business expenditures.

Although these trends are promising, caution is warranted, given past fluctuations in inflation and economic activity. The recent easing of financial conditions serves as a reminder of the multitude of factors influencing economic trends, underscoring the importance of prudent policymaking. Overall, a positive momentum is anticipated for 2024, with an optimistic outlook prevailing. it's important to maintain an optimistic outlook while exercising prudence.



# Climate Change: Assessing Nepal's Role and Urgent Needs

*Despite not being a major contributor to climate change, Nepal is currently grappling with its severe consequences. Even though our nation has not significantly contributed to climate-altering activities, we are acutely feeling the impact.*

*As we endeavor to shield our beautiful country of Nepal from the adverse effects of climate change, it becomes imperative to call on countries with substantial emissions to acknowledge their pivotal role in this global challenge. Collaborative efforts are essential to ensure that Nepal receives its fair share of assistance for implementing effective climate protection measures.*

*Despite challenges, the Nepalese economy is demonstrating resilience and progress, marked by stable inflation rates and a narrowing trade deficit. Remittances are experiencing an upward trend, contributing to increased financial inflows, while a surplus in the Balance of Payments and robust reserves signal overall stability. The growth in broad money and deposits further indicates the country's positive trajectory.*

*While there is concern over the rising level of Non-Performing Assets (NPAs), it's important to view this within a broader context. Elevated NPAs don't necessarily equate to an economy in decline but rather highlight areas that require attention and corrective action. Understanding the underlying causes is key. NPAs often result from borrower behavior, mismanagement, or the consequences of policy decisions. Loose monetary policies, for instance, have contributed to high NPA levels in Nepalese financial institutions. These policies prompted the introduction of seemingly secure yet risky financial products and low-interest rates, sometimes overlooking associated risks.*

*Some institutions inadvertently took on substantial risks by bundling risky loans into apparently safe products. While initially promising high returns with minimal risk, these products ultimately proved to be high-risk and low-yield. This underscores the importance of a comprehensive understanding of financial products and their inherent risks to effectively navigate challenges.*

*Furthermore, banking regulations emphasizing minimal capital requirements, light supervision, and market discipline have inadvertently exacerbated market instability. During upswings, they encourage riskier investments, while during downturns, they lead to reduced investments, amplifying market volatility. As banking and financial institutions (BFIs) grapple with the mounting pressure of meeting capital requirements, it is imperative for the Nepal Rastra Bank (NRB) to consider raising the maximum threshold for regulatory retail portfolios to Rs 50 million. This adjustment would provide much-needed relief to BFIs, allowing them to bolster their Capital Adequacy Ratio (CAR), a crucial indicator of financial health and stability. By accommodating larger retail portfolios within the regulatory framework, BFIs can enhance their ability to manage risk and allocate resources effectively.*

*Moreover, NRB should conduct a comprehensive review of the risk weightage assigned to various items on the balance sheet. This entails a meticulous assessment of the potential risks associated with different assets and liabilities held by BFIs. By recalibrating the risk weightage, NRB can ensure that the regulatory framework accurately reflects the inherent risks in banking activities, thereby promoting prudence and stability in the financial sector. This proactive approach by the regulatory authority would not only facilitate the strengthening of BFIs' CAR but also contribute to overall systemic resilience and confidence in the banking system.*

*Despite these challenges, which also include issues related to corporate governance and declining customer confidence, the Nepalese economy remains resilient. With proactive measures and a commitment to addressing underlying issues, Nepal is poised for continued growth and stability.*

Feburary 2024



# 2024 “Familiar risks emerge in new ways”

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*In the wake of the COVID-19 pandemic, Nepal endured a severe credit crunch scenario throughout 2023 and early 2024, presenting daunting challenges. However, amidst these adversities, a glimmer of hope emerges. The country's economic resurgence has commenced, albeit with growth expectations falling below historical norms. Despite this setback, there is a cautious optimism for a resilient recovery. The initial wave of pessimism is gradually yielding to a spirit of resilience and adaptability, signaling the potential for significant economic advancement.*

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*Despite ongoing challenges, there is a dedicated effort to confront them head-on. Strategic measures are being implemented to tackle the aftermath of the financial crisis, nurturing an atmosphere favorable to investment, innovation, and overall economic progress. Considering these challenges and the pervasive uncertainty surrounding the economic landscape, we will remain vigilant, closely monitoring data, particularly the upcoming inflation data revisions and reports. This information will be crucial in determining the suitable trajectory for monetary policy.*

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*Inflation expectations have remained relatively stable. Anticipated growth in consumer spending this year is expected to be slower compared to last year. The substantial reserves of excess savings accumulated in the initial stages of the pandemic have bolstered household spending over recent years. However, it is probable that these surplus savings have been largely depleted, particularly among households in the lower income brackets. There are emerging indications of heightened financial strain among certain households, as evidenced by increasing delinquency rates on credit cards and mortgages.*

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*Business spending growth is expected to slow down slightly this year, mainly due to the anticipated stabilization of the widely discussed low-capacity utilization, which is expected to persist for the next few months. Nonetheless, over time, there is a projection for investment to increase, although this transition is likely to be gradual. Consequently, fiscal and monetary sector conditions are expected to become slightly less restrictive.*

# 2024 “Optimistic outlook while exercising prudence”

Positive developments are emerging for Nepal, propelled by proactive measures implemented by the central bank to address financial stability risks and achieve primary objectives. The Nepal Rastra Bank (NRB) acknowledges the intricate relationship between monetary policy and financial stability, emphasizing the need for coherent policy actions to prevent undue strain on the financial system. This commitment underscores a dedication to fostering a positive and secure financial environment.

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While the recent arrest of some businessmen and bureaucrats has understandably caused concern within the business community,. Transparent communication of the rationale behind such actions is crucial to allay uncertainties. Upholding the rule of law is paramount, with the presumption of innocence until proven guilty being fundamental.

By promoting transparency and accountability, confidence in the stability and fairness of the legal system can be upheld within the business community. While acknowledging potential impacts on economic activity, trust in the economy's resilience to navigate through challenges is essential. Moreover, positive developments are evident in both manufacturing and non-manufacturing activities among businesses. With moderate long-term interest rates, overall improvements in financial conditions are expected to support household and business expenditures.

Although these trends are promising, caution is warranted, given past fluctuations in inflation and economic activity. The recent easing of financial conditions serves as a reminder of the multitude of factors influencing economic trends, underscoring the importance of prudent policymaking. Overall, a positive momentum is anticipated for 2024, with an optimistic outlook prevailing. it's important to maintain an optimistic outlook while exercising prudence.

# Charting a New Course for Reform

## *Financial Sector Reform Objectives:*

*The primary goals of financial sector reform should encompass averting credit crunches and banking crises while emphasizing effective management should such crises occur. Additionally, these reforms must prioritize support for low-income earners. Prudential regulation and supervision should address not only microeconomic but also macroeconomic risks associated with boom-bust cycles.*

## *Asset Management Company (AMC):*

*Given the escalating levels of non-performing assets (NPAs) and the potential for corporate defaults to trigger economic downturns and unemployment, the opportune moment has arrived to initiate the establishment of an Asset Management Company (AMC). Establishing an AMC to handle the bad loans of Banking and Financial Institutions (BFIs) can strategically address NPAs and enhance the financial health of the banking sector. The creation of an NPA management AMC is a pivotal step in addressing challenges posed by bad loans, benefiting BFIs by improving financial health and contributing to overall economic stability and growth. I wholeheartedly endorse the establishment of such an institution and believe it can be a game-changer in addressing NPA-related issues in the financial industry.*

## *Amendment to the NRB Act:*

*Amending the NRB Act should heavily emphasize a comprehensive evaluation of the NRB Board's composition. The current composition, predominantly comprising retired NRB employees, should undergo restructuring to include experts from diverse economic and professional backgrounds. However, careful consideration of specific qualifications and selection criteria for these external experts is crucial to ensure they possess the necessary skills and knowledge to contribute effectively to the central bank's functions. Additionally, the governance structure should strike a balance between external expertise and the central bank's internal knowledge and experience.*

## *Establishment of a Monetary Policy Committee:*

*The establishment of a Monetary Policy Committee is imperative to ensure both independence and accountability in the policymaking process. While separating the roles of monetary policy and credit policy can offer advantages, emphasizing the significance of coordination and communication among responsible authorities is essential. These factors are vital for safeguarding overall economic stability and the health of the financial system.*

<b>BAFIA Amendment:</b>	<p><i>The BAFIA (Banking and Financial Institutions Act) requires amendments that incorporate provisions for an exit mechanism for BFI promoters. Encouraging a significant public holding will elevate governance standards within these institutions. Additionally, a reevaluation of the Board's composition is recommended, introducing a blend of executive and non-executive directors to enhance governance. Furthermore, restructuring BFIs based on their functions, rather than solely on capital, will promote efficiency and relevance in the financial sector.</i></p>
<b>GDP Base Review:</b>	<p><i>The Government of Nepal should contemplate updating the base year for GDP calculation from 2010/11 to 2020/21. This adjustment is warranted due to four significant events post the Great Gorkha Earthquake: a trade embargo, changes in government structure, and the impact of the Covid-19 pandemic. Shifting the base year to 2020/21 will provide a fresh perspective for policy formulation and response, considering the evolving economic landscape</i></p>
<b>Prompt Corrective Action:</b>	<p><i>In addition to the current PCA guidelines, the NRB should consider introducing supplementary provisions. If the net NPA level is below 7%, no further action is necessary. However, if it surpasses 7% but remains below 9%, falling within the first threshold, BFIs should refrain from approving new loans. Crossing the 9% threshold triggers the second tier, where BFIs must abstain from accepting new deposits. Should this metric reach 11% or higher, the bank will be categorized into the third tier, prompting PCA initiation.</i></p> <p><i>Furthermore, concerning the Income Tax Act, the permissible provisions charged to the Profit and Loss statement (P&amp;L) should be increased from 5% to 9%. Additionally, the NRB should undertake a comprehensive review of the risk weightage assigned to various items on the balance sheet. This involves a meticulous assessment of the potential risks associated with different assets and liabilities held by BFIs. Through recalibrating the risk weightage, the NRB can ensure that the regulatory framework accurately reflects the inherent risks in banking activities, thereby fostering prudence and stability in the financial sector.</i></p>

## Charting a New Course for Reform

# March 2024

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As the Investment Summit 2024 approaches, there's an opportunity for the Nepalese government to enhance its readiness, emphasizing the importance of prioritizing key factors to foster Foreign Direct Investment (FDI). Both Nepalese and foreign investors, from both private and public sectors, stand to benefit from a range of investment avenues in Nepal. Considerations such as tax advantages, parent company relationships, technical assistance, technology infusion, business and financial projections, and liability limitations offer promising opportunities when selecting the appropriate investment vehicle or structure.

1. *Acquiring stock or assets by foreign companies:* Clearing up authorities and discretionary powers can streamline the process of purchasing shares or assets of local companies, ensuring smoother market access. Swift government attention can resolve these issues and boost preparedness.
2. *Establishing a branch by foreign companies:* Simplifying the branch registration process will facilitate efficient communication and accounting, requiring legal reforms and administrative improvements for enhanced operational efficiency.
3. *Setting up a representative office by foreign companies:* While representative offices serve non-income-generating activities, they contribute to FDI and business promotion in Nepal, warranting thoughtful consideration despite ongoing reform efforts.
4. *Establishing a subsidiary by foreign companies:* While creating new companies presents benefits, addressing commercial and legal concerns, including liability limitations, calls for careful government oversight. Legal and tax reforms are pivotal to support established subsidiaries.
5. *Joint ventures:* Strategic planning is essential for effective resource pooling through joint ventures, particularly amid ongoing legal reforms.

The Investment Summit presents an opportunity for Nepal to accelerate progress and avoid falling behind. Despite challenges, there's a spirit of cautious optimism, and success is anticipated at the summit.

As we prepare for the upcoming investment summit, we are reaching out to highlight crucial considerations vital for its success, requiring the attention of the Government of Nepal (GoN). Beyond logistical arrangements, hosting an investment summit demands a deep understanding of investors' needs and expectations. Demonstrating respect for investors entails actively listening to their concerns, addressing their priorities, and providing a platform for their voices to be heard. By doing so, GoN can foster a sense of trust and partnership crucial for nurturing long-term relationships and future investments.

Additionally, We have observed several significant impediments to foreign direct investment (FDI) across multiple sectors, including:

1. *Investment restrictions and entry barriers in sectors of substantial potential or investor interest.*
2. *Lack of consistent long-term policies, non-implementation, or policy reversals.*
3. *Inequitable playing fields, particularly in sectors dominated by public sector undertakings (PSUs).*
4. *Rigidity in labor laws*
5. *Redundant regulatory agencies and multiple approval requirements lead to bureaucratic delays.*
6. *Subjective practices, discretionary interpretation, and bureaucratic biases.*
7. *High entry costs, increasing transaction expenses, and ineffective dispute resolution mechanisms.*
8. *Poor infrastructure maintenance and development.*
9. *Lack of clearly identified priority sectors.*
10. *Challenges related to corruption, red tape, and indecision.*

Furthermore, we urge the government to prioritize the overhaul of the dispute resolution mechanism. Investor confidence in the protection of their interests and the prompt resolution of disputes is paramount. Currently, several factors hinder fair tax assessments in Nepal, such as:

1. *Insufficient proficiency of tax investigators leading to errors in assessments.*
2. *Inconsistent exercise of discretionary powers.*
3. *Lack of standardized procedure for interpretation of statutes resulting in uncertainties and disputes.*

Addressing these challenges necessitates initiatives to enhance the skills of tax investigators, promote information-sharing, standardize the application of discretionary powers, and provide clearer guidelines for interpreting tax laws. By modernizing and enhancing dispute resolution mechanisms, GoN can instill confidence in the integrity of the investment landscape, crucial for attracting more investors and fostering economic growth.

Investors who feel respected listened to, and assured of fair treatment are more likely to actively engage and contribute positively to the summit's objectives. Therefore, addressing these concerns will ultimately enhance the summit's success by strengthening relationships, facilitating agreements, and driving investment.

## 2024 "Persistent Stagnation in Bank Credit Growth Despite Lower Lending Rates"

Economic activity within Nepal has been sluggish, although there are some positive developments, primarily attributed to increased remittances. However, the manufacturing sector, which plays a pivotal role in industrial activity, has not experienced notable advancements on the supply side.



Migration and urbanization have triggered a downturn in rural demand, expected to persist at lower levels compared to the previous fiscal year of 2023/24. Throughout the ongoing fiscal year, there has been a 1.52% decrease in the weighted average lending rates. Consequently, there has been a slight rise in urban demand for domestic capital goods, as evidenced by various economic indicators.

Despite the low lending rates, credit demand has remained subdued, with bank credit growth remaining stagnant. This is attributed to the elevated concentration of government securities and excess liquidity held by financial institutions. As a result, banks have persisted in adjusting their lending and deposit rates downwards to accommodate the lack of significant demand for credit. This ongoing trend has resulted in notable decreases in the weighted average lending and deposit rates.



Consumer confidence for this year has reached a record low, and construction activity has also been lackluster. Investment outlook remains bleak due to various factors, including subdued demand for credit from corporate, especially those in manufacturing; sustained low government capital expenditure; weakened balance sheets of both banks and corporates; diminished capacity utilization; and declining business sentiment.



# Strategic Measures for Economic Recovery and Stimulus Initiatives in Nepal

## Strategic Path for Economic Recovery

The Government of Nepal is urged to articulate a comprehensive strategy for economic recovery, incorporating the following measures:

### 3. Embrace the "New Economy"

Identify and capitalize on opportunities within the "new economy," focusing on financial services, digital technology, telecommunications, and other sectors less reliant on physical presence.

### 4. Enhance Competitiveness

Evaluate the ease of doing business, aligning with international standards to enhance competitiveness.

### 1. Foundational Concepts for Inclusive Revival

Develop and prioritize foundational concepts to ensure an inclusive economic revival.

### 2. Sectoral Adaptation and Support

Anticipate and address challenges in vital economic sectors through strategic support, encompassing agriculture, manufacturing, retail, hospitality, construction, and related industries.

### 6. Stakeholder Engagement

Promote active engagement with stakeholders, including businesses, employee representatives, and other bodies.

### 7. Tailored Initiatives

Create, develop, and assess actionable initiatives tailored to specific sectors (e.g., hospitality, Agri, and technology) and overarching themes (e.g., productivity).

### 8. Data Enhancement

Scrutinize existing data sources and explore innovative metrics to improve decision-making.

### 9. Performance Framework

Contemplate a new delivery and performance framework for reporting key economic achievements.

April 2024



Let's begin by summarizing our review of the catastrophic failure of cooperatives. This incident marks the first large-scale collapse of non-regulated Saving and Credit Cooperatives since the promulgation of the Federal Nepal constitution, highlighting a dire need for a thorough and uncompromising examination of the underlying failures.

Inexperienced and poorly trained staff within the cooperatives were directly involved in conducting business. Consequently, the cooperative's management was utterly incapable of managing risks, and its board failed miserably in overseeing management. Additionally, the review uncovered that supervisors did not identify issues swiftly enough, and when risks were finally acknowledged, their response was agonizingly slow and insufficient to effect meaningful change in management behavior.

There is an urgent need to enhance the speed, force, and agility of supervision to align with the risks, size, and complexity of cooperatives. The Government of Nepal (GoN) must focus on several critical areas: intensifying supervision at an appropriate pace, ensuring timely supervisory action and escalation, and improving the overall agility of supervision. Immediate and long-term measures must be implemented to strengthen supervision.

Supervisors do not manage cooperatives; their role is to evaluate a cooperative's significant risks in light of its operations and ensure the cooperative maintains adequate governance and controls, capital, and liquidity to function both in normal and stressful times. The GoN should concentrate on the unique risks of each cooperative while also considering the broader risk landscape across similar firms within the banking system. These two perspectives are crucial for identifying and prioritizing key risk areas and compelling management to address the most critical issues.

The goal of supervision is not to prevent all failures. In a market economy, poorly managed firms should be allowed to fail. Likewise, the aim of supervision is not to dictate a cooperative's business model viability; the market will determine that. Instead, the focus should be on helping cooperative managers and boards identify and address weaknesses in risk measurement and management practices, legal compliance, and the adequacy of capital and liquidity given the cooperative's risk profile. Proactive supervisory actions can help firms address issues before they become insurmountable, allowing for earlier intervention and providing firms with more options to rectify their problems..



# 2024 “Optimistic outlook while exercising prudence”

*Let's start by evaluating the current situation with a more critical perspective.*

*Despite some proactive measures taken by the central bank to address financial stability risks, the effectiveness of these actions remains questionable. The Nepal Rastra Bank (NRB) recognizes the complex interplay between monetary policy and financial stability, but whether their strategies will prevent undue strain on the financial system is uncertain. This situation reveals the NRB's ongoing struggle to maintain a stable and secure financial environment.*

*Recent economic indicators for April 2024 show only a slight improvement in consumer spending compared to previous quarters. The rebound in retail sales, particularly in interest rate-sensitive sectors like motor vehicles, may be a temporary response to the NRB's accommodating monetary policy rather than a sign of sustained economic health.*

*The recent arrest of businessmen and bureaucrats has understandably caused significant concern within the business community. The lack of transparent communication regarding the rationale behind these actions has only heightened uncertainties. While upholding the rule of law is crucial, the presumption of innocence until proven guilty must be maintained to avoid undermining confidence in the legal system.*

*Promoting transparency and accountability is essential to restore trust in the stability and fairness of the legal system within the business community. However, the potential negative impacts on economic activity cannot be overlooked. The business community's confidence in the economy's resilience to navigate through these challenges remains fragile. Although there are some positive signs in both manufacturing and non-manufacturing activities, these improvements are modest at best. The expectation that moderate long-term interest rates will support household and business expenditures is overly optimistic, given the persistent uncertainties.*

*While these trends offer a glimmer of hope, caution is necessary, especially considering past fluctuations in inflation and economic activity. The recent easing of financial conditions serves as a stark reminder of the multitude of factors that can influence economic trends, highlighting the critical need for prudent policymaking. Overall, while there is some momentum heading into 2024, a more cautious and realistic outlook is warranted. Instead of an overly optimistic view, it is imperative to remain vigilant and prudent in managing the economic challenges ahead.*

## Decriminalization of Corporate Laws: Paving the Way for Business Innovation

In today's rapidly evolving business environment, decriminalization is crucial for fostering growth and innovation. But what does decriminalization mean, and why is it important?

## Understanding Decriminalization:

Decriminalization involves removing criminal penalties for certain corporate actions or omissions. Instead of criminal prosecution, non-compliance may lead to civil fines. This shift from punitive measures to a more pragmatic approach helps protect business reputations and build trust and confidence among stakeholders.

## Reasons for Decriminalizing Business Laws:

- **Protection of Reputation:** Criminal charges can damage a business's reputation, affecting its relationships with customers, partners, and investors, even if the charges are not substantiated.
- **Facilitating Innovation:** Simplified compliance protocols and streamlined procedures encourage creativity and investment, driving economic growth.
- **Global Trends:** Leading economies like the UK, Singapore, and the US are implementing regulatory reforms to reduce bureaucracy and enhance the business environment, setting a model for others to follow.

## Tangible Benefits of Decriminalization:

- **Reduced Compliance Burden:** Businesses can focus on core operations and innovation without the fear of imprisonment for minor infractions.
- **Faster Business Setup:** Streamlined regulations speed up the registration process, attracting more entrepreneurs and investment.
- **Lower Costs:** Legal fees associated with defending against minor criminal charges are reduced, and simplified regulations lower administrative costs.
- **Improved Efficiency:** Resources are freed up, allowing courts to prioritize serious crimes. Businesses are motivated to self-regulate to avoid fines.
- **Enhanced Business Confidence:** A predictable regulatory environment fosters trust and encourages risk-taking, driving economic growth.

**Real-World Examples:** India's Jan Vishwas Bill and amendments to Korea's Companies Act highlight the positive impact of decriminalization on business landscapes.

**Challenges:** Balancing deterrence with leniency for minor infractions and ensuring effective enforcement mechanisms remain critical issues.

**Conclusion:** Decriminalization is not about avoiding consequences but creating a business-friendly environment that promotes growth and innovation. Pragmatic reforms in corporate law are essential for shaping a brighter future for businesses worldwide.

# *Nine Enablers of Nepalese Economy*

*As capital expenditure is crucial for achieving growth objectives in the Federal Structure Economy, Nepal should focus on following basic principles:-*

- *Design Long-term vision and strategy for economic development and social harmony,*
- *Prepare Project Banks - investment project preparation to invite local as well as foreign investment,*
- *Reduce Budgetary processes to speed up capital expenditure,*
- *Improve Procurement Efficiency and maintain budgetary discipline,*
- *Implement Stringent Contract Management and enforcement requirements to maintain time schedule of the project.*
- *Design an Effective Monitoring system to improve the productivity of investment,*
- *Appoint Competent Project Personnel led by dynamic person,*
- *Support effective Legal Institutional Framework for PPP investment and introduce fund base investment approval process.*
- *Enabling sectoral policy Operation Framework*

*The government of Nepal must plan effectively and effectively and should continuously monitor its activities to achieve sustainable goals and high growth.*

May 2024

## International Monetary Fund (IMF)

According to International Monetary Fund (IMF) Nepal's economy, after a slowdown last year, is showing signs of recovery. Economic activity is expected to increase, supported by a cautiously accommodative monetary policy, increased capital expenditure in the FY2024/25 budget, additional hydropower generation, and a rise in tourist arrivals. Inflation is projected to stay within the 5.5 percent target, and the external position is expected to strengthen further.

Significant fiscal achievements include the approval of a Domestic Revenue Mobilization Strategy and an Action Plan for improving budget execution. The Nepal Rastra Bank (NRB) has also finalized and implemented a Supervisory Information System for banks and is making progress on procuring an international consultant for a Loan Portfolio Review of the 10 largest banks.

Nepal is also committed to improving its anti-money laundering and combating the financing of terrorism (AML/CFT) framework. Recent legal amendments and ongoing efforts to align with international standards are steps in this direction, with continued technical support from the IMF and other donors.

Looking ahead, growth is expected to reach 4.9 percent in FY2024/25, driven by stronger domestic demand and strategic investments, particularly in the energy sector. The policies and reforms under the ECF program are designed to support this growth while maintaining macroeconomic stability. Key priorities include accelerating capital spending, strengthening the monetary framework, and enhancing the financial system's resilience.

Despite these advances, the economy faces challenges. Growth is projected at around 3 percent for FY2023/24, below potential due to subdued domestic demand and post-pandemic balance sheet repairs. Inflation has decreased to 4.6 percent in April 2024 from a peak of 8.6 percent in September 2022. However, the tax-to-GDP ratio remains below pre-pandemic levels, limiting fiscal space for development spending. Additionally, non-performing loans in banks have doubled since August 2022, and the financial health of savings and credit cooperatives has worsened.

# 16th Five-Year Periodic Plan (2081/82-2085/86)



GOOD GOVERNANCE,



SOCIAL JUSTICE,



PROSPERITY.

The plan aims to address structural obstacles to development and implement transformational strategies to achieve its ambitious targets.

<i>Strengthen</i>	<i>Strengthen macroeconomic fundamentals and promote rapid economic growth.</i>
<i>Enhance</i>	<i>Enhance production, productivity, and competitiveness.</i>
<i>Create</i>	<i>Create decent jobs and promote productive employment.</i>
<i>Foster</i>	<i>Foster educated, skilled, and healthy human capital.</i>
<i>Develop</i>	<i>Develop quality infrastructure and integrated transport systems.</i>
<i>Promote</i>	<i>Promote modern, sustainable urbanization and settlements.</i>
<i>Empower and include</i>	<i>Empower and include marginalized communities.</i>
<i>Improve</i>	<i>Improve fiscal management and capital expenditure.</i>
<i>Promote</i>	<i>Promote good governance, LDC graduation, and sustainable development goals.</i>

#### **Economic Goals:**

1. Achieve an economic growth rate of 7.3% (current: 3.9%).
2. Increase per capita income to \$2,413 (current: \$1,456).
3. Reduce absolute poverty to 17 % and consumer inflation to 5%.
4. Improve the human development index from 0.601 to 0.650.
5. Extend average life expectancy from 71.3 to 73 years.

#### **Economic Projections**

1. Raise the revenue-GDP ratio to 24% (current: 17.8%).
2. Increase federal expenditure to 32% of GDP (current: 26.5%).
3. Maintain sovereign debt below 45% of GDP.
4. Reduce the trade deficit to 24% of GDP (current: 27%).

#### **Social and Infrastructure Goals:**

1. Enhance access to health facilities to 90% of families (current: 77%).
2. Raise literacy rates to 85% and reduce unemployment from 11.4% to 5%.
3. Boost hydropower production from 3,100 MW to 11,769 MW.
4. Ensure 90% internet access and 85% financial institution access for families.

## Sectoral Strategies:

### **A. Foreign Employment:**

- Identify new high-return employment destinations.
- Sign bilateral labor agreements for safe and secure foreign employment opportunities.

### **B. Energy Sector:**

- Export electricity worth Rs 41 billion annually by the end of the plan.
- Promote the energy sector to reduce the trade deficit.

### **C. Employment and Social Goals:**

- Create 1.2 million jobs annually.
- Raise the minimum wage to Rs 25,000 per month.
- Increase social security beneficiaries to 2 million.

### **D. Governance and Competitiveness:**

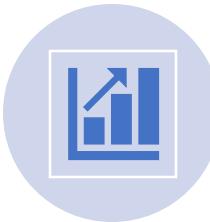
- Improve the rule of law index from 0.52 to 0.80.
- Increase the global competitiveness index from 52 to 65.
- Enhance the corruption reduction awareness index from 35 to 43

## Implementation Strategy:

- Focus on structural transformation, adopting new technologies, and promoting research and development.
- Collaborate with private, government, and non-government sectors for national skill development.
- Prioritize marginalized community empowerment and inclusive employment

## **Summary of Nepal's Economic and Financial Condition in FY 2022/2023:**

*The economic condition of Nepal appeared modest in FY 2022/2023. Inflation was marginally above the target, while remittance inflows and foreign exchange reserves showed a positive trend, increasing gradually. The external sector performed well, leading to a reduction in the current account deficit and maintaining a surplus in the balance of payments. The consolidation of banks and financial institutions resulted in a decrease in the number of financial institutions, thereby strengthening the resilience of the financial system. However, with larger financial institutions, vigilant regulation to manage the buildup of risks is becoming increasingly important.*



*Financial soundness indicators demonstrated the resilience and stability of the financial system. The capital adequacy of BFIs remained well above regulatory requirements. However, there are concerns about the stability of BFIs due to deteriorating asset quality. High interest rates and borrowing costs have suppressed demand, and firms continue to face challenges in financing their debt. This situation has negatively impacted banks' balance sheets, as evidenced by low profitability and elevated levels of non-performing loans. The unwinding of accommodative monetary policy in the context of Covid-19 could further affect borrowers' repayment capacity and put additional pressure on the stability of financial institutions. Despite these challenges, BFIs managed to maintain adequate capital, liquidity, and profitability.*



*The growing share of the non-bank financial sector has increased the interdependence and interconnectedness within the financial system. Sharing financial resources among BFIs, insurance companies, cooperatives, FinTechs, and other contractual savings institutions like the Citizen Investment Trust, Social Security Fund, and Employees Provident Fund has facilitated the mobilization of resources to support economic activities. However, this interconnectedness also introduces risks in new areas of the financial system. Issues such as mission drift, weak governance practices, and predatory lending without proper financial analysis raise concerns about the soundness of cooperative institutions. These issues, coupled with political instability and economic slowdown, could exacerbate the situation and create spillover effects in the financial system.*



*The NRB has been actively working towards financial inclusion and access by introducing regulatory measures targeting specific sectors, deprived populations, and small borrowers. The expansion of bank branches to almost all local levels, rising financial literacy, and the growing use of digital financial services have significantly improved financial inclusion and access.*



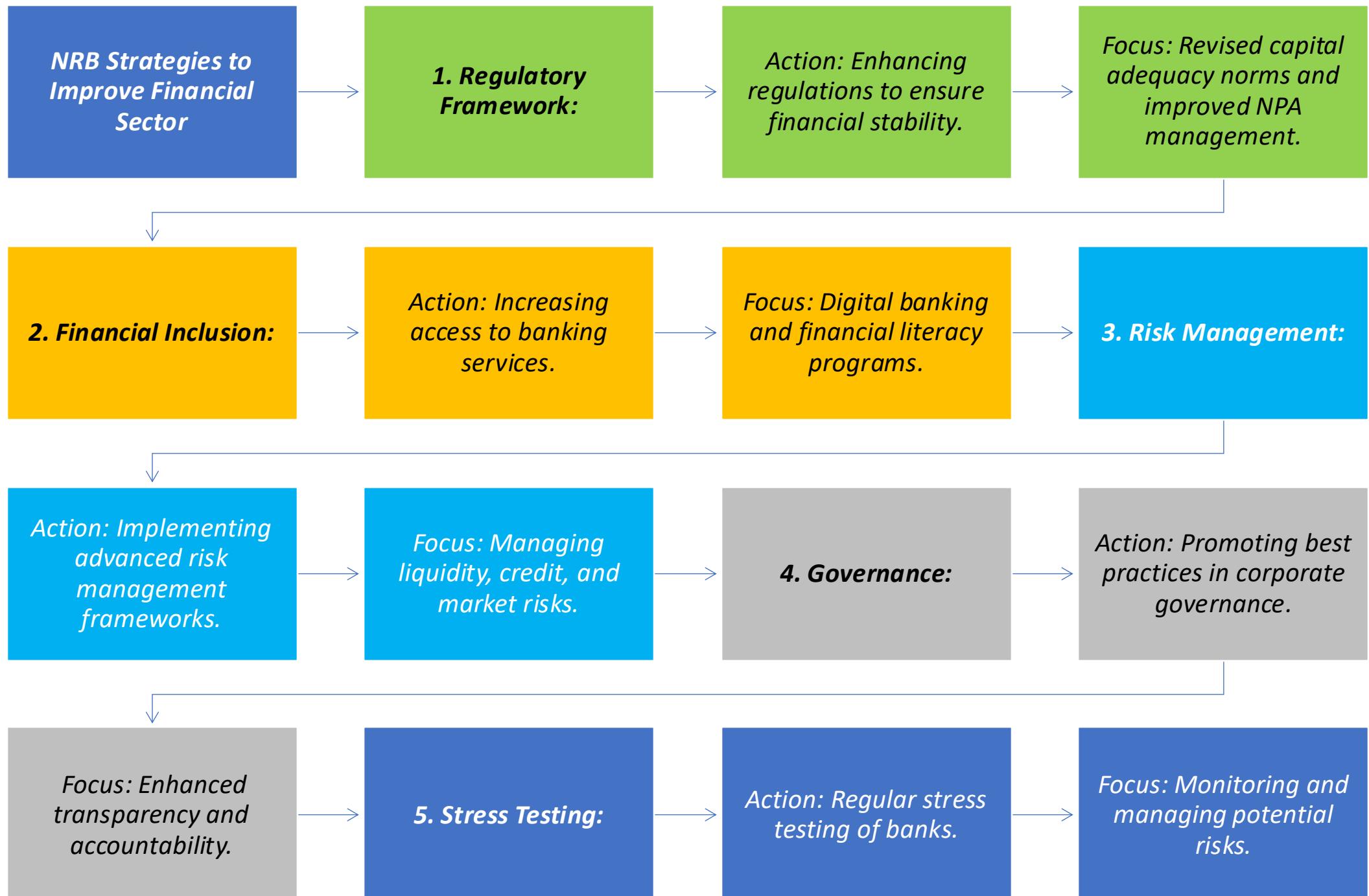
*Digital payment modes such as QR payment, Connect IPS, mobile banking, and RTGS have further enhanced NRB's mandate to promote financial inclusion and access. However, the rapid acceleration in digital financial services poses challenges to the financial system. Protecting financial consumers against risks such as information safety, online deception, and fraud remains challenging.*



*Additionally, vulnerabilities and risks in digital infrastructures and institutions could undermine the effectiveness of regulation and increase system-wide risks. Therefore, strong oversight of digital financial services is essential to maintain financial stability.*



*In summary, tighter monetary policy supported by macro-prudential regulations helped contain price and external sector imbalances. The financial system remains stable despite increased uncertainties. However, the path ahead appears challenging, with downside risks in domestic and international economies threatening the soundness of the financial system. Maintaining financial stability and resilience will significantly depend on initiatives to assess the financial system's soundness in conjunction with prudent regulation and supervision of risk buildup.*



# Budget 2024/25

**Impact of COVID-19:** The significant gap between the budgeted and actual growth rates in 2020/21 and 2021/22 highlights the severe impact of the COVID-19 pandemic on Nepal's economy. The lower actual growth rates reflect the disruptions in business activities, loss of confidence, and overall economic slowdown.

**Recovery and Projections:** The budgeted growth rates for 2022/23 and 2023/24 show optimism for recovery. However, the actual and estimated figures suggest that the recovery is slower than expected, with growth rates still below pre-pandemic levels.

**Inflation Trends:** Inflation has been volatile, with actual rates often exceeding budgeted expectations, especially in 2021/22 and 2022/23. This indicates economic instability and challenges in controlling price levels. The estimated decrease in inflation for 2023/24 suggests anticipated stabilization as the economy gradually recovers.

Overall, the data illustrates the challenges Nepal faced due to the pandemic, including slower growth and higher inflation, and highlights cautious optimism for recovery in the coming years.

Particulars	Budget 2020/21	Budget 2021/22	Budget 2022/23	Budget 2023/24	Budget 2024/25
Growth Rate	7.0%	6.5%	8.0%	6.0%	6.0%
Inflation	7.0%	6.5%	7.0%	6.5%	5.5%
Particulars	Actual 2020/21	Actual 2021/22	Actual 2022/23	Estimated 2023/24	Estimated 2024/25
Growth Rate	4.3%	4.5%	2.16%	3.5-4.5%	3.5-4.5%
Inflation	3.6%	7.3%	7.44	4.5-5.5%	4.1-5.1%

*The five primary priorities of the budget 2024/25*

*Economic reforms and private sector promotion*

*Development of agriculture, energy, information technology, tourism, industrial development, and infrastructure construction*

*Development of social sectors including education and health*

*Inclusiveness and social security*

*Promotion of good governance and improvement in public service delivery*

*The principles guiding the fiscal policy:*

*Ensuring fiscal discipline through prudent management of public finances, including revenue collection, expenditure control, and efficient utilization of domestic and foreign resources.*

*Broadening the tax base and strengthening tax administration and enforcement mechanisms to enhance revenue mobilization, promote equity, and ensure compliance.*

*Promoting investment-friendly policies and facilitating private sector participation in economic development through conducive regulatory frameworks and incentives.*

*Enhancing transparency and accountability in fiscal management through effective monitoring, evaluation, and public disclosure of financial information.*

*Pursuing a balanced and sustainable fiscal policy that supports economic growth, social development, and environmental sustainability.*

## *Key Goals:*

<i>Increase</i>	<i>Boost</i>	<i>Develop</i>	<i>Utilize</i>	<i>Service</i>
<i>Increase production, productivity, and employment.</i>	<i>Boost investor confidence to enhance investment and intensify economic activities.</i>	<i>Develop human resources.</i>	<i>Utilize resources and assets in a balanced and equitable manner to reduce economic inequality and poverty.</i>	<i>Make public service delivery more efficient.</i>

## Key highlights

### Electricity

*In the upcoming fiscal year, an additional capacity of 900 megawatts will be added, bringing the total capacity to 4,500 megawatts.*

### Agriculture

*The government has announced a ten-year investment plan in agriculture, starting from the fiscal year 2081 to 2091, with participation from private, cooperative, and public sector partners.*

### Financial Sector:

*The Nepal Rastra Bank Act and the Foreign Exchange Regulation Act will be amended. The institutional capacity of the Securities Board of Nepal and the Nepal Insurance Authority will be improved. Structural reforms will be made to Nepal Stock Exchange Limited and CDS and Clearing Limited. Legal and institutional arrangements will be made to operate a commodity exchange market. Companies with capital exceeding a specified amount will be required to be listed on the securities market.*

### Information technology

*In Nepal, a ten-year plan will be implemented to advance information technology. The plan aims to achieve significant progress by the end of the decade, with the establishment of 5 lakh new jobs in the information technology sector and the provision of training for 10 lakh individuals.*

### Tourism

*Attract 1.6 million tourists to Nepal.*

### Industries

*To increase domestic production, establish new ventures, and promote innovation and entrepreneurship, as well as to create employment opportunities through increased production and demand, partnerships between production and employment sectors will be implemented.*

**Non-Resident Nepali :** Non-Resident Nepali (NRN) campaign will be conducted to connect the capital, knowledge, and skills of non-resident Nepalis to their motherland. The campaign will also facilitate the utilization and investment opportunities of the **NRN Nepal Development Fund** established Jointly by GoN and non-resident Nepalis.

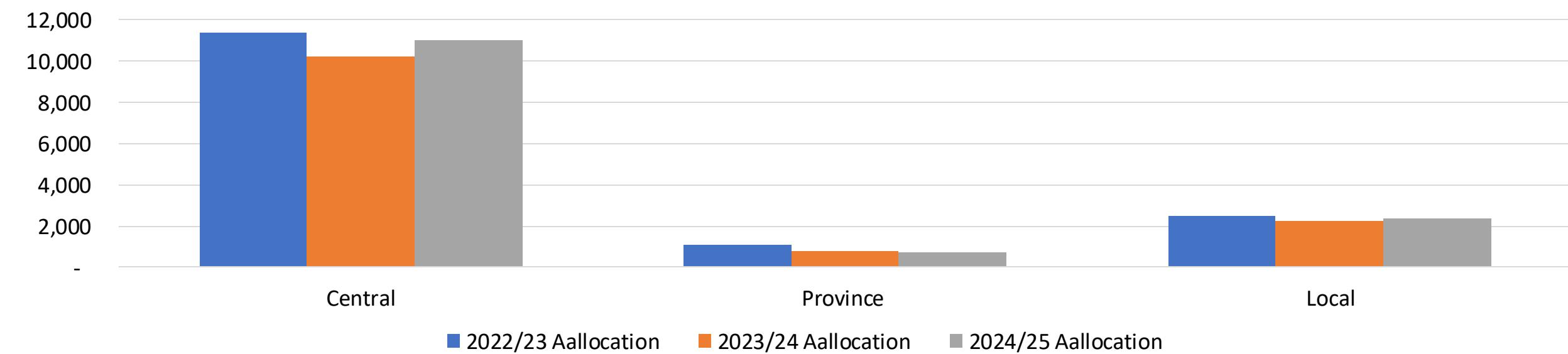
**Base year:** Shift the base year for National Accounting

# Budget Sources

	Exchange Factor 1 USD = NPR 120							Variance	1 USD= NRP 132				1 USD= NRP 132	
	Actual Budget Amount (\$ Million) 2020/21	Budget Amount (\$ Million) 2021/22	Revised Amount (\$ Million) 2021/22	Actual Amount (\$ Million) 2021/22	Budget Amount (\$ Million) 2022/23	Revised Amount (\$ Million) 2022/23	Change	Budget Amount (\$ Million) 2023/24	Revised Amount (\$ Million) 2023/24	Change	Budget Amount (\$ Million) 2024/25	Change	Change 2023/24 Revised and 2024/25 Budget	
Revenue Sources													Change 2023/24 Revised and 2024/25 Budget	
Tax Revenue	7,211.40	8,540.89	8,487.72	8,216.69	10,334.32	8,666.67	-16.14%	9,459.24	9.15%	8,449.20	-10.68%	9,547.75	13.00%	
Foreign Grant	304.01	528.14	206.74	229.07	462.15	320.49	-30.65%	378.36	18.06%	224.38	-40.70%	396.41	76.67%	
Deficit	3,307.90	4,660.78	3,368.19	3,027.74	4,152.18	3,554.50	-14.39%	3,429.92	-3.50%	2,920.03	-14.87%	4,149.04	42.09%	
Foreign Debt	1,441.24	2,577.44	1,440.65	1,089.11	2,018.84	1,421.16	-29.61%	1,611.74	13.41%	1,101.85	-31.64%	1,649.04	49.66%	
Domestic Debt	1,866.67	2,083.33	1,927.53	1,938.63	2,133.33	2,133.33	0.00%	1,818.18	-14.77%	1,818.18	0.00%	2,500.00	37.50%	
Total	10,823.32	13,729.80	12,062.64	11,473.50	14,948.64	12,541.65	-16.10%	13,267.52	5.79%	11,593.60	-12.62%	14,093.20	21.56%	

# Budget Allocations

	Exchange Factor 1 USD = NPR 120							1 USD= NRP 132				1 USD= NRP 132	
	Allocated Budget	Actual Budget Amount (\$ Million) 2020/21	Budget Amount (\$ Million) 2021/22	Actual Amount (\$ Million) 2021/22	Budget Amount (\$ Million) 2022/23	Revised Amount (\$ Million) 2022/23	Variance	Budget (\$ Million) 2023/24	Change	Revised Amount	Variance	Budget Amount (\$ Million) 2024/25	Change 2023/24 Revised and 2024/25 Budget
Current Expenditure	3,764.18	5,655.11	4,535.35	6,278.36	5,336.60	-15.00%	5,618.92	5.29%	5,194.73	-7.55%	5,543.85	6.72%	
Capital Expenditure	1,906.97	3,118.91	1,801.78	3,169.87	2,152.88	-32.08%	2,288.44	6.30%	1,631.11	-28.72%	2,669.35	63.65%	
Financial Provisioning	1,864.53	1,733.15	1,752.41	1,918.48	1,693.83	-11.71%	2,329.19	37.51%	1,875.40	-19.48%	2,782.46	48.37%	
Intergovernmental Fiscal Transfer	3,287.63	3,222.64	3,383.96	3,581.94	3,358.33	-6.24%	3,030.96	-9.75%	2,892.37	-4.57%	3,097.55	7.09%	
<b>Total</b>	<b>10,823.31</b>	<b>13,729.81</b>	<b>11,473.50</b>	<b>14,948.65</b>	<b>12,541.65</b>	<b>-16.10%</b>	<b>13,267.52</b>	<b>5.79%</b>	<b>11,593.60</b>	<b>-12.62%</b>	<b>14,093.20</b>	<b>21.56%</b>	



# Sectoral distribution 2024/25

Areas of Budget allocation	2021/22		2022/23		2023/24		2024/25		Compare to last year	
	Amount in \$ Mn	in % age	Amount in \$ Mn	in % age	Amount in \$ Mn	in % age	Amount in \$ Mn	in % age	In figure	In %
General Public Service	4,034	29.42%	4,779	31.97%	4,777	36.00%	7,067	50.15%	Up	Up
Defense	414	3.02%	462	3.09%	434	3.27%	442	3.13%	Up	Down
Public Order and Safety	484	3.53%	545	3.65%	539	4.07%	569	4.04%	Up	Down
Economic Affair	3,684	26.87%	3,890	26.02%	2,962	22.32%	2,903	20.60%	Down	Down
Environmental Protection	105	0.76%	92	0.61%	65	0.49%	64	0.46%	Down	Down
Housing and Community Amenities	671	4.89%	738	4.94%	500	3.77%	508	3.60%	Up	Down
Health	1,180	8.60%	1,027	6.87%	779	5.87%	434	3.08%	Down	Down
Recreation, Culture and Religion	56	0.41%	80	0.54%	50	0.38%	45	0.32%	Down	Down
Education	1,500	10.94%	1,641	10.98%	1,498	11.29%	440	3.12%	Down	Down
Social protection	1,582	11.54%	1,694	11.34%	1,663	12.53%	1,621	11.50%	Down	Down
Total	13,709	100%	14,949	100%	13,268	100%				
Exchnage Factor	USD 1 = NPR 120				USD 1 = NPR 132					

## Sectoral distribution

- The allocation for general public service and Economic affair constitute approximately 47.95% of the budget.
- Decrease in allocation allocation of budget for Health and Environmental protection by 44% and 1.3% respectively.
- Budget for Recreation, Culture and Religion has been decreased by 11.68%.

## Observations

- **Revenue Growth Target:** The global unrest and surge in commodity prices will likely impact government revenue receipts. Consequently, the revenue growth target of 13% appears challenging.
- **Foreign Loan Mobilization:** The mobilization of \$1,649 million in foreign loans seems ambitious. Aside from emergency financial assistance from multilateral agencies, the mobilization of other loans hinges on progress made on projects. Therefore, there is a need to ramp up the capital budget absorption capacity.
- **Domestic Borrowing:** The planned domestic borrowing of \$2,500 million, combined with increasing non-performing loans, may pressure Banks and Financial Institutions (BFIs). Consequently, BFIs might be less motivated to lend to the private sector.
- **Foreign Grant Mobilization:** The target of mobilizing \$396 million in foreign grants is higher than the amount received in recent years, which could be overly optimistic.
- **Provincial and Local Government Allocation:** \$3,098 million has been allocated to provincial and local governments, representing approximately 21.98% of the budget. This is 0.87% less than the previous year's allocation.
- **Sub-National Government Role:** The government aims to enhance the role of sub-national governments in national priority projects, which is crucial for balanced regional development.
- **Engagement of Non-Resident Nepalese:** The government aims to attract Non-Resident Nepalese to bring back their knowledge, skills, and capital, which could positively impact national development.



Given the current economic uncertainties and challenges, achieving these ambitious targets will require effective implementation and favorable economic conditions.

**Revenue:** The tax revenue for 2024/25 is projected to increase by 13% from the revised amount of 2023/24. This reflects an ambitious target, indicating optimism for higher economic activity and improved tax collection efficiency.

**Foreign grants** The substantial increase of 76.67% in foreign grants for 2024/25 suggests high expectations for increased international aid and donor support, contrasting sharply with the significantly reduced amount in 2023/24.

**Deficit:** The projected deficit increase of 42.09% for 2024/25 points to a highly ambitious budget with expanded spending plans, likely aimed at stimulating economic growth despite the slow recovery.

**Foreign debt:** The significant increase of 49.66% in foreign debt for 2024/25 indicates ambitious borrowing plans to finance the deficit and potentially fund major projects or initiatives.

The overall budget increase of 21.56% for 2024/25 compared to the revised budget of 2023/24 is a highly ambitious fiscal plan. The government appears to be banking on substantial economic recovery, improved revenue collection, and significant external and domestic borrowing.

The FY 2024/25 budget for Nepal is indeed ambitious. The government aims to significantly boost revenue from taxes and foreign grants while also planning for higher borrowing both domestically and internationally. This approach suggests a strong focus on economic recovery and growth despite the current slow growth and challenges in revenue collection. Achieving these ambitious targets will require effective implementation and potentially favorable economic conditions.

*Nepal requires an immediate economic rescue plan to revive its economy.*

*The plan should aim to restore fiscal balance, ensure financial stability, and control inflation.*

*Importance of Fiscal Balance*

*Fiscal balance is crucial for sustainable economic growth. It involves managing government revenues and expenditures to prevent budget deficits. Ensuring fiscal balance fosters investor confidence and supports long-term economic stability.*

*Ensuring Financial Stability*

*Financial stability is essential for a robust economy. It involves maintaining stability in the banking sector, preventing financial crises, and ensuring smooth credit flows. Upholding financial stability boosts investor trust and encourages economic investment.*

*Anchoring Inflation*

*Controlling inflation is vital for economic health. Excessive inflation erodes purchasing power and destabilizes the economy. Anchoring inflation to a reasonable limit supports price stability and fosters economic growth.*

*Components of the Emergency Economic Plan*

*Fiscal Measures: Implementing prudent fiscal policies to manage government finances and reduce budget deficits. Financial Sector Reforms: Strengthening regulatory frameworks and enhancing oversight to ensure stability in the banking sector. Monetary Policy Actions: Implementing measures to control inflation through appropriate monetary policy tools.*

*Immediate Action Steps*

*Assessing the current economic situation and identifying priority areas for intervention. Formulating and implementing policies swiftly to address fiscal imbalances, ensure financial stability, and control inflation. Collaboration between government agencies, financial institutions, and international partners to implement the plan effectively.*

*Benefits of the Plan*

*Stimulating economic growth and creating employment opportunities. Restoring investor confidence and attracting foreign investment. Enhancing the overall economic resilience of Nepal in the face of future challenges.*

*Conclusion*

*An emergency economic plan is essential for Nepal to overcome its economic challenges. By maintaining fiscal balance, financial stability, and controlling inflation, Nepal can jump-start its economy and pave the way for sustainable growth and development.*

June 2024



**The IMF Executive Board has completed the fourth review of the Extended Credit Facility (ECF) for Nepal, which allows the country to draw about US\$52.25 million. This brings total disbursements under the ECF arrangement to approximately US\$222.5 million. The ECF program, which began in January 2022, has helped Nepal mitigate the economic impacts of the COVID-19 pandemic and other global shocks, support vulnerable populations, and maintain macroeconomic stability. The report highlights several key points about Nepal's economic status:**

**Economic Performance:** Nepal experienced a significant economic slowdown after a post-pandemic rebound driven by a credit boom. Growth is expected to recover to 3.5% in the fiscal year 2023/24, supported by increased domestic demand, new hydroelectric capacity, and a recovery in tourism.

**Inflation and Fiscal Deficit:** Inflation, although declining, remains high at 8.2% as of September 2023. The country faces a widening fiscal deficit despite measures to control expenditures, largely due to low domestic demand affecting government revenue.

**Risks:** The outlook for Nepal's economy remains uncertain with risks skewed to the downside, particularly from external sectors due to high remittance income and dependence on imported goods. There are also concerns about the stability of the banking sector.

**The economic outlook for Nepal remains complex.** Economic activity is expected to pick up with growth reaching 4.9 percent in FY2024/25, supported by stronger domestic demand. The cautiously accommodative monetary policy stance. This growth is driven by increased domestic demand, new hydroelectric capacity, and a recovery in tourism.

**Bank asset quality has deteriorated**, with the increase in NPAs putting additional pressure on the banking sector. The Nepal Rastra Bank (NRB) has introduced measures to improve bank supervision and regulation, including new guidelines and asset classification regulations.

**Maintaining macroeconomic stability**, advancing fiscal reforms, and addressing financial sector vulnerabilities are critical for Nepal's sustainable growth. The IMF emphasizes the need for prudent fiscal and monetary policies to manage risks and support economic recovery. monetary policy transmission is still weak in a context of balance sheet repair, a cautious and data dependent monetary policy remains appropriate to preserve price and external stability.

**The IMF has stressed** the importance of continuing reforms in areas such as fiscal discipline, banking regulation, governance, and improving the business climate to ensure sustainable economic growth and stability.

## GON defaults on its contractual obligations

If the Government of Nepal (GoN) continue to default on its contractual obligations by not paying contractors' running bills, interest subsidies on agricultural loans, and COVID-19 insurance, it can have several significant consequences, even though Nepal does not currently have a sovereign rating from any rating agency. Here are the potential consequences:

### • **Erosion of Trust and Credibility**

- **Domestic and International Trust:** Defaulting on obligations erodes the trust of both domestic and international stakeholders, including contractors, financial institutions, and potential investors. This loss of trust can make future engagements and negotiations more difficult and expensive.

- **Reputation:** The country's reputation for financial management and reliability would suffer, potentially deterring foreign investment and aid.

### • **Impact on Contractors and Businesses**

- **Financial Strain:** Contractors and businesses relying on timely payments from the government may face financial strain, leading to potential layoffs, bankruptcies, or project delays.

- **Project Delays:** Essential infrastructure and development projects might be delayed or halted, impacting economic growth and public services.

### • **Banking Sector Instability**

- **Loan Defaults:** If the government fails to provide interest subsidies on agricultural loans, farmers and other beneficiaries might default on their loans, leading to increased non-performing assets (NPAs) in the banking sector.

- **Credit Crunch:** Banks might become more cautious in lending, leading to a credit crunch that can stifle economic growth.

### • **Insurance Sector Impact**

- **Policyholder Confidence:** Not honoring COVID-19 insurance claims can undermine confidence in the insurance sector, causing policyholders to lose trust in the system.

- **Increased Risk Premiums:** Insurers might increase premiums or reduce coverage to mitigate risks associated with government defaults.

### • **Economic Slowdown**

- **Reduced Spending and Investment:** Uncertainty and lack of trust in the government's financial commitments can lead to reduced spending and investment by both the private sector and consumers.

- **Growth Inhibition:** An economic slowdown can result from decreased activity in key sectors affected by the defaults.

## Consequences continued

### Potential for Lower Future Ratings

**Negative Outlook:** Even without a current sovereign rating, these defaults could influence future ratings if Nepal seeks them. Rating agencies would consider these defaults as indicators of poor financial management and increased risk.

**Higher Borrowing Costs:** A lower rating or negative outlook can lead to higher borrowing costs for the government and businesses, as lenders would demand higher interest rates to compensate for perceived risks.

### Political and Social Consequences

**Public Dissatisfaction:** Unmet financial commitments can lead to public dissatisfaction and unrest, potentially destabilizing the political environment.

**Policy Reevaluation:** The government may need to reevaluate its fiscal policies and spending priorities, possibly leading to austerity measures or budget cuts in other areas.

### Conclusion

The consequences of the GoN defaulting on its contractual obligations are far-reaching, impacting various sectors of the economy and society. The erosion of trust and credibility, financial strain on businesses, banking sector instability, and potential future impacts on sovereign ratings are all critical issues that need to be addressed to maintain economic stability and growth.

## 2024 “Optimistic outlook while exercising prudence”

*There is a sign that Nepal may have political stability and a strong government, as a 7-point agreement between the two largest parties has brought some hope. It seems the Government of Nepal (GoN) will put its effort and strength into economic development and is likely to initiate more economic reforms. However, we are cautiously optimistic.*

*Despite some proactive measures taken by the central bank to address financial stability risks, the effectiveness of these actions remains questionable. The Nepal Rastra Bank (NRB) recognizes the complex interplay between monetary policy and financial stability, but whether their strategies will prevent undue strain on the financial system is uncertain. This situation reveals the NRB's ongoing struggle to maintain a stable and secure financial environment.*

*The proposed amendment to the Bank and Financial Institutions Act (BAFIA) has sparked significant concerns within the business community. This review highlights key issues and implications, particularly focusing on Sections 2 and 52 of the proposed Act, which impose restrictions on shareholders owning more than 1% of a bank's shares from borrowing money from any bank in Nepal.*

*Section 52 extends this restriction, specifying that shareholders and their relatives cannot engage in business transactions with any other bank if they hold shares exceeding the 1% threshold in any bank. This rule could negatively impact investment, as shareholders with substantial stakes in banks often have a vested interest in the success of these institutions. By limiting their ability to borrow from any other bank in Nepal, the amendment might discourage potential investors who seek both equity in one bank and credit facilities from another bank where they have not invested.*

*Although the stringent rule aims to enhance governance and transparency within financial institutions, it could lead to unintended consequences. Shareholders may be forced to disinvest their ownership in banks, creating an oversupply and potentially causing a crash in the capital market. Additionally, banks might lose valuable business relationships and opportunities from reputable clients. The blanket restriction fails to consider the individual creditworthiness and business acumen of shareholders, potentially penalizing competent investors who could contribute positively to the banking sector.*

*Overall, while there is some momentum heading into 2024, a more cautious and realistic outlook is warranted. Instead of an overly optimistic view, it is imperative to remain vigilant and prudent in managing the economic challenges ahead.*

## 2024 "Persistent Stagnation in Bank Credit Growth Despite Lower Lending Rates"

Economic activity in Nepal has been sluggish, despite some positive developments. May 2024 saw only a slight improvement in consumer spending, primarily due to increased remittances and lower borrowing costs. However, the manufacturing sector, crucial to industrial activity, has not experienced significant advancements on the supply side.



Migration and urbanization have led to a decline in rural demand, which is expected to remain below the levels seen in the 2023/24 fiscal year. During the current fiscal year, the weighted average lending rates have **decreased by 2.07%**. As a result, there has been a modest increase in urban demand for domestic capital goods, as indicated by various economic indicators.

Despite the low lending rates, credit demand has remained subdued, with bank credit growth remaining stagnant. This is attributed to the elevated concentration of government securities and excess liquidity held by financial institutions. As a result, banks have persisted in adjusting their lending and deposit rates downwards to accommodate the lack of significant demand for credit. This ongoing trend has resulted in notable decreases in the weighted average lending and deposit rates.



Consumer confidence for this year has reached a record low, and construction activity has also been lackluster. Investment outlook remains bleak due to various factors, including subdued demand for credit from corporate, especially those in manufacturing; sustained low government capital expenditure; weakened balance sheets of both banks and corporates; diminished capacity utilization; and declining business sentiment.



July 2024



# *Monetary policy transmission*

*1. Interest Rate Channel*

*Less Effective*

*2. Lending Rates Channel*

*Not Effective*

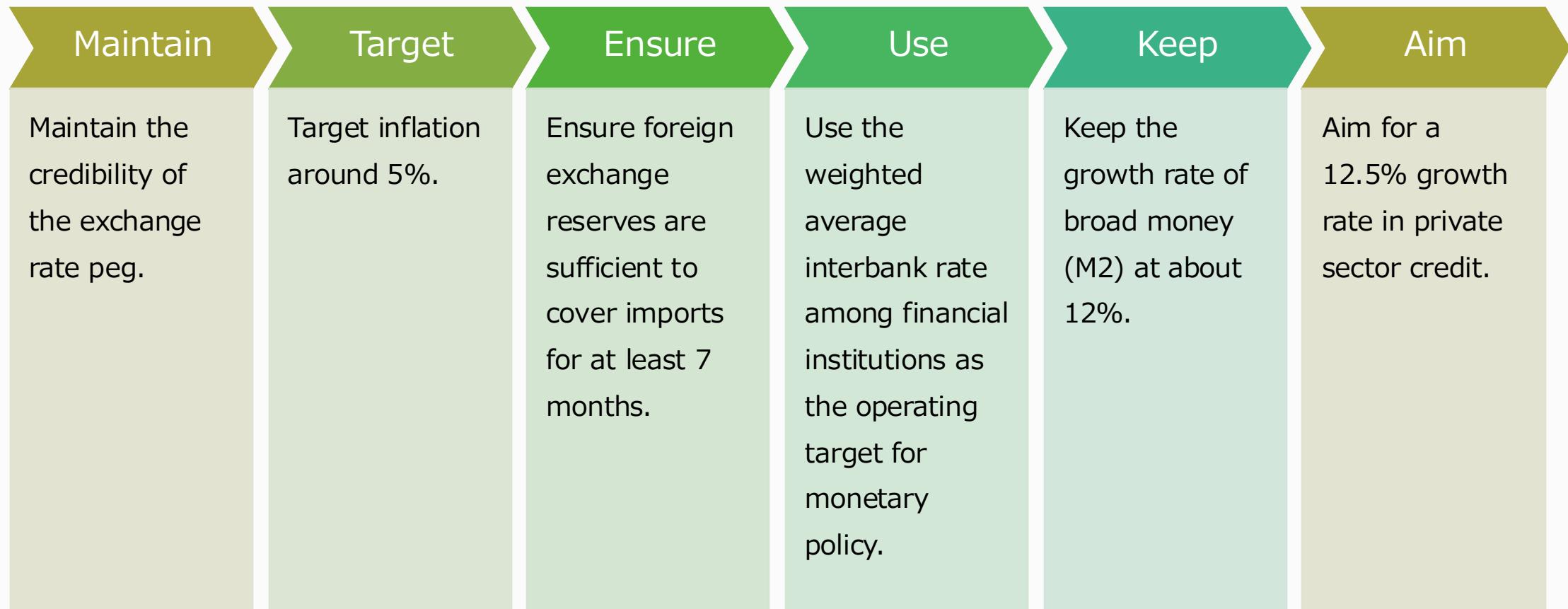
*3. Asset Price Channel*

*Not Effective*

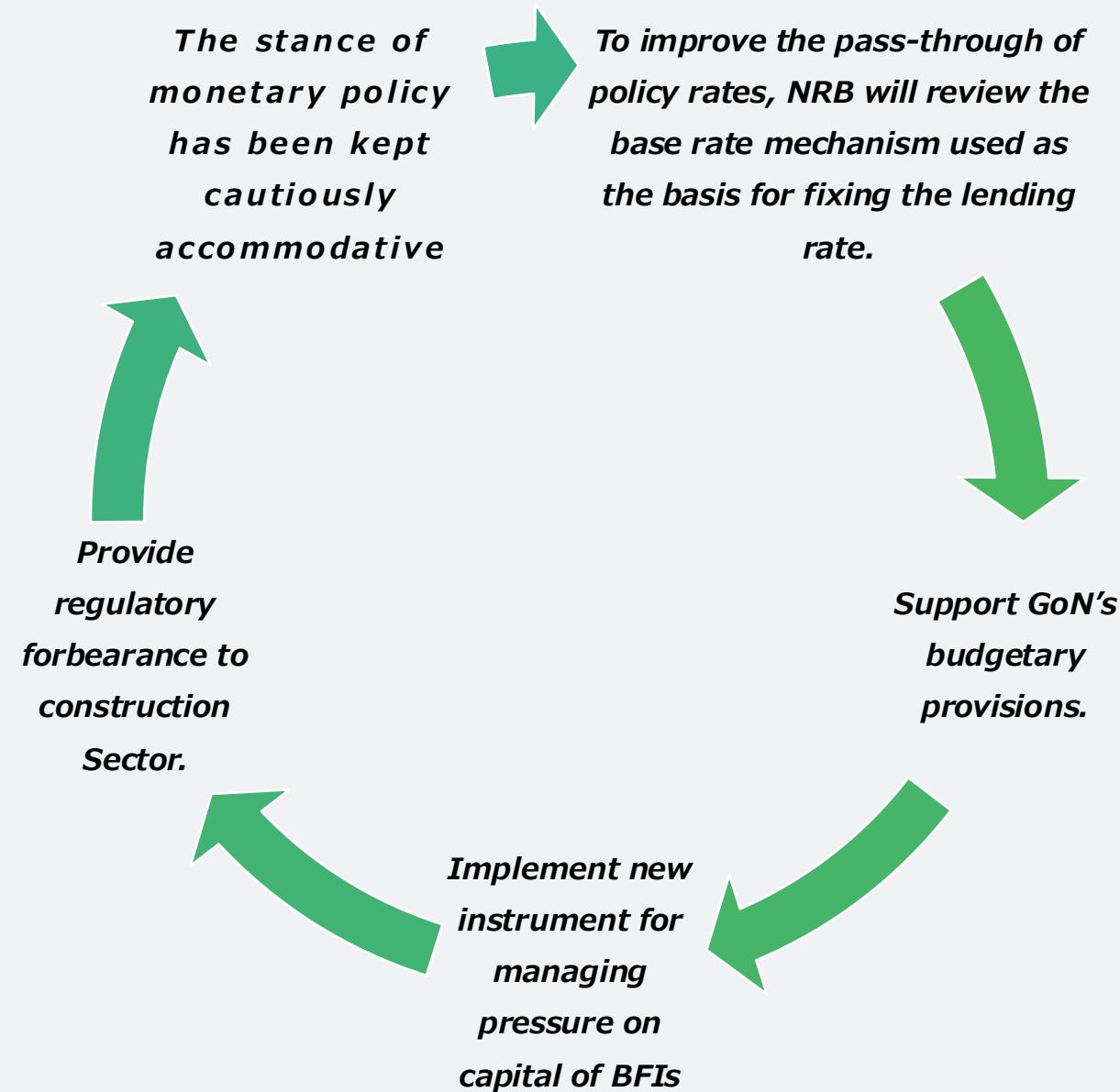
*4. Exchange Rate Channel*

*Not Effective*

# Policy Stance



## *The NRB acknowledged economic slowdown since last two years*



Policy  
Stance and  
Objectives

*The NRB has maintained a cautiously accommodative monetary policy stance, emphasizing the need to support economic recovery while managing inflation and ensuring financial stability. The central bank targets inflation around 5% and aims to maintain foreign exchange reserves sufficient to cover imports for at least seven months. The weighted average interbank rate among financial institutions is used as the operating target for monetary policy, with a growth rate of broad money (M2) kept at about 12% and a private sector credit growth target of 12.5%.*

Monetary  
Policy  
Transmission  
Channels

*Interest Rate Channel: (Less effective) The transmission of monetary policy through interest rates has been less effective. The review highlights that while the impact on the short-term money market is immediate, the medium-term money market shows less responsiveness. Despite reductions in policy rates and the interest rate corridor's higher limit, the broader transmission to the credit market remains weak.*

*Lending Rates Channel: (Not effective) The effectiveness of monetary policy transmission through lending rates is limited. The readiness and health of the banking system significantly affect this channel. Issues within banks or their unwillingness to lend result in ineffective rate cuts, which fail to stimulate demand as intended.*

*Asset Price Channel: (Not effective) This channel is also noted to be ineffective. Despite lower interest rates, there has not been a significant increase in asset prices, such as real estate, due to subdued lending growth and low market confidence.*

*Exchange Rate Channel: (Not effective) The exchange rate channel has not been effective either. Lower domestic investment returns due to interest rate cuts have not led to substantial foreign capital inflows, impacting the domestic currency and trade balance.*

Policy  
Responses  
and  
Measures

*Capital Adequacy: The NRB plans to review the capital adequacy framework and introduce new instruments to alleviate pressure on core capital. It also aims to allow regulatory reserves to be included in Tier 2 Capital up to 100% of Tier 1 Capital.*

*Foreign Exchange: The policy includes measures to simplify foreign exchange processes, maintain the exchange rate peg with the Indian currency, and expand the list of available foreign currencies. Additionally, the spending limit from domestic foreign exchange accounts has been raised.*

*Asset Management and Transparency: The NRB intends to establish an asset management company and integrate tax office submissions with the banking system to improve transparency. Provisions related to asset quality grading and working guidelines have been relaxed to support financial stability.*

## Prosperity

*Wealthy nations are prosperous today because they have experienced steady growth over a long period, not necessarily because they grew particularly fast. One of the most noticeable differences when traveling from a rich country to a poor one is the stark contrast in levels of physical capital.*

## Physical capital

*In wealthy nations, vast airports accommodating large planes, enormous factories filled with high-tech machinery, expansive farms with advanced irrigation systems and massive combines, top-tier education and healthcare systems, well-managed public transportation, and households equipped with appliances and gadgets for every imaginable purpose all suggest a significantly higher use of physical capital compared to poorer countries. Physical capital boosts income by making workers more productive—a single construction worker with a backhoe, for example, can move far more earth than several workers with shovels and wheelbarrows.*

## The real challenge

*The real challenge in our country is that we are still in the early stages of growth and lack the organizational structure needed to deploy large quantities of physical capital effectively. Our government, in general, lacks the capacity to intervene and create a nurturing environment for growth, even if the intention is there. Unfortunately, the government remains heavily reliant on import duties for its revenue. Government policies, domestic vested interests, and household habits formed during the years of catch-up growth continue to keep us dependent. To progress, we need to industrialize our country and harness our available natural resources. However, tapping into these resources requires significant capital, far more than our local resources can provide. Clearly, much more is needed*

# 2024/25 “Optimistic outlook while exercising prudence”

*We can't console ourselves by saying, "there is no crisis"!*

*The biggest challenge faced by the Nepalese economy isn't its fundamentals, which are relatively strong in the short term. The real challenge is the threat to business and the loss of private sector confidence due to rising extremism, red tape, outdated laws, bureaucratic hurdles, complex regulations, declining governance, and rent-seeking behavior. These negative developments deter investors and consumers.*

*Nepalese planners need to identify the causes that could push the economy into a negative trajectory and find ways to alleviate these conditions.*

*Much more needs to be done to accelerate economic growth by creating jobs, encouraging both local and foreign investment, seeking foreign aid, utilizing natural resources, increasing productivity, and reducing the trade deficit.*

*We must understand that the most successful free market environments are those where the government enables but does not attempt to control the economy.*

*We risk emphasizing short-term growth at the expense of addressing medium to long-term challenges. We can't wait for a crisis to act. We must act now. But are we preparing enough?*

August 2024

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# IMF Review: September 2024

*Nepal's economy is showing signs of recovery, with import growth improving, stronger tax collections, and rising public investment. Inflation has dropped to 3.6%, supported by favorable commodity prices and subdued demand. International reserves are increasing due to remittances and a rebound in tourism. Key reforms in public investment, banking regulation, and cooperative oversight are critical. Governance enhancements, including amendments to the Anti-Money Laundering Act and improvements in public enterprise transparency, will support sustained growth.*

*Accelerating the reform momentum is critical to put the economy on a path towards sustainable, strong, and inclusive economic growth. This will require enhancing public investment execution, further strengthening of domestic revenue mobilization, and prompt disbursement of Child Grants.*

*As banks deal with elevated non-performing loans and capital constraints, continued vigilance is necessary, including by continuing to strengthen regulation and completing the loan portfolio review of the largest 10 banks. Addressing vulnerabilities among the savings and credit cooperatives remains a priority. The recent amendments to the Anti-Money Laundering Act are a welcome step.*

*Amending the Nepal Rastra Bank (NRB) Act, completion of NRB's external audit and increasing public enterprise's transparency will enhance governance and accountability. The Investment Facilitation Act will bolster Nepal's investment climate. The IMF-supported program's progress will be reviewed formally in its fifth evaluation.*

# 2024/25 “Optimistic outlook while exercising prudence”

*The biggest challenge facing the Nepalese economy is not its short-term fundamentals, which remain relatively stable, but the growing threat to business and the erosion of private sector confidence. This decline is being fueled by rising extremism, excessive bureaucracy, outdated laws, regulatory complexities, weakening governance, and rampant rent-seeking behavior. These negative forces are discouraging both investors and consumers. Nepal's policymakers must identify the root causes that could push the economy toward stagnation and take decisive action to address them.*

*Much more needs to be done to accelerate economic growth. This includes creating jobs, attracting both local and foreign investment, securing foreign aid, leveraging natural resources, boosting productivity, and reducing the trade deficit.*

*Domestically, key drivers such as private consumption and gross fixed investment have shown little sequential improvement, likely offering limited support to GDP growth in Q1 of 2024-25. Gains in energy sector were offset by sluggish manufacturing and a weakening services sector. Household consumption remains low and is unlikely to improve in Q2, despite easing headline inflation, due to slowing rural demand. Although CPI inflation came in below the target, food price volatility remains a contingent risk based on recent trends.*

*While the Government of Nepal has set an ambitious growth target of 6% for this fiscal year, several challenges—such as reduced government capital expenditure, declining corporate profitability, lower core output, and weak demand—may cause actual growth to fall below 4%.*

Forecasts for Nepal's GDP growth by major institutions reveal significant variations and frequent revisions, illustrating the complexity of predicting the country's economic trajectory.

The World Bank projects a steady recovery, with growth forecasted at 3.9% for FY 2023/24, improving to 5.3% by FY 2025/26. However, even within their estimates, there was a 2.2% downward revision between April and October 2023, reflecting a re-evaluation of global and domestic factors. Similarly, the IMF slashed its FY 2022/23 growth forecast by 3.6% in October 2023, before improving the outlook to 3.9% for FY 2023/24 and 4.9% for FY 2024/25, indicating a highly reactive stance to changing circumstances. The ADB also revised its forecast multiple times, cutting its FY 2022/23 projection by 2.1% and further increasing its FY 2023/24 growth estimate from 3.0% to 3.6%, slightly adjusting it upwards again in later revisions. Meanwhile, CBS—the national statistics agency—has consistently set moderate projections, estimating 2.16% for FY 2022/23 and 3.0% for FY 2023/24.

These frequent revisions and variations make it extremely challenging for the Nepalese government and the Nepal Rastra Bank (NRB) to craft effective economic policies. The NRB, in particular, has consistently refrained from offering GDP growth forecasts, possibly due to the volatile nature of such estimates and their potential to mislead. However, the Government of Nepal (GoN) tends to maintain ambitious growth targets, which often diverge from the more conservative projections made by international agencies. This disconnect between optimistic government targets and more cautious external forecasts complicates policy interventions, especially when managing inflation, interest rates, and public investment strategies.

The disparity between forecasts highlights the uncertainty in Nepal's economic outlook and emphasizes the difficulty of making informed decisions in such a volatile environment. For policymakers, relying on a single projection source can lead to misguided policies, and the constant adjustments force the government to adapt frequently, making long-term planning difficult. As a result, there is a critical need for the GoN and NRB to base their strategies on a range of forecasts while remaining flexible to unexpected shifts in economic conditions.

# September 2024

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# 2024/25 “Optimistic outlook while exercising prudence”

*The biggest challenge for Nepal’s economy is not its short-term fundamentals, which remain relatively stable, but the increasing risks to businesses and the decline in private sector confidence. Unpredictable weather patterns and flash floods have significantly disrupted the economy, impacting key sectors such as agriculture, transport, energy, and services.*

*The economic and infrastructural damage requires immediate attention. The Nepal Rastra Bank (NRB) and the Ministry of Finance (MOF) must collaborate to design effective recovery strategies, including regulatory reforms and fiscal stimulus, to support the affected sectors and build resilience.*

*To accelerate economic growth, much more effort is needed. Priority areas include job creation, attracting local and foreign investments, securing foreign aid, leveraging natural resources, boosting productivity, and reducing the trade deficit.*

*Domestically, key economic drivers such as private consumption and gross fixed investment have shown minimal improvement, providing limited support to GDP growth in the first quarter of 2024-25. Although there have been gains in the energy sector, they were wiped out by the loss of hydropower projects, both operational and under construction, due to flooding. Sluggish performance in manufacturing and a weakening services sector continue to restrain overall growth. Household consumption remains low, and despite easing headline inflation, it is unlikely to recover in the second quarter due to slowing rural demand. While Consumer Price Index (CPI) inflation is below the target, food price volatility remains a risk based on recent trends.*

*The Government of Nepal has set a growth target of 6% for this fiscal year. However, multiple challenges—including reduced government capital expenditure, declining corporate profitability, lower core output, and weak demand—may result in growth falling below 4%.*

## Credit Growth

Nepal's current macroeconomic situation presents a mix of opportunities and challenges. Credit growth in the private sector has remained modest, increasing by only 1.4% over two months and 6.6% on a year-on-year basis, despite significant reductions in interest rates, with average lending rates for commercial banks dropping from 12.23% to 9.52%. This slow growth in credit uptake could indicate weak demand from the private sector, likely due to ongoing economic uncertainties or sluggish recovery in key sectors like manufacturing, real estate, and construction. Banks may also be exercising caution in lending, possibly driven by concerns over rising non-performing assets and the broader economic environment.

## Regulatory easing

To address this, the government and the central bank should consider targeted fiscal policies to boost demand in these sectors, potentially through public-private partnership initiatives, infrastructure development projects, or incentives for small and medium-sized enterprises (SMEs). Additionally, regulatory easing for banks in terms of credit provisioning could stimulate lending activities.

## Strong external position

The accumulation of foreign exchange reserves, which now stand at USD 16 billion, is enough to cover 16.8 months of imports, suggesting a strong external position. However, this also points to subdued import demand, likely due to weak economic activity and limited domestic investment opportunities. Excessive reserves without corresponding domestic economic expansion may reflect inefficiencies, such as underutilized capital. To address this, Nepal could explore measures to boost domestic investment, such as easing restrictions on foreign direct investment (FDI), providing tax incentives for export-oriented industries, and improving infrastructure to attract more investments.

## Potential deflation

On the inflation front, year-on-year consumer price inflation has slowed to 3.85%, down from 8.19% a year ago. This significant decline, particularly in non-food inflation, indicates weakened demand-side pressures and raises concerns about potential deflation. Prolonged deflation could stifle investment and consumer spending, leading to slower economic growth. To combat this, Nepal should consider expansionary fiscal and monetary policies to boost consumer confidence and spending. Increasing government capital expenditure in infrastructure, healthcare, and education could stimulate job creation and demand.

## Economic growth

Overall, while the current economic conditions reflect positive aspects like strong foreign reserves and reduced inflation, the underlying issues of weak credit growth, underutilized investment potential, and risks of deflation must be addressed. Corrective actions should focus on stimulating private sector investment, enhancing fiscal spending, and adopting policies that boost domestic consumption and job creation, ensuring that economic growth is both sustainable and inclusive.

## 1. Challenges

Nepal faces considerable growth challenges, with both longstanding and new issues affecting its economic future. The underwhelming performance in fiscal year 2023-24 can largely be attributed to political instability and weak economic diplomacy. Despite these setbacks, there are positive signs. Recent data shows remittance inflows have exceeded expectations, providing some stability to the balance of payments. Additionally, Nepal has recorded a surplus in foreign exchange reserves, which offers a hopeful indicator amidst broader concerns.

## 2. Termites

Nevertheless, underlying challenges persist. Like silent termites weakening a structure over time, some economic risks may not be immediately obvious but can cause significant long-term damage. The economy faces several key issues, including falling corporate earnings, weak government revenues, low capital expenditure, and sluggish market demand. Even though inflation appears to have stabilized, many citizens are still burdened by the rising cost of living. Other long-standing issues such as political unrest, strained relationships with neighboring countries, slow growth, high trade deficits, poor investment environments, and currency volatility continue to prevent efficient resource utilization.

## 3. Imports vs Exports

Nepal's heavy reliance on imports, even for basic goods, is a significant vulnerability. With increased remittance inflows, consumer habits have shifted towards imported products, making Nepal an attractive market for foreign brands. This dependency drains foreign exchange reserves and exacerbates the trade imbalance. Although remittances provide a temporary financial buffer, they cannot fully compensate for the country's insufficient exports. Nepal is also missing out on the potential benefits of boosting local production. Developing domestic industries could create jobs, raise incomes, and reduce reliance on costly imports. Locally produced goods would also be cheaper, but this opportunity remains largely untapped.

## 4. Hope Over Fear

Nepal continues to face familiar economic challenges, such as currency depreciation, inflation, and sluggish growth. However, embracing a pro-market strategy that focuses on openness and efficiency could unlock multiple benefits, even with the current level of investment. These include:

1. Higher economic growth driven by increased productivity.
2. Labor-intensive industrialization, resulting in rapid job creation.
3. Greater competition, encouraging market entrants and improving rural economies.
4. Capital investment flowing into underserved regions, reducing regional and social inequalities over time.

# *Strategic Measures for Economic Recovery and Stimulus Initiatives in Nepal*

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*There is hope that Nepal will embrace a comprehensive strategy for economic recovery built on nine pivotal measures aimed at addressing both immediate and long-term challenges. This begins with establishing **Foundational Concepts for Inclusive Revival**, ensuring that growth benefits all sectors of society. **Sectoral Adaptation** will address specific challenges in agriculture, retail, and manufacturing, while the nation embraces the “**New Economy**” by focusing on digital technology and services.*

*Nepal is poised to **Enhance Competitiveness** by aligning with global standards and adopting **Global Best Practices** from successful policies around the world. Engaging key stakeholders—businesses, employees, and government—will ensure inclusive and collaborative economic planning.*

*The strategy also includes **Tailored Initiatives** to target key sectors like hospitality and technology, while addressing productivity concerns. To drive informed decision-making, Nepal will need to prioritize **Data Enhancement**, improving data systems and metrics. Finally, adopting a **Performance Framework** will help monitor progress, ensuring that economic achievements are transparent, measurable, and continuously improving.*

*With the right commitment, Nepal can pave the way for sustainable and inclusive economic growth.*

## *Documentation:*

*Exporting from Nepal or attracting foreign direct investment (FDI) currently takes 4 times longer, with 3 times more documents and 7 times more signatures than in developed countries. This inefficiency hinders our trade potential and economic growth.*



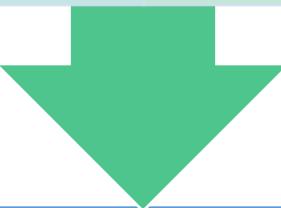
*To boost trade and investment, Nepal urgently needs:*

*Streamlined customs processes*

*Upgraded FDI regulations*

*Implementation of digital systems*

*Enhanced coordination among government agencies*



*By simplifying these procedures, we can make Nepal a more competitive destination for trade and investment, driving economic progress. It's time to rethink and reform for growth!*



*Business Ready's analytical framework goes beyond simply evaluating the "ease of doing business" by recognizing that fostering a healthy business environment involves more than just reducing business costs. Lowering these costs can sometimes lead to unintended societal consequences. Therefore, Business Ready not only assesses the regulatory burden on businesses—such as how long it takes to establish one—but also examines the quality of regulations. For instance, do labor laws protect employees from unjust dismissal? Or do they unintentionally make female workers less competitive than their male counterparts, thus discouraging their participation in the workforce?*



*In addition to evaluating regulations, Business Ready explores the role of public services in turning business intentions into outcomes. This includes assessing whether utilities such as water and electricity are reliably provided to businesses. It also looks at whether governments simplify compliance with tax obligations and environmental and social regulations. Furthermore, it evaluates whether systems are in place for government agencies to efficiently share business-related information and whether public databases exist to promote transparency and the free flow of information necessary for a robust business climate.*

**Based on the World Bank's Business Ready 2024 report, Nepal's performance in Operational Efficiency stands out, scoring 72.21 points.** Nepal's strong performance in Operational Efficiency reflects its efforts to streamline business processes, making it easier for firms to comply with regulatory demands. This is especially important in reducing administrative burdens for businesses. Despite the country's challenges in areas like public services, the high score in this pillar suggests that Nepal is creating conditions where businesses can navigate operational tasks more smoothly compared to peers. This environment helps firms maintain productivity and resilience, contributing to overall business readiness in Nepal.

*The findings are based on selected data points and could be subject to debate, as different perspectives may arise about how accurately the sample represents Nepal's overall business environment. Nonetheless, the report provides a valuable starting point for understanding the country's progress.*

# Growth Projections

## World Bank

1.Jan 2024.	3.90%. (Improved for FY 2023/24)
➤April 2024	3.3%. (0.6% down from Jan 2024 for 2023/24)
2.April 2024	4.6%. FY 2024/25 Fresh projections
➤Oct. 2024	5.1% (0.5% Improved from April 24 for 2024/25)
3.April 2024	5.3 % FY 2025/26 Fresh projections
➤Oct 2024	5.5 %. (0.2% Improved from April 24 for FY 2025/26)

## ADB

1.Sept 2024.	2.00 2.10 % down form April 23 (FY 2022/23)
2.April 2024.	3.6% - FY 2023/24 Fresh projections
➤Sept. 2024.	3.90. 0.60% up from previous for FY 2023/24
3.April 2024.	4.8% - FY 2024/25 Fresh projections
➤Sept 2024.	4.9% 0.1- up from April 2024 for 2024/25

## IMF

1.Oct 2023.	0.80 % 4.3 % down from Jan 2023 (FY 22/23)
2.Dec 2023.	3.5 % Forecast for 2023/24
➤May 2024.	3.9%. (0.4%Improved from Dec. 2023 for 2023/24)
3.May 2024	4.9% FY 2024/25 Fresh projections

## CBS

• April 2023	2.16% 2022/23
• April 2024	3% FY 2023/24

The wide variation in forecasts and the frequent revisions from these institutions indicate significant economic uncertainty in Nepal, particularly for FY 2023/24.

However, projections become more optimistic in the medium term for FY 2024/25 and beyond.

The World Bank seems to anticipate a faster recovery, while the ADB and IMF offer more conservative short-term outlooks, though they, too, foresee stronger growth in the years ahead.

These contrasting forecasts reflect the complexity and unpredictability of Nepal's macroeconomic environment, which is influenced by both domestic and international factors.

Forecasts for Nepal's GDP growth by major institutions reveal significant variations and frequent revisions, illustrating the complexity of predicting the country's economic trajectory.

*The World Bank projects a steady recovery, with growth forecasted at 3.9% for FY 2023/24, improving to 5.3% by FY 2025/26. However, even within their estimates, there was a 2.2% downward revision between April and October 2023, reflecting a re-evaluation of global and domestic factors. Similarly, the IMF slashed its FY 2022/23 growth forecast by 3.6% in October 2023, before improving the outlook to 3.9% for FY 2023/24 and 4.9% for FY 2024/25, indicating a highly reactive stance to changing circumstances. The ADB also revised its forecast multiple times, cutting its FY 2022/23 projection by 2.1% and further increasing its FY 2023/24 growth estimate from 3.0% to 3.6%, slightly adjusting it upwards again in later revisions. Meanwhile, CBS—the national statistics agency—has consistently set moderate projections, estimating 2.16% for FY 2022/23 and 3.0% for FY 2023/24.*

*These frequent revisions and variations make it extremely challenging for the Nepalese government and the Nepal Rastra Bank (NRB) to craft effective economic policies. The NRB, in particular, has consistently refrained from offering GDP growth forecasts, possibly due to the volatile nature of such estimates and their potential to mislead. However, the Government of Nepal (GoN) tends to maintain ambitious growth targets, which often diverge from the more conservative projections made by international agencies. This disconnect between optimistic government targets and more cautious external forecasts complicates policy interventions, especially when managing inflation, interest rates, and public investment strategies.*

*The disparity between forecasts highlights the uncertainty in Nepal's economic outlook and emphasizes the difficulty of making informed decisions in such a volatile environment. For policymakers, relying on a single projection source can lead to misguided policies, and the constant adjustments force the government to adapt frequently, making long-term planning difficult. As a result, there is a critical need for the GoN and NRB to base their strategies on a range of forecasts while remaining flexible to unexpected shifts in economic conditions.*

## 2024 "Persistent Stagnation in Bank Credit Growth Despite Lower Lending Rates"

Economic activity in Nepal has been sluggish, despite some positive developments. May 2024 saw only a slight improvement in consumer spending, primarily due to increased remittances and lower borrowing costs. However, the manufacturing sector, crucial to industrial activity, has not experienced significant advancements on the supply side.

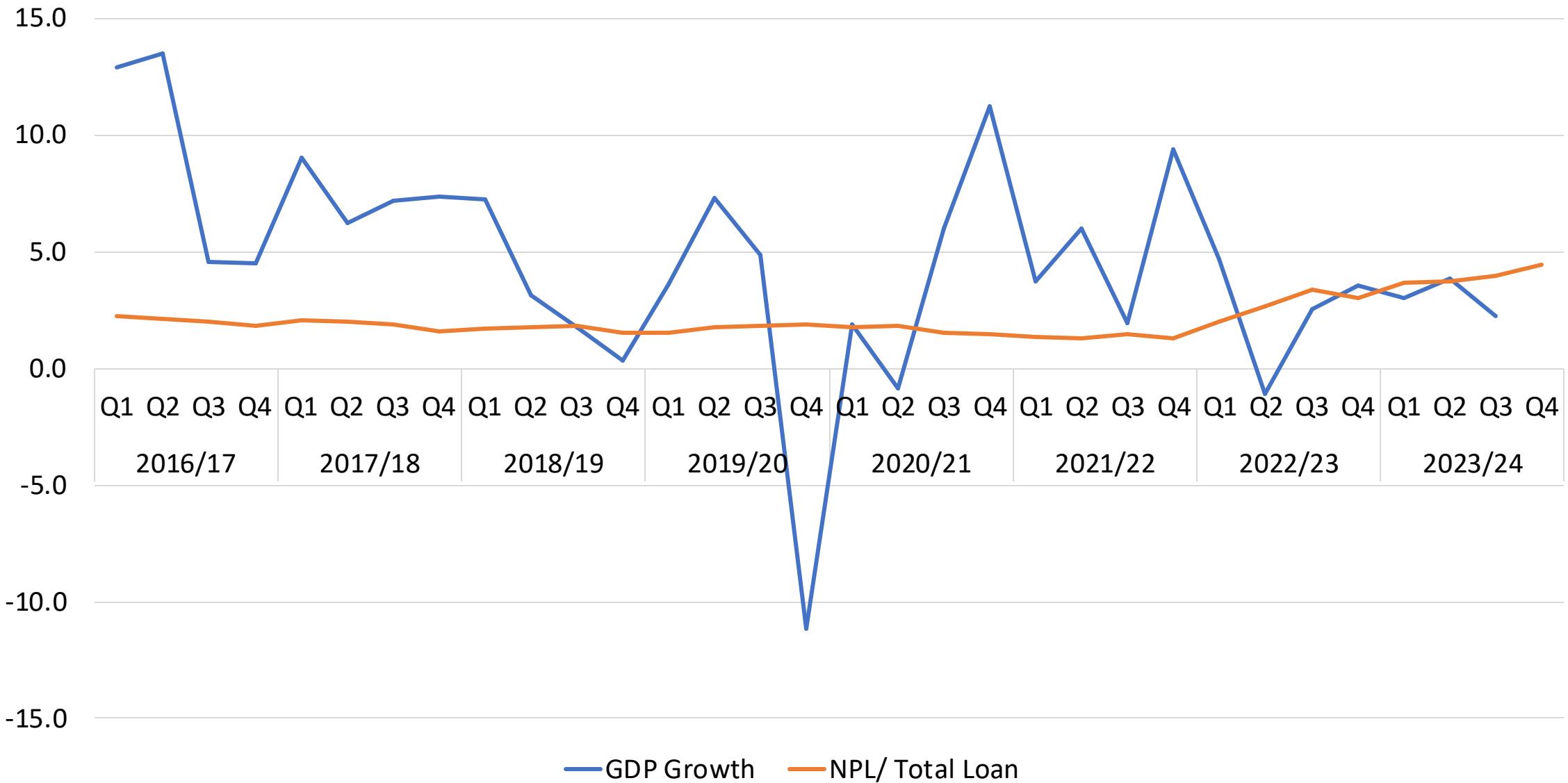


Migration and urbanization have led to a decline in rural demand, which is expected to remain below the levels seen in the 2023/24 fiscal year. During the current fiscal year, the weighted average lending rates have **decreased by 2.72%**. As a result, there has been a modest increase in urban demand for domestic capital goods, as indicated by various economic indicators.

Despite the low lending rates, credit demand has remained subdued, with bank credit growth remaining stagnant. This is attributed to the elevated concentration of government securities and excess liquidity held by financial institutions. As a result, banks have persisted in adjusting their lending and deposit rates downwards to accommodate the lack of significant demand for credit. This ongoing trend has resulted in notable decreases in the weighted average lending and deposit rates.



Consumer confidence for this year has reached a record low, and construction activity has also been lackluster. Investment outlook remains bleak due to various factors, including subdued demand for credit from corporate, especially those in manufacturing; sustained low government capital expenditure; weakened balance sheets of both banks and corporates; diminished capacity utilization; and declining business sentiment.



# October 2024

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*Fitch Ratings has assigned Nepal a long-term foreign-currency issuer default rating (IDR) of 'BB-', reflecting a mix of strengths and vulnerabilities in the country's economic and financial framework.*

### **Key Highlights:**

#### **1. Debt and Liquidity:**

- Nepal's debt burden is low compared to its peers, with government debt at 44% of GDP for FY24, below the 'BB' median of 55%.
- The debt structure benefits from high concessional external financing, with average interest rates around 1% and a long average maturity of 13 years.

#### **2. Economic Growth:**

- Medium-term GDP growth is forecasted at 5%, supported by hydropower development and export agreements with India.
- The remittance inflows, constituting about 25% of GDP, continue to drive consumption and investment, enhancing resilience.

#### **3. Fiscal Challenges:**

- Nepal's fiscal deficit, estimated at 5% of GDP for FY24, is expected to narrow to 4% by FY26, supported by fiscal consolidation and domestic revenue mobilization strategies.
- A reliance on optimistic revenue projections and weak spending execution at state levels are persistent issues.

#### **4. External Position:**

- Nepal experienced a current account surplus of 4% of GDP in FY24 due to import compression, remittance inflows, and tourism recovery.
- Foreign exchange reserves reached over \$13 billion, covering nearly 12 months of external payments, well above the 'BB' median.

#### **5. Structural Weaknesses:**

- Nepal remains vulnerable to external shocks and natural disasters, with a GDP per capita of \$1,400—significantly below the 'BB' median.
- Governance indicators, though improving, remain weak, reflecting political instability and institutional inefficiencies.

#### **6. Banking Sector:**

- Bank credit to the private sector, though high at 86% of GDP, is supported by a remittance-funded deposit base.
- Non-bank financial institutions add credit risks, but regulatory improvements are underway.

#### **Outlook and Risks:**

*The stable outlook reflects expectations of continued economic stability without significant credit pressures. However, risks include:*

- Challenges in implementing development projects amidst political instability.
- Potential strain on foreign exchange reserves if external financing support declines.

#### **Conclusion:**

*Nepal's 'BB-' rating underscores its capacity to manage debt and leverage external financing while highlighting vulnerabilities in governance and economic diversification. Growth prospects tied to hydropower and remittances are key drivers, but addressing structural weaknesses will be crucial for improving its credit profile.*

1. Nepal's economy is facing significant challenges that extend beyond its short-term fundamentals, which remain relatively stable. These challenges include rising risks to businesses, declining private sector confidence, and vulnerabilities posed by climate-induced disruptions. According to Fitch Ratings, Nepal's credit profile reflects a delicate balance between economic potential and fiscal vulnerabilities, with the latest rating indicating cautious optimism amid structural challenges.

### **2. Current Economic Context**

The economy has been heavily impacted by unpredictable weather patterns, including flash floods, which have caused substantial damage to agriculture, hydropower, transport, and services. Agriculture, a sector contributing approximately 23.9% of GDP, has suffered from reduced productivity, while key hydropower projects—both operational and under construction—have incurred losses estimated at NPR 30 billion.

### **3. Economic Indicators and Performance**

- 1. GDP Growth:** The Government of Nepal has set a growth target of 6% for 2024-25; however, due to reduced capital expenditure, declining corporate profitability, and weak demand, growth is expected to fall below 4%. Fitch forecast growth to pick up to about 5% over the medium term, from the policy-induced slowdown to 2% in FY23 and an estimated 3% in FY24.
- 2. Inflation:** While the Consumer Price Index (CPI) inflation has eased to an annualized rate of 4.82% (as of October 2024), food price volatility remains a significant concern, exacerbated by weather-related disruptions and supply chain constraints.
- 3. Trade Deficit:** Nepal's trade deficit continues to widen, standing at \$ 3.54 billion for the first four months of 2024/25. Imports have surged due to higher energy and commodity prices, while exports, primarily agricultural goods and handicrafts, remain subdued.
- 4. Private Sector Confidence:** Private consumption, which accounts for roughly 67% of GDP, has stagnated, with household spending impacted by high inflation and slowing rural demand. Gross fixed capital formation, a critical driver of economic growth, showed only a marginal increase of 2.3% in the first quarter of 2024-25.
- 5. Energy Sector:** Hydropower—accounting for over 90% of Nepal's electricity generation—has faced setbacks due to flooding. Estimated losses in this sector exceed NPR 30 billion, negating gains from earlier investments.

## Policy Recommendations

*Nepal Rastra Bank (NRB) and the Ministry of Finance must adopt targeted fiscal and monetary measures to stabilize the economy and regain business confidence. Recommendations include:*

- 1. Monetary Policy: The Nepal Rastra Bank (NRB) must take decisive steps to stimulate demand while ensuring that interest rate policies are carefully calibrated to support economic recovery. A balanced approach to monetary easing and inflation control is crucial to restoring confidence and fostering growth in key sectors.*
- 2. Fiscal Stimulus: The government must expedite capital expenditure, particularly in infrastructure, to create jobs and stimulate domestic demand. Allocating resources for post-disaster recovery and building climate-resilient infrastructure should be a priority.*
- 3. Investment Climate: Attracting local and foreign investment through regulatory reforms, tax incentives, and ease of doing business initiatives is essential for long-term growth. Efforts should focus on developing sectors such as tourism, IT, and renewable energy.*
- 4. Trade Policies: Reducing the trade deficit requires boosting exports through diversification and leveraging trade agreements with neighboring countries. Strengthening local industries and substituting imports with domestic production can also help.*
- 5. Climate Resilience: Investment in disaster management and climate adaptation projects will be critical to mitigate the economic damage from unpredictable weather events.*

## Outlook 2024-25

*Nepal's economic trajectory for 2024-25 will depend on the effectiveness of government policies and the private sector's recovery. Despite Fitch's rating reflecting cautious optimism, the economy faces significant downside risks. Addressing inflation, rebuilding flood-damaged infrastructure, and improving investor confidence are vital for achieving sustainable growth. Without immediate action, the government's ambitious 6% growth target may remain out of reach, with actual growth projected at 3.8–4.0%.*

# *Strategic Measures for Economic Recovery and Stimulus Initiatives in Nepal*

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*There is hope that Nepal will embrace a comprehensive strategy for economic recovery built on nine pivotal measures aimed at addressing both immediate and long-term challenges. This begins with establishing **Foundational Concepts for Inclusive Revival**, ensuring that growth benefits all sectors of society. **Sectoral Adaptation** will address specific challenges in agriculture, retail, and manufacturing, while the nation embraces the “**New Economy**” by focusing on digital technology and services.*

*Nepal is poised to **Enhance Competitiveness** by aligning with global standards and adopting **Global Best Practices** from successful policies around the world. Engaging key stakeholders—businesses, employees, and government—will ensure inclusive and collaborative economic planning.*

*The strategy also includes **Tailored Initiatives** to target key sectors like hospitality and technology, while addressing productivity concerns. To drive informed decision-making, Nepal will need to prioritize **Data Enhancement**, improving data systems and metrics. Finally, adopting a **Performance Framework** will help monitor progress, ensuring that economic achievements are transparent, measurable, and continuously improving.*

*With the right commitment, Nepal can pave the way for sustainable and inclusive economic growth.*

## *Nepal's import data*

- *Nepal's import data for the fiscal years 2022/23, 2023/24, and projected 2024/25 reveals significant shifts in trade patterns across various commodities, reflecting evolving economic dynamics.*

## *Shifting consumer preferences*

- *Certain goods, such as crude soybean oil, liquefied petroleum gas (LPG), and smartphones, exhibit steady growth, highlighting rising consumer demand and modernization. For instance, LPG imports are projected to grow by 17.93%, signaling a transition from traditional fuels to cleaner energy sources, while smartphone imports are expected to rise by 13.59%, showcasing increased adoption of digital technologies. Similarly, crude sunflower oil shows remarkable growth of 43.24%, indicating shifting consumer preferences toward healthier alternatives.*

## *Changing economic priorities*

- *In contrast, several key commodities are witnessing a sharp decline in imports. Gold imports are projected to plummet by 472.73%, possibly due to reduced demand or policy restrictions. Diesel imports are also expected to decline by 39.01%, indicating decreased movement of industrial finished goods or a shift toward alternative energy sources. Crude palm oil imports show a significant drop of 191.67%, likely reflecting changes in import policies or reduced consumption. These trends suggest changing economic priorities and consumption patterns, which may help in narrowing trade deficits.*

## *Agricultural imports*

- Agricultural imports reveal a mixed trend. While maize imports are expected to decline slightly (-8%), the import of low erucic acid rape or colza seeds is projected to grow significantly by 29.41%, potentially due to changing consumer preferences or favorable import policies. These shifts highlight ongoing diversification in Nepal's agricultural trade.

## *Technology sector*

- In the technology sector, imports of laptops and notebooks are anticipated to grow by 13.64%, reflecting Nepal's increasing focus on digital transformation and tech adoption. Combined with the growth in smartphone imports, this points to the country's growing emphasis on digitization and modernization.

## *Overall*

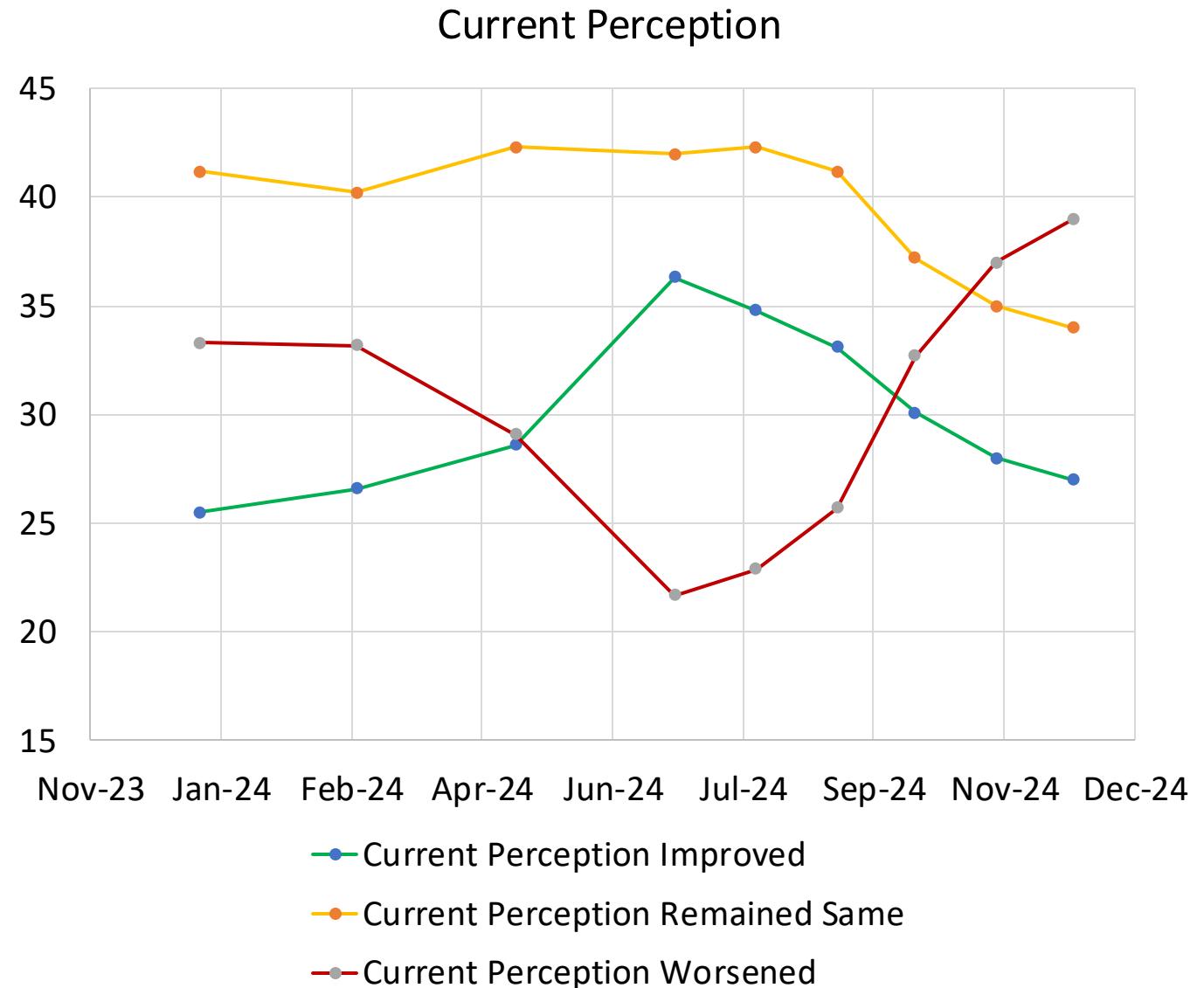
- Overall, the data reflects Nepal's economic transformation, characterized by declining imports of high-value commodities like gold and diesel and growing demand for industrial inputs, clean energy, and technology. The decline in diesel imports suggests subdued activity in transportation and finished goods distribution, while the rise in industrial raw material imports points to increased production and infrastructure projects. These trends indicate that Nepal's growth is becoming more industrially driven, potentially laying the foundation for long-term economic expansion and structural change.

# November 2024

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The Consumer Perception Survey for 2024 reveals fluctuating consumer sentiment regarding economic conditions throughout the year. Optimism, measured by the percentage of respondents who felt conditions improved, increased steadily from 26% in January to a peak of 36% in July, reflecting positive developments or seasonal influences. However, this optimism declined gradually after August, dropping to 27% by December, signaling waning confidence as the year progressed. Meanwhile, a significant proportion of respondents consistently believed conditions remained unchanged, with this sentiment ranging between 40% and 42% for most of the year before falling slightly to 34% in December.

On the other hand, the perception of worsening conditions decreased from 33% in January to a low of 22% in July but rose sharply from September onward, peaking at 39% in December. This shift indicates increasing pessimism and economic concerns in the latter months of the year, potentially driven by inflation, economic uncertainties, or declining market confidence. Overall, consumer sentiment shifted from mid-year optimism to end-of-year pessimism, highlighting the fragile nature of consumer confidence.



*Nepal's economy in 2025 is likely to encounter significant challenges, not due to immediate fundamental weaknesses but because of waning confidence within the private sector and growing risks to business stability. Key issues such as excessive bureaucracy, outdated regulations, weak governance, rising extremism, and rent-seeking practices continue to undermine both investor and consumer trust. Addressing these structural problems is imperative to avoid economic stagnation and promote sustainable growth.*

*Although inflationary pressures have moderated, consumer price inflation (CPI) is expected to range between 4.75% and 5.5% in 2025, with food price volatility continuing to present a significant risk. On a positive note, exports have demonstrated substantial progress, rising to NPR 20.80 billion in December 2024, a significant increase from NPR 8.6 billion in early 2019. Nevertheless, imports remain elevated at NPR 148.20 billion, maintaining considerable pressure on Nepal's trade deficit. Private sector credit grew minimally in 2024, highlighting a slow and uneven recovery in lending activities following prior disruptions in credit availability.*

*On the fiscal front, government spending reached NPR 141 billion during November-December 2024, but capital expenditure lagged at only NPR 6.4 billion. Revenue collection amounted to NPR 76 billion, which, while steady, remains inadequate to address rising social security obligations and administrative costs. This fiscal shortfall continues to exacerbate the government's debt burden.*

*Interest rates have trended downward, with the weighted average lending rate expected to decline to 8.25% and base rate falling to 7.00% by December 2024. However, deposit rates also decreased to 4.99%, reducing incentives for savings mobilization. Despite the softer interest rate environment, domestic demand remains subdued, and private consumption has shown little improvement, thereby constraining domestic economic momentum. Domestic economic drivers, including private consumption and gross fixed investment, have shown limited sequential progress. While gains in energy production are promising, they have been offset by sluggish manufacturing activity and a weakening services sector. Although the government has set an ambitious growth target of 6% for this fiscal year, persistent structural bottlenecks and weak economic fundamentals suggest actual growth may fall below 4%.*

*To stimulate economic growth, Nepal must prioritize job creation, attract local and foreign investment, secure foreign aid, harness its natural resources, boost productivity, and address its trade imbalance. These strategic actions will be essential to overcoming current challenges and laying the foundation for sustainable economic development.*

## Economic Growth

## Inflation

GoN set GDP growth target rate at 6% for FY 2024/25

For FY 2024/25 the GoN set target rate of inflation at 5.5%  
**November inflation 5.60%**  
**Exceeded NRB target**

The GDP growth trends over the last two fiscal years highlight varying sectoral performances. Stable contributors like **Agriculture, Forestry, and Fishing** showed consistent growth, while **Electricity, Gas, Steam, and Air Conditioning Supply** and **Accommodation and Food Service Activities** demonstrated potential as key drivers despite some quarterly fluctuations.

In 2023/24, a comparison of Q3 and Q4 reveals that most sectors experienced a slowdown in Q4, including **Transportation and Storage, Accommodation and Food Services, and Electricity Supply**, while a few, like **Agriculture** and **Real Estate**, showed modest improvements.

**Electricity Sector:** After robust growth in Q3 of 2023/24 (47.4%), the sector witnessed a sharp fall, entering a negative trajectory in Q4 (-3.5%). However, the **Tourism sector**, reflected in Accommodation and Food Services, indicates a strong recovery post-pandemic, with growth momentum driven by increased international and domestic travel. On the downside, sectors like **Construction** and **Manufacturing** struggled, pointing to challenges in infrastructure development and industrial growth.

To drive the economy forward in the next fiscal year, Nepal could focus on enhancing the **energy sector** for sustainable growth and leveraging **tourism** to boost services and hospitality. Addressing challenges in **construction** and **manufacturing** with targeted policies could further stabilize economic performance.

Industrial Classification	2022/23				2023/24				Q4 vs Q3
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	
Agriculture, forestry and fishing	3.1	2.5	3.9	1.8	2.3	3.4	3.1	3.2	Up
Mining and quarrying	-3.9	1.2	-2.7	9.0	10.5	1.5	-5.3	3.3	Up
Manufacturing	-2.6	-3.5	-1.3	-0.4	0.6	-4.2	-3.6	1.1	Up
Electricity, gas, steam and air conditioning supply	35.0	11.5	21.6	36.1	23.5	26.1	47.4	-3.5	Down
Water supply; sewerage, waste management	1.8	3.7	2.8	4.8	3.9	3.1	2.4	1.7	Down
Construction	4.4	-16.8	-5.5	13.7	12.6	2.0	-6.6	-13.4	Down
Wholesale and retail trade; repair of motor vehicles & motorcycles	-0.5	-14.3	-1.9	7.3	-0.4	1.4	-2.4	2.0	Up
Transportation and storage	2.1	1.2	1.0	1.3	3.1	16.7	17.5	10.9	Down
Accommodation and food service activities	53.7	-1.1	5.3	27.5	15.8	36.4	23.7	12.3	Down
Information and communication	6.2	4.1	4.7	1.6	6.9	7.9	6.4	-1.6	Down
Financial and insurance activities	16.3	10.8	21.0	-13.4	10.1	8.2	7.0	6.2	Down
Real estate activities	2.2	2.2	2.2	2.2	3.0	3.0	3.0	3.0	Up
Professional, scientific and technical activities	3.7	3.3	4.1	4.6	5.4	4.1	3.9	3.3	Down
Administrative and support service activities	4.8	5.9	4.4	5.1	6.0	2.1	2.3	5.8	Up
Public administration and defence; compulsory social security	5.1	5.6	12.2	0.5	2.9	2.8	1.6	10.8	Up
Education	2.7	6.6	3.7	2.8	2.1	2.5	3.4	2.9	Down
Human health and social work activities	10.7	6.1	5.0	4.7	5.9	5.4	7.0	3.8	Down
Others services	10.1	3.4	4.1	3.0	0.6	6.4	5.3	4.4	Down
Aggregate	4.6	-1.1	2.6	3.7	4.5	4.6	3.1	2.1	Down

# Policy Mistakes

## 1. Consumer Price Inflation (CPI)

*Consumer price inflation exhibited considerable volatility from 2019 to 2024. The initial years saw relatively high inflation rates, which moderated slightly during the pandemic but surged again in the subsequent years.*

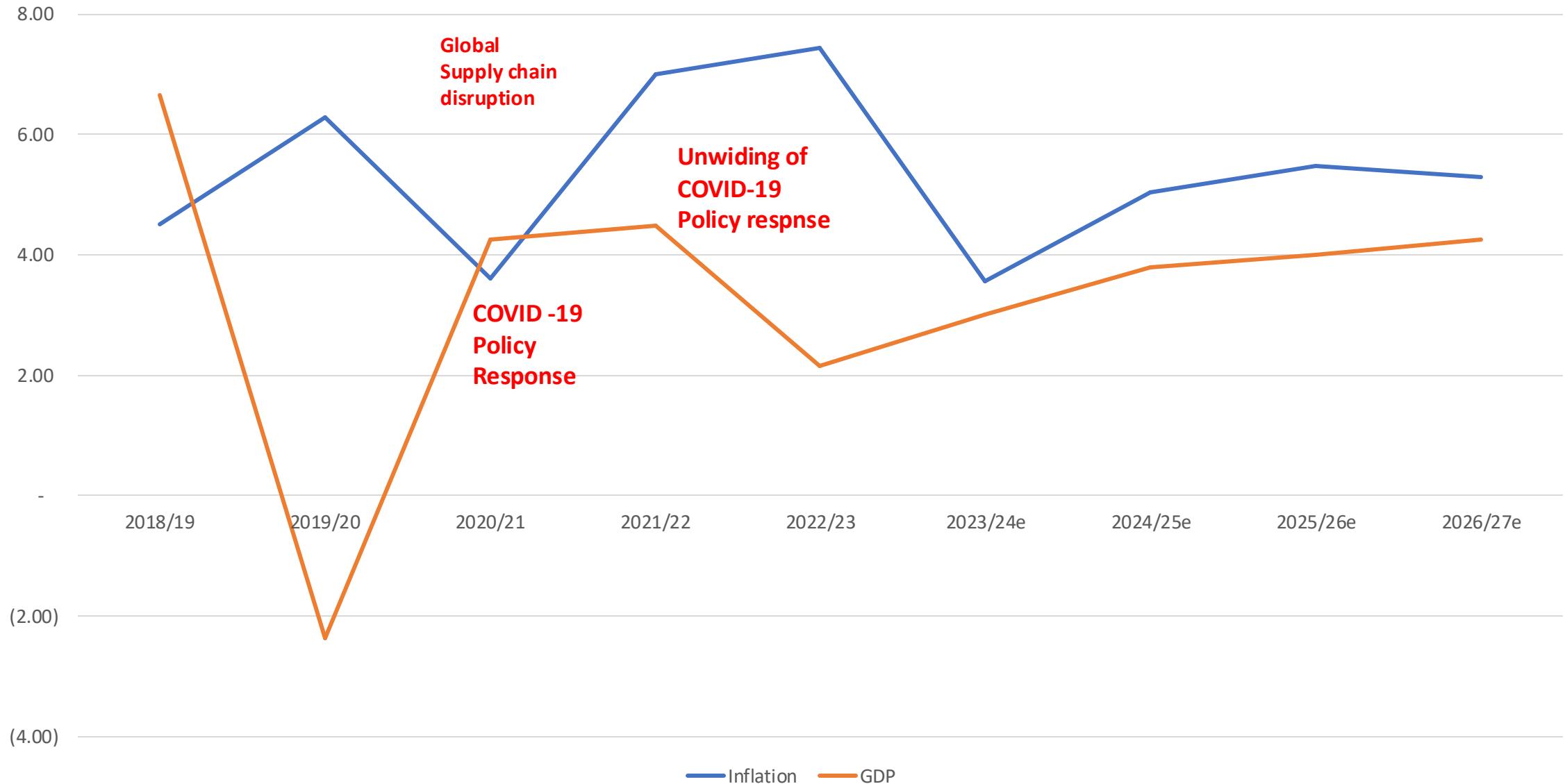
- 2019-2021: CPI fluctuated between 4.44% and 6.95%.
- 2022: A decline in CPI, reaching a low of 2.70% in Jan-Feb, reflecting subdued demand during the pandemic.
- 2023-2024: Inflation surged, peaking at 8.56% in 2023 before stabilizing around 5.60% by November 2024.

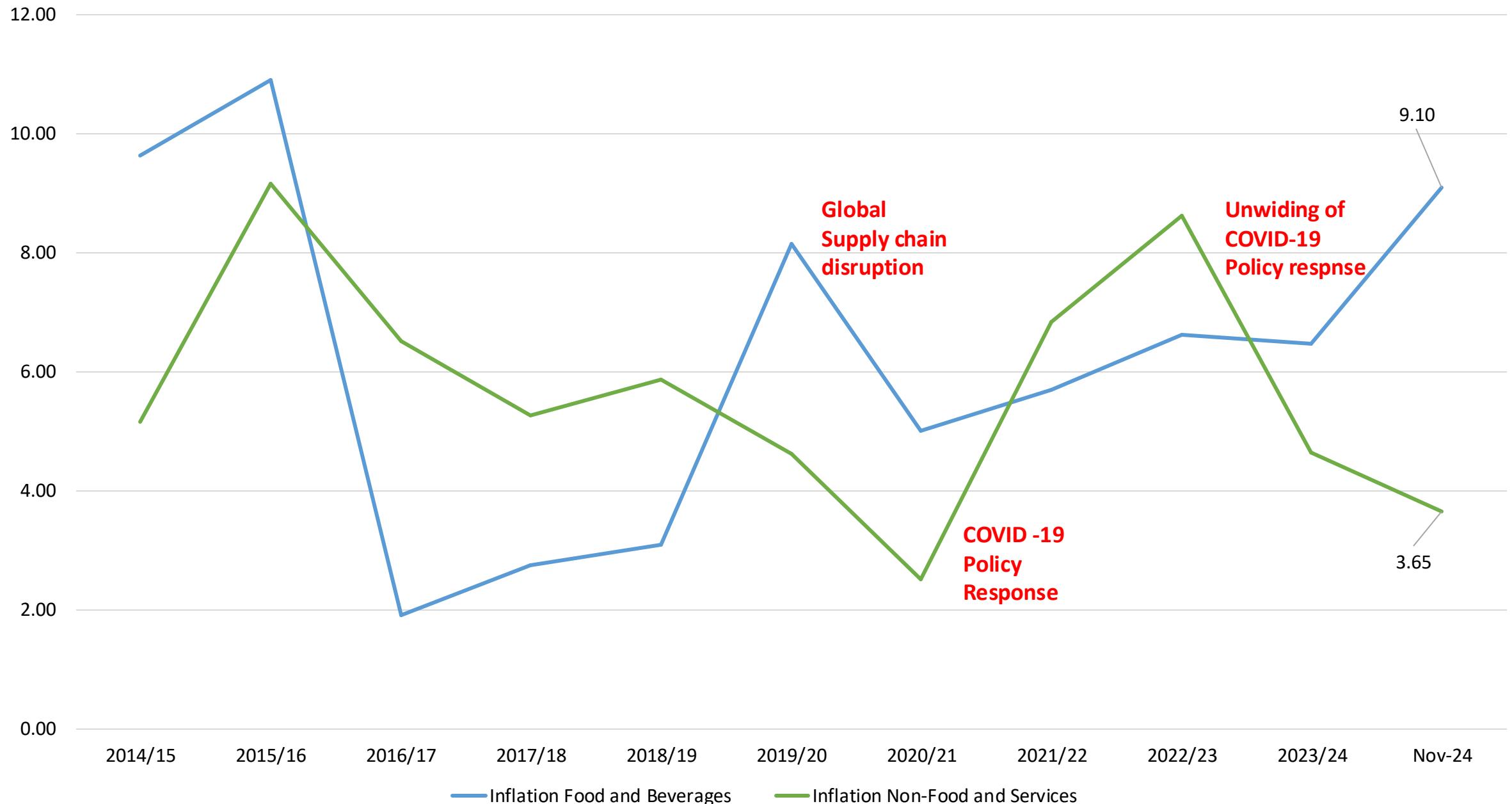
### Policy Mistakes:

- **Reactive Inflation Control:** Sudden adjustments in interest rates aimed at controlling inflation have contributed to economic instability. Nepal's Consumer Price Index (CPI) is heavily influenced by price movements in the Indian market, rendering it largely independent of the Nepal Rastra Bank's (NRB) policy rate. In November, the CPI rose to 5.50%, driven by supply chain disruptions caused by natural calamities.

### Recommendations:

- Gradual and predictable adjustments to interest rates to manage inflation more effectively.
- Implement supply-side policies to address structural causes of inflation.





## 2. Exports and Imports

*The trade dynamics of Nepal showed significant variations, with exports growing inconsistently and imports experiencing sharp fluctuations.*

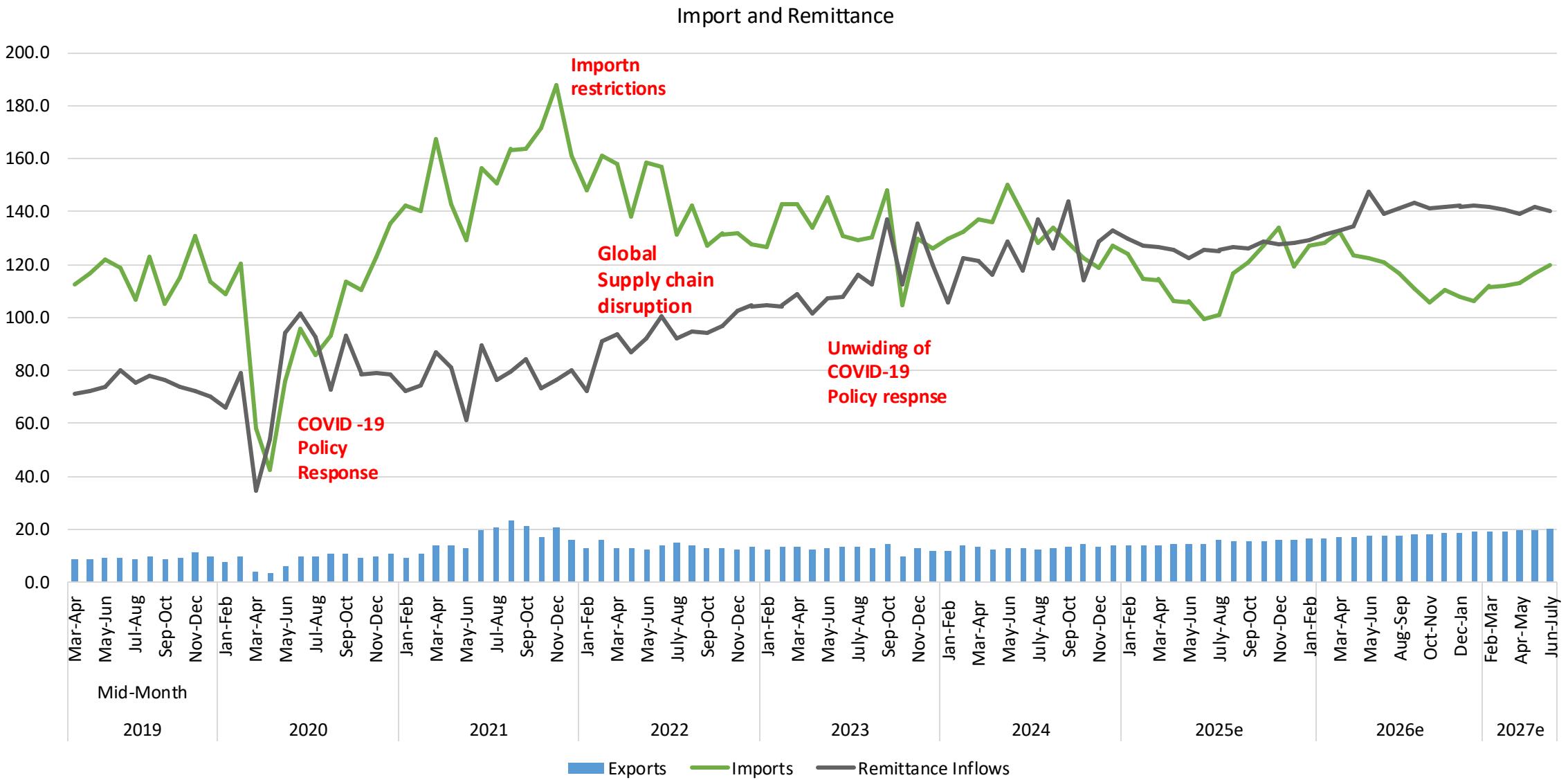
- Exports grew steadily from NPR 8.6 billion in early 2019 to NPR 13.33 billion by December-January 2024, before surging further to NPR 20.8 billion. In contrast, imports experienced significant increases, rising from NPR 112.5 billion in early 2019 to NPR 188.1 billion by December 2021. To address this sharp rise, the Government of Nepal (GoN) imposed import restrictions. Despite these measures, imports rebounded to NPR 148.20 billion by December 2024, indicating a partial recovery.

### Policy Mistakes:

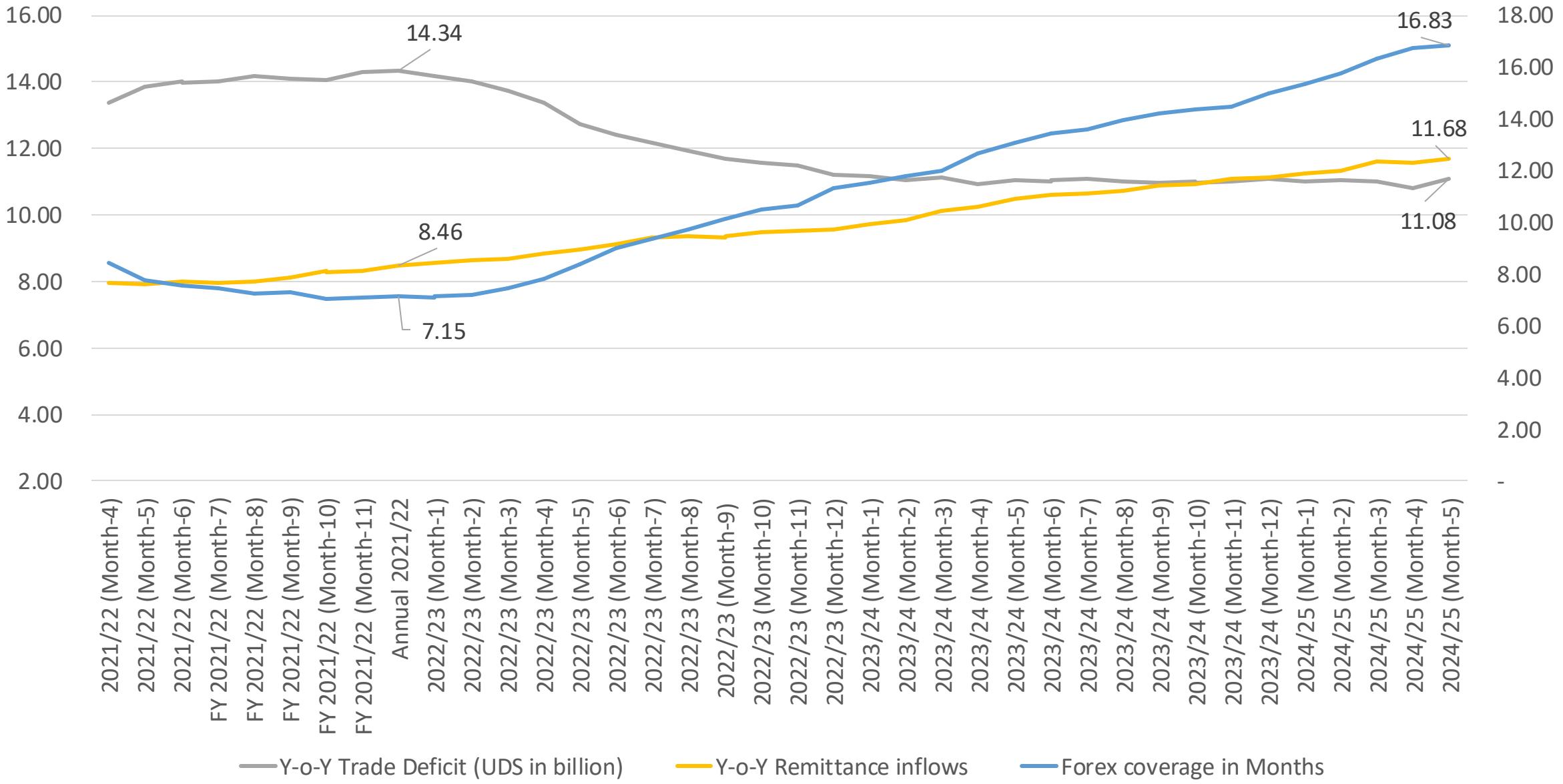
- Overreliance on import restrictions proved to be a short-term solution, causing supply chain disruptions without providing a sustainable resolution to the trade deficit. The ongoing currency depreciation and rising costs are expected to continue exerting pressure on the balance of payments (BOP).

### Recommendations:

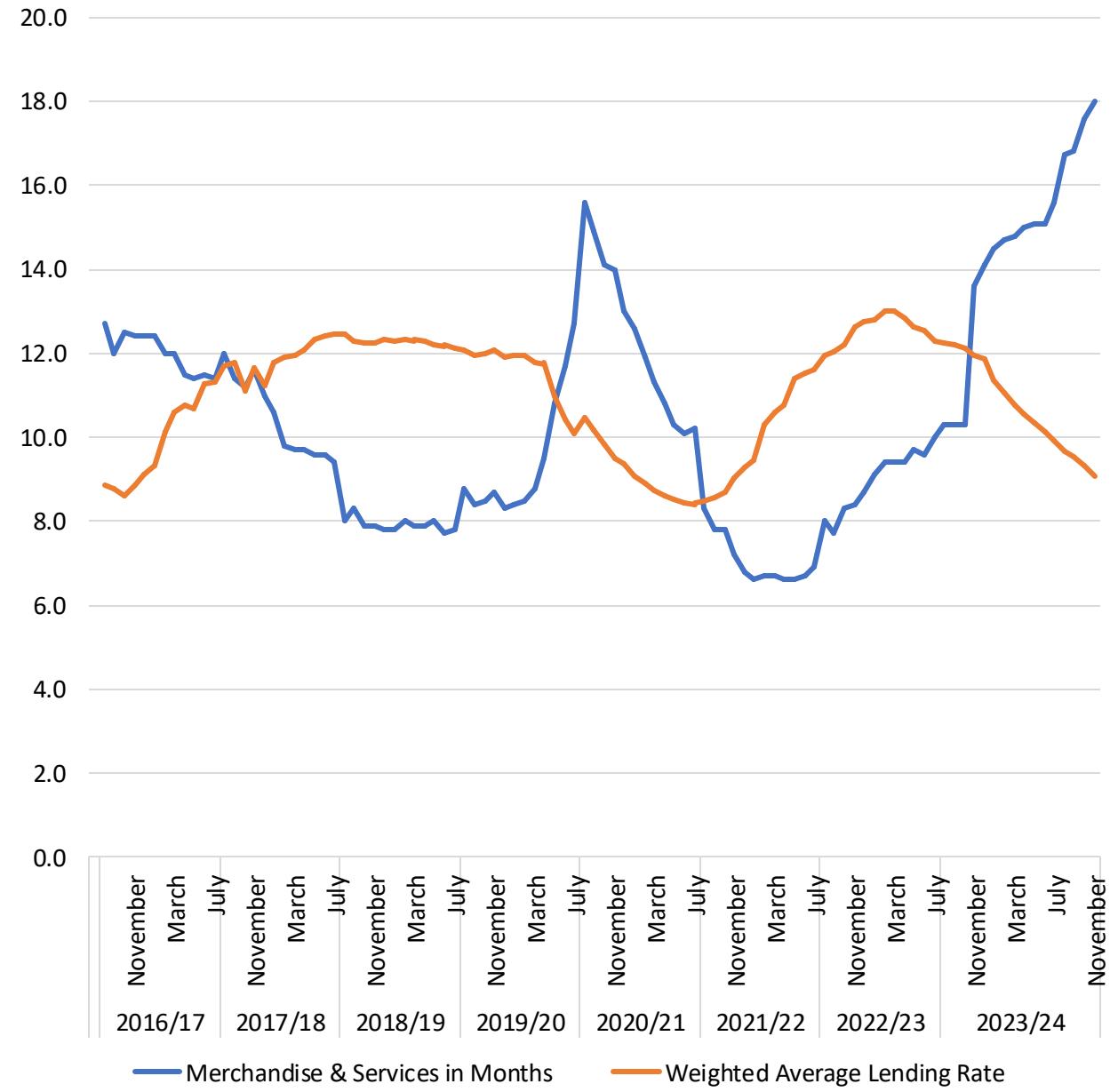
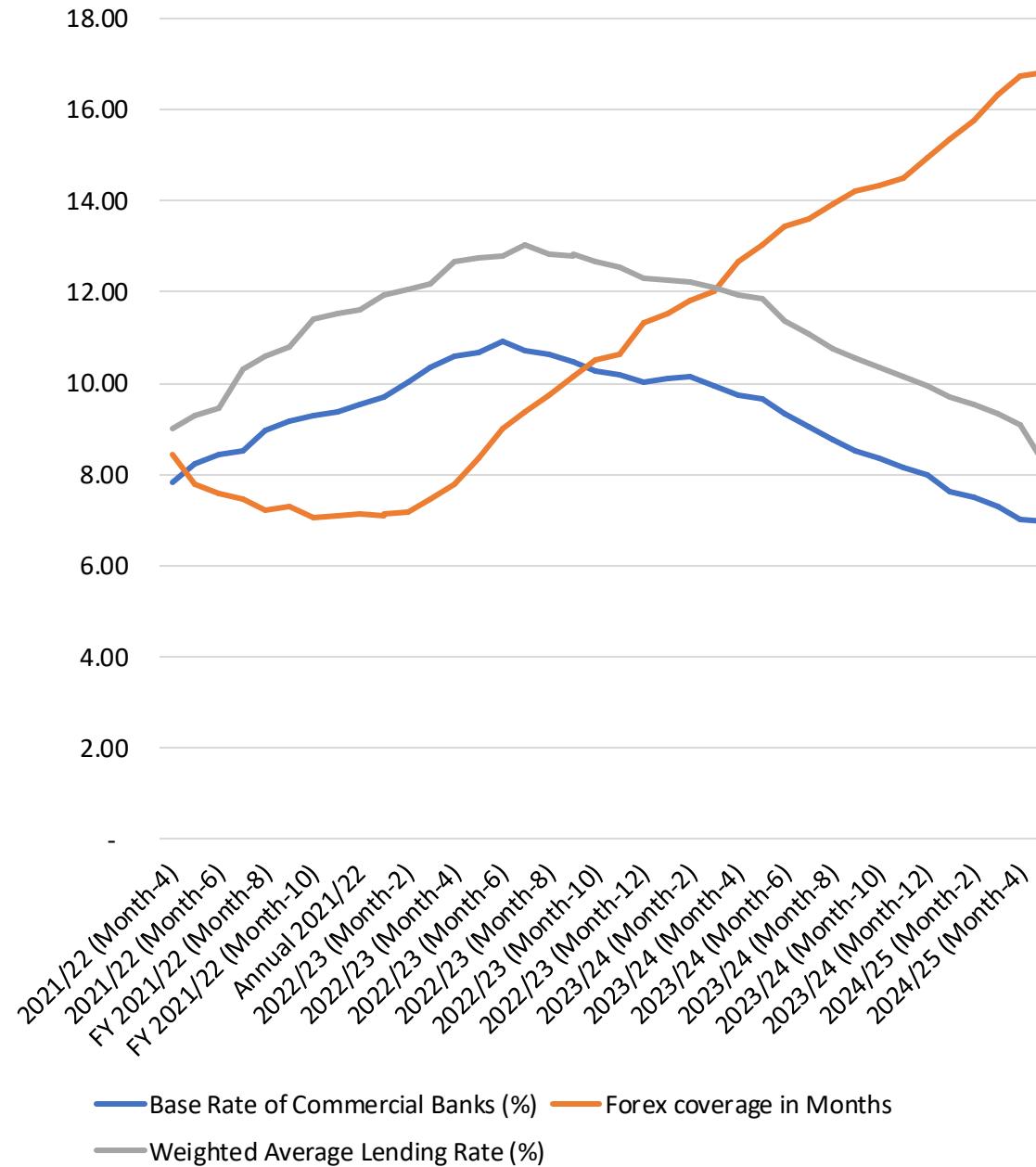
- Develop and promote local industries to reduce import dependency.
- Implement balanced trade policies to ensure essential imports while fostering domestic production.



## Y-O-Y External Sector



# Interest rates and Extranational Sector



### 3. Government Expenditure

*Government expenditure showed considerable volatility, particularly during the pandemic, with significant increases aimed at economic stabilization.*

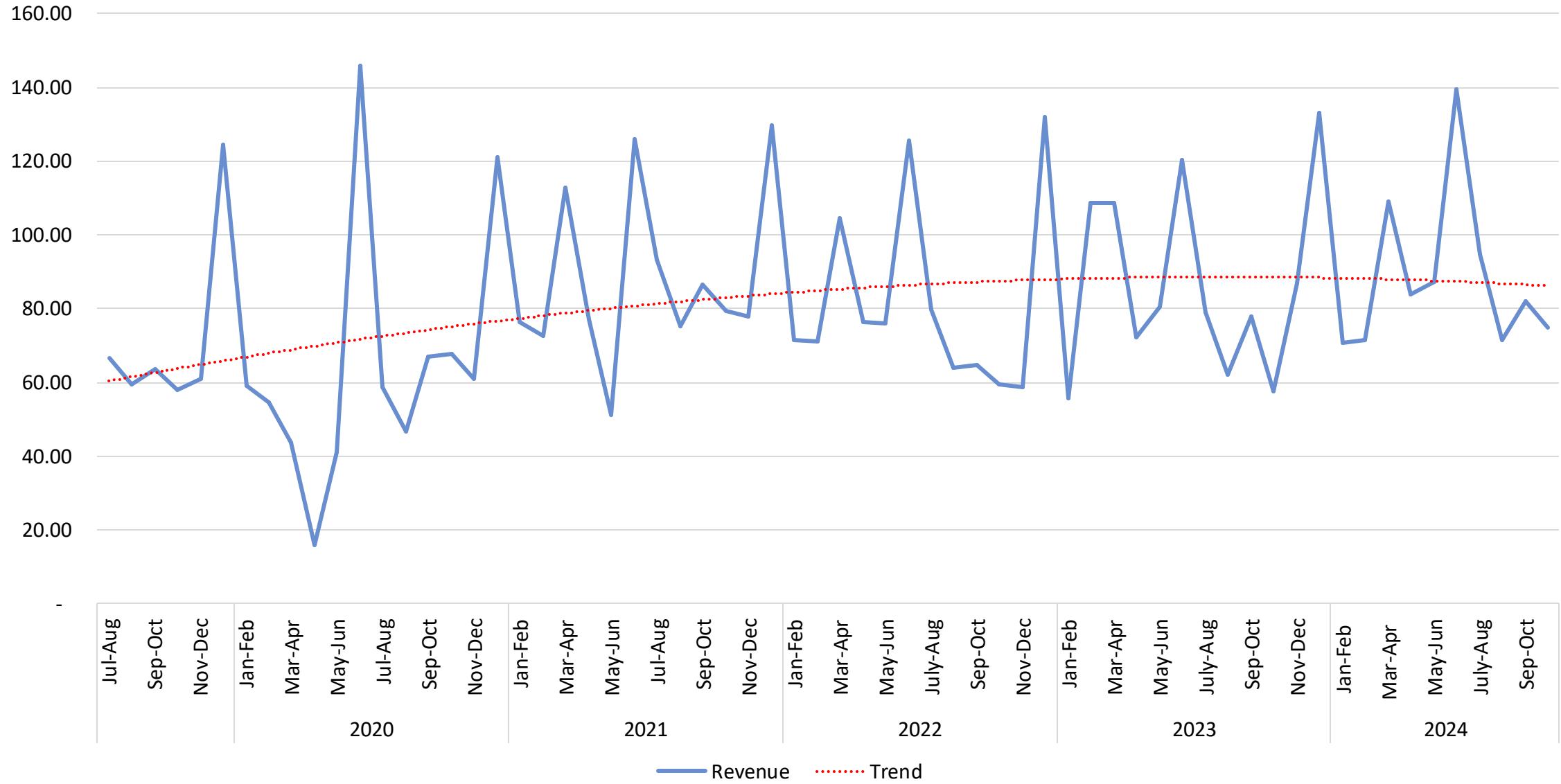
- 2019-2021: Varied widely, peaking at NPR 264.1 billion in Jun-Jul 2021.
- 2022-2024: Continued to fluctuate, reaching NPR 107.8 billion by Mar-Apr 2024.

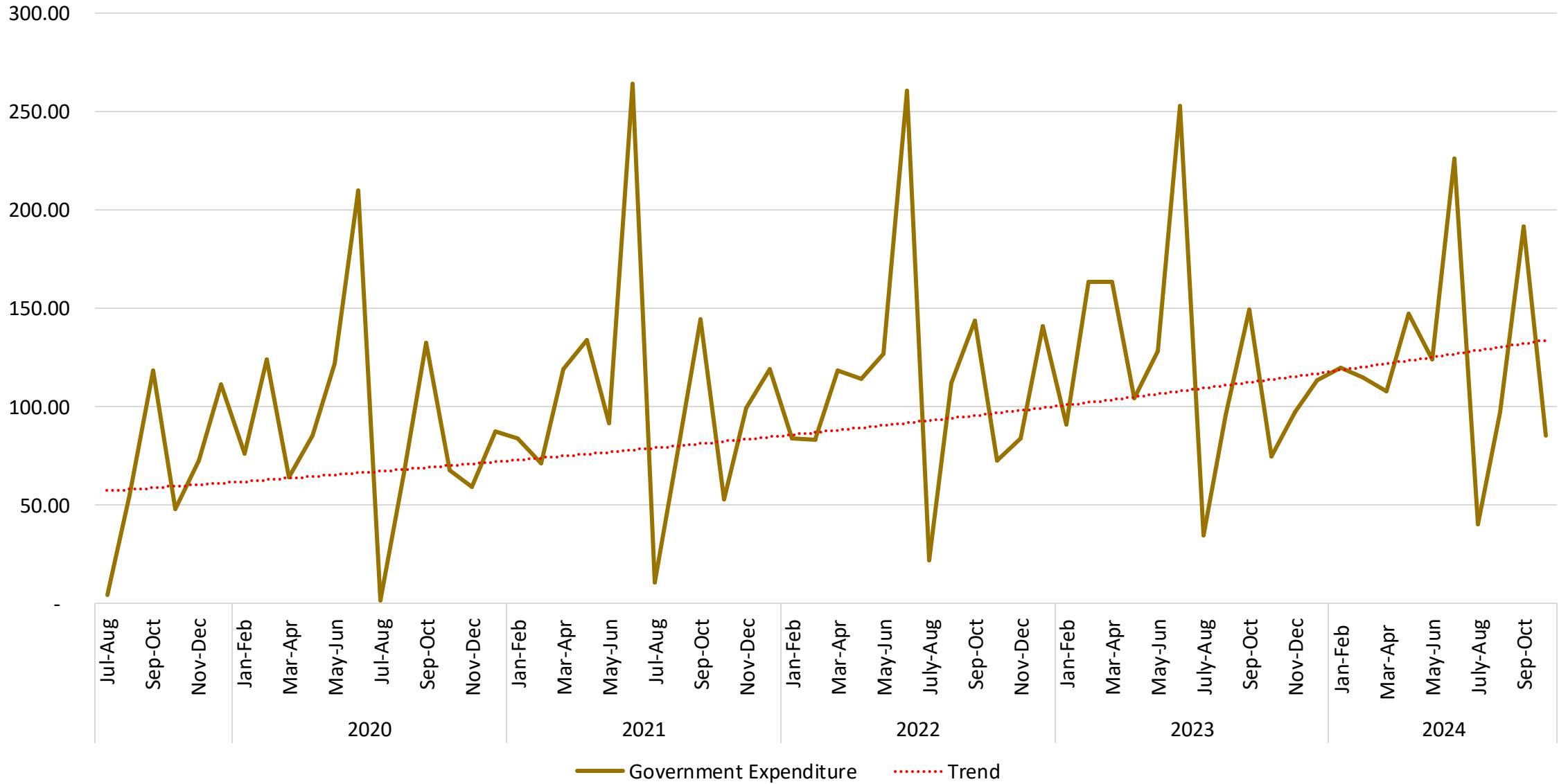
#### Policy Mistakes:

- *Inconsistent fiscal stimulus, marked by delays and erratic implementation, has undermined its effectiveness in stabilizing the economy. High administrative costs and growing social security commitments have increased debt burdens and reduced revenue collection, further straining government spending.*

#### Recommendations:

- *Ensure timely and consistent fiscal interventions to support economic stability.*
- *Focus on efficient allocation and utilization of government resources.*





## 4. Private Sector Credit and Deposit Mobilization

*Private sector credit and deposit mobilization showed high variability, reflecting changes in economic confidence and policy impacts.*

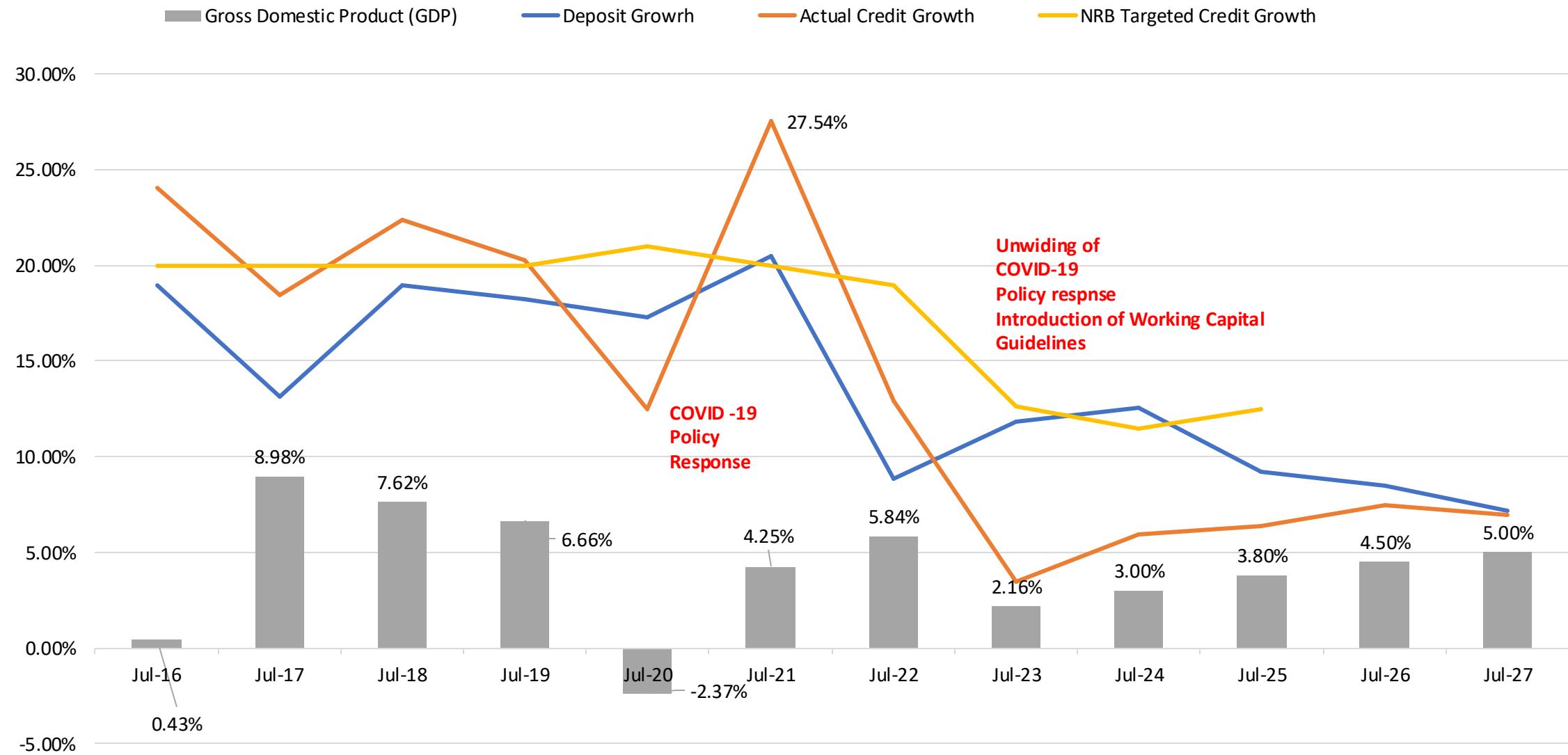
- *Private Sector Credit: Saw periods of contraction and growth, with notable increases during economic recovery phases.*
- *Deposit Mobilization: Experienced similar volatility, with significant peaks and troughs.*

### Policy Mistakes:

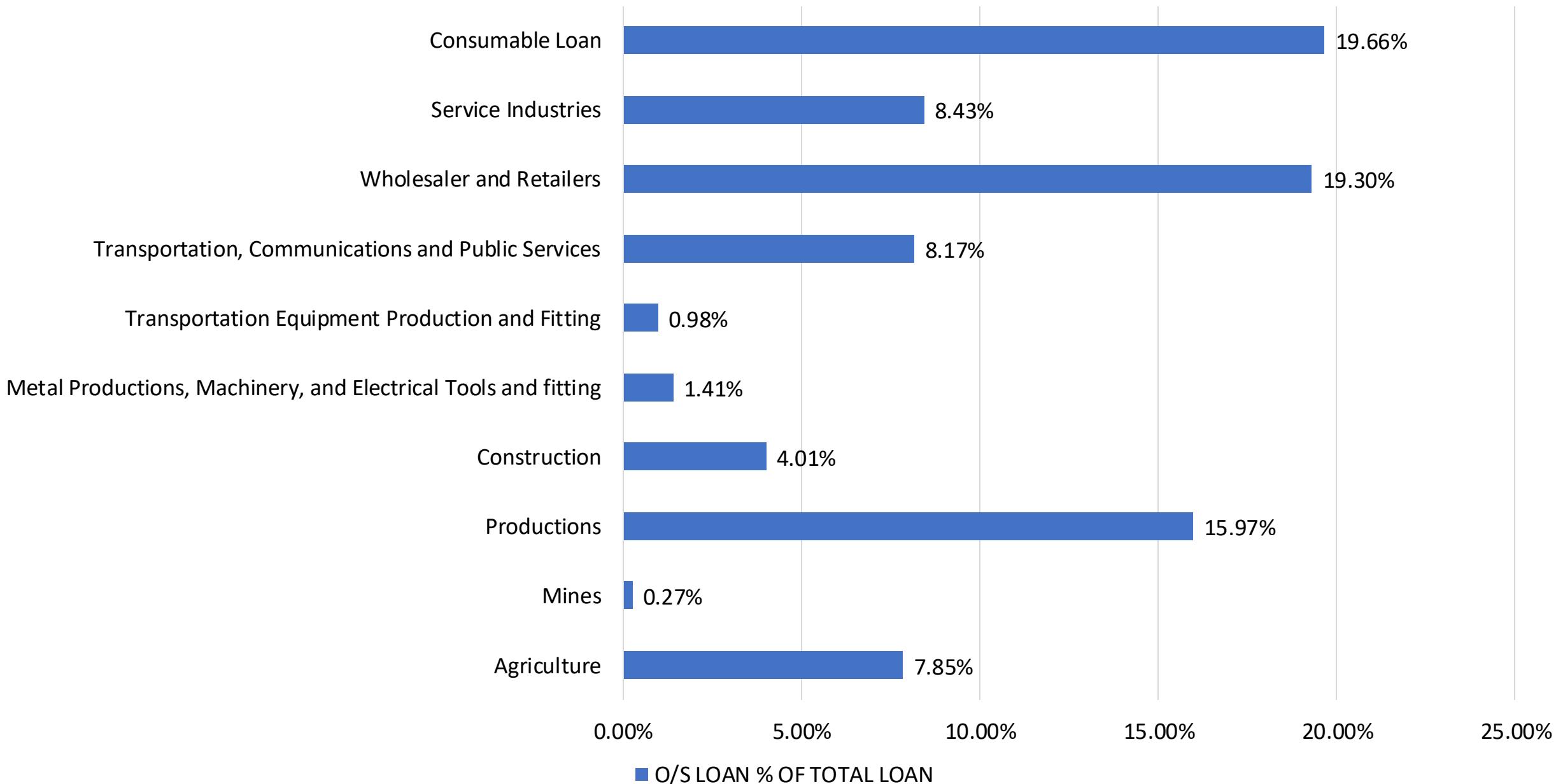
- *Sudden policy changes, such as the rapid implementation of working capital guidelines, caused short-term disruptions in credit availability. Increasing non-performing assets (NPA) have added pressure on capital, while diminished confidence among both lenders and borrowers has further strained domestic demand.*

### Recommendations:

- *Introduce policy changes with phased rollouts to minimize disruptions.*
- *Engage stakeholders in policy development to ensure smooth transitions.*



2024 Nov (P) O/S LOAN % OF TOTAL LOAN



## 5. Interest Rates

Interest rates exhibited a general upward trend, particularly post-pandemic, as the NRB attempted to control inflation and stabilize the economy.

- *Deposit Rates: Increased from approximately 6.70% in early 2019 to around 8.08% by April-May 2023, before declining to 5.01% in November. Despite the lower rates and surplus liquidity, the market continues to experience a credit crunch.*
- *Lending Rates: Rose from about 12.30% in early 2019 to nearly 12.55% by April-May 2023, but have since dropped to 7.02% November.*
- *Base Rates of Commercial Banks: Gradually increased over the period, indicating the impact of a tighter monetary policy stance.*

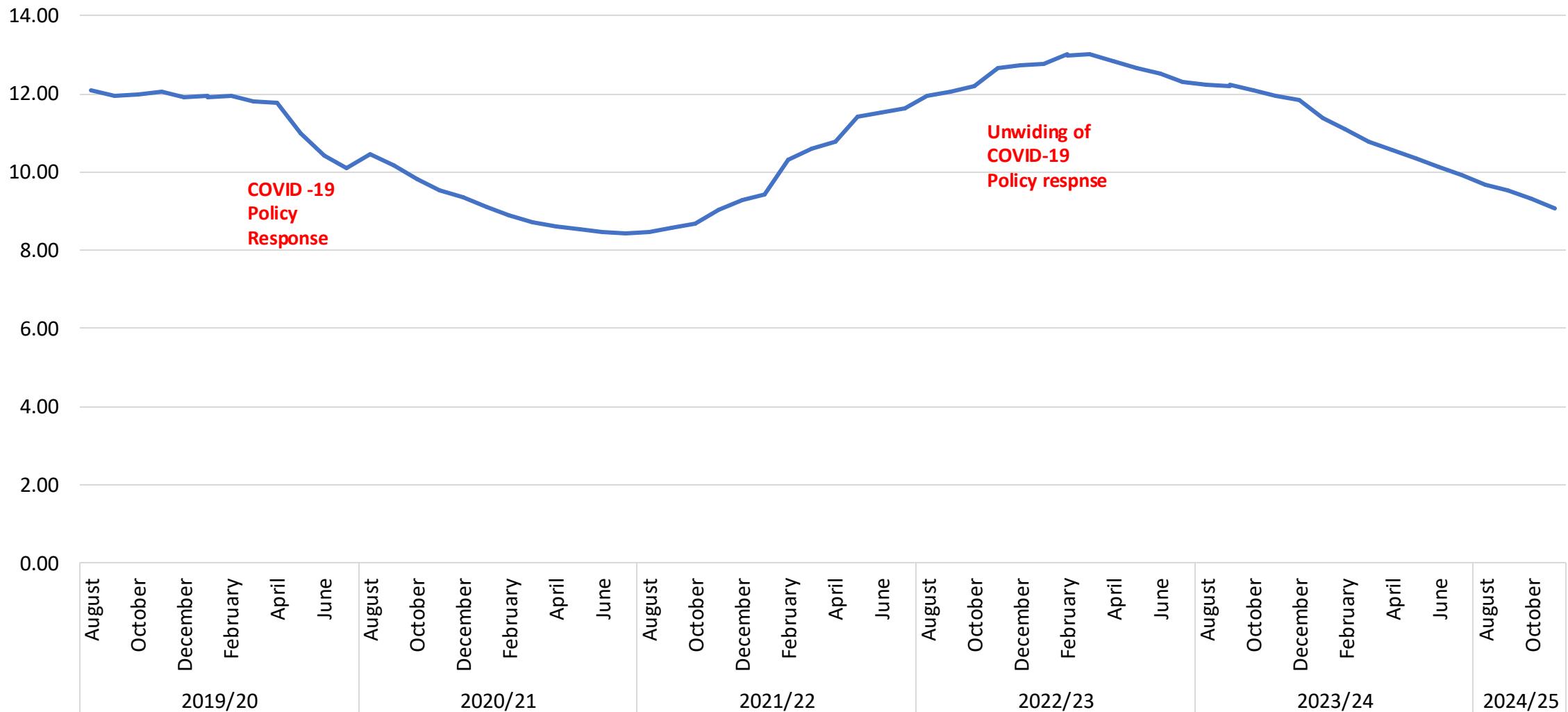
### Policy Mistakes:

- *Overemphasis on Monetary Measures: Relying solely on interest rate adjustments without tackling broader economic challenges proves insufficient. Excessive focus on working capital guidelines, risk weightage, and asset classification fails to align with the subdued growth dynamics of the economy.*

### Recommendations:

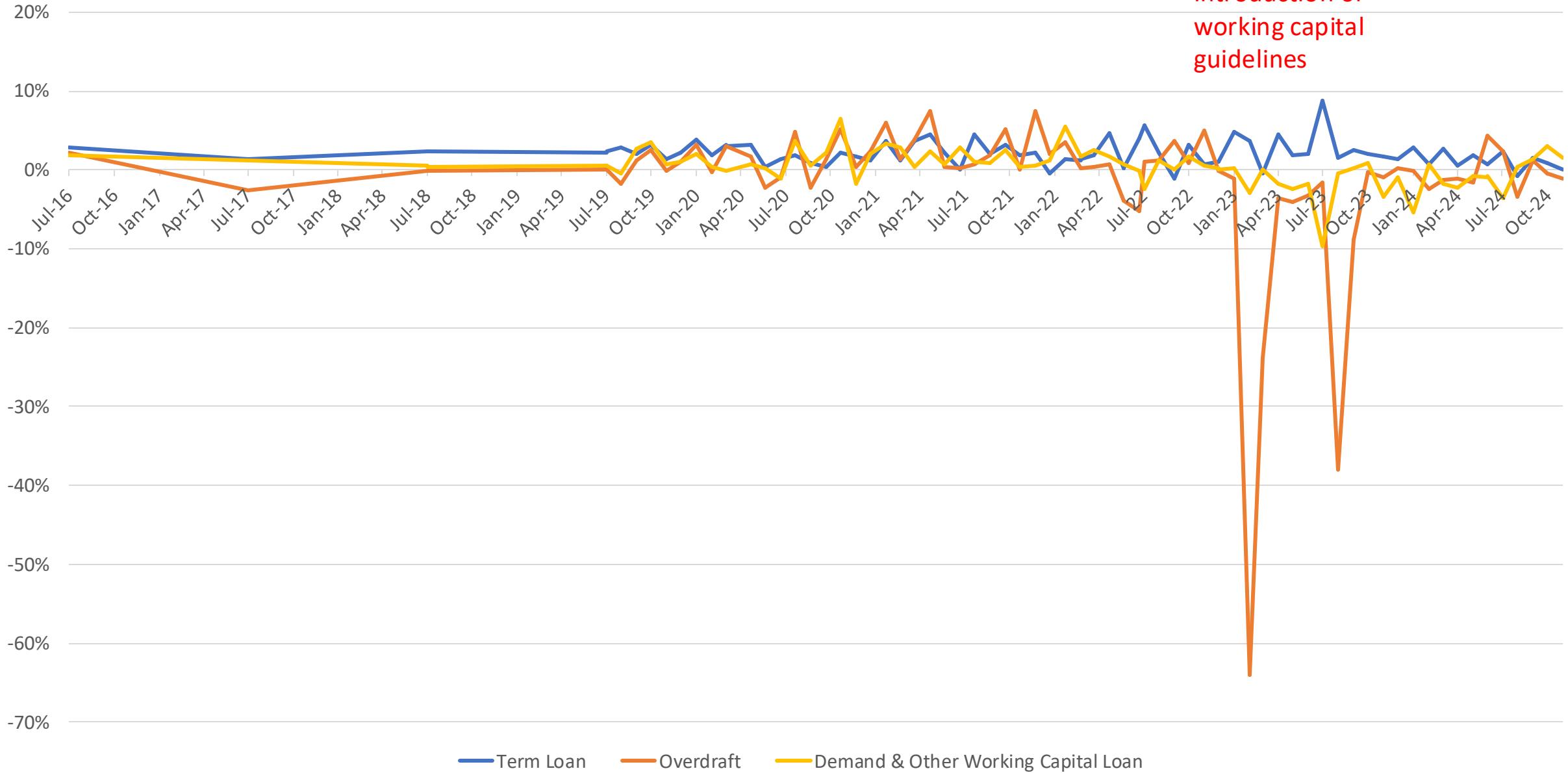
- *Balance monetary measures with structural reforms to enhance overall economic resilience.*
- *Implement targeted lending programs to support critical sectors.*

## Weighted Average Lending Rate (Commercial Bank)

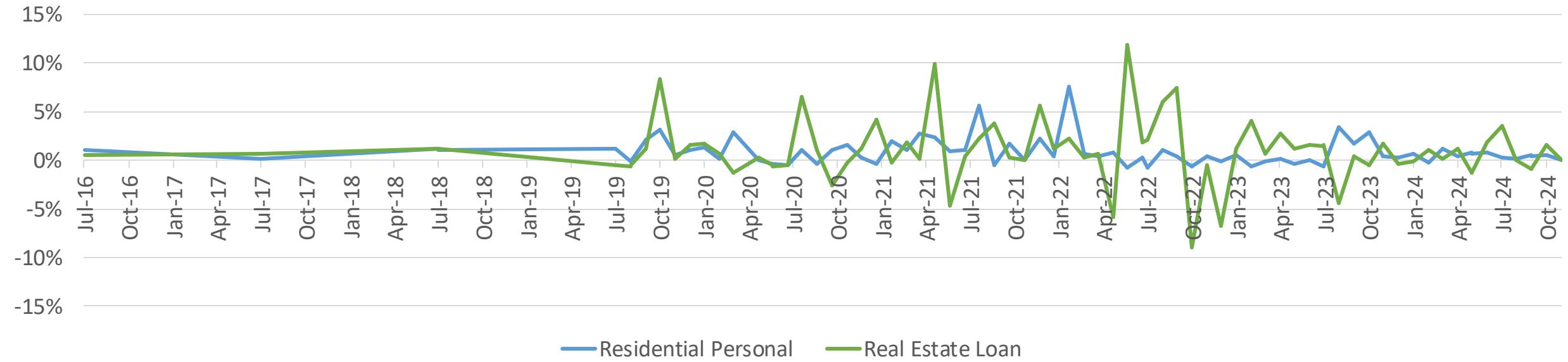


Product wise  
Loan Growth

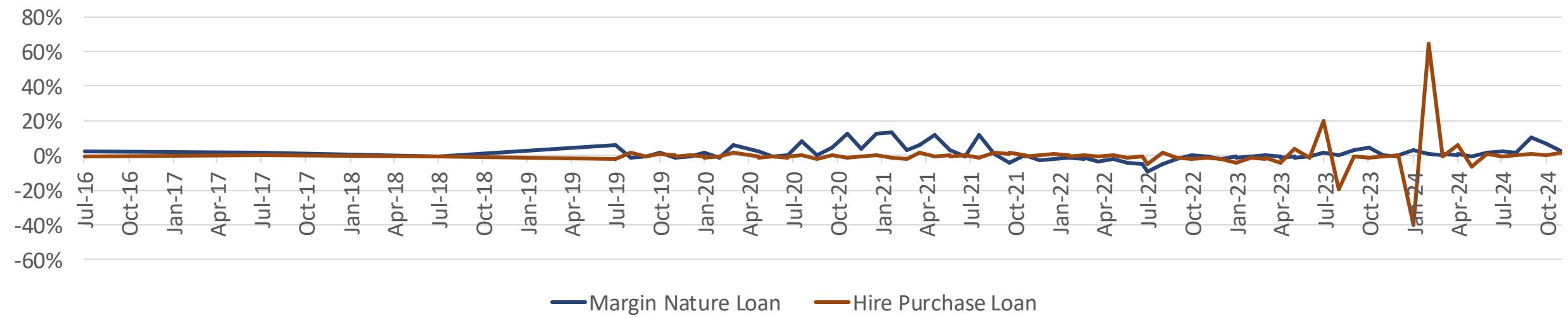
Introduction of  
working capital  
guidelines



## Product wise Loan Growth



## Product wise Loan Growth



# Reforms agenda

**Policy Action Chart**  
**Immediate-Term Actions (0–12 Months)**

<b>Policy Area</b>	<b>Action</b>	<b>Expected Outcome</b>
Monetary Policy	<i>Reduce policy rates to stimulate investment and demand.</i>	<i>Increased credit flow to private sectors and MSMEs.</i>
Fiscal Policy	<i>Expedite post-flood infrastructure rebuilding</i>	<i>Employment creation and restored infrastructure functionality.</i>
Private Sector Support	<i>Offer tax breaks for MSMEs and revive export industries with targeted subsidies.</i>	<i>Improved private sector confidence and export competitiveness.</i>
Climate Resilience	<i>Allocate funds to immediate disaster management projects.</i>	<i>Minimized economic damage from extreme weather events.</i>

## Medium-Term Actions (1–3 Years)

Policy Area	Action	Expected Outcome
Infrastructure	<i>Invest in hydropower projects targeting annual export of electricity worth NPR 100 billion.</i>	<i>Boost in export revenue and trade deficit reduction.</i>
Trade Policy	<i>Negotiate favorable trade agreements with India and China.</i>	<i>Increased market access for Nepali products and reduced trade deficit.</i>
Banking Sector Reform	<i>Implement AMC for managing NPAs and enhance financial stability.</i>	<i>Reduced banking sector vulnerabilities and credit flow normalization.</i>
Financial Inclusion	<i>Develop schemes to integrate rural communities into the formal banking system.</i>	<i>Greater economic participation and savings mobilization.</i>

## *Long-Term Actions (3–5 Years)*

<b><i>Policy Area</i></b>	<b><i>Action</i></b>	<b><i>Expected Outcome</i></b>
<i>Structural Reforms</i>	<i>Update GDP base year from 2010/11 to 2020/21 for accurate economic planning.</i>	<i>Improved policy formulation and realistic economic targets.</i>
<i>Export Diversification</i>	<i>Focus on high-value agricultural exports and IT services.</i>	<i>Increased global competitiveness and export earnings.</i>
<i>Digital Transformation</i>	<i>Modernize FDI and business registration systems to attract investors.</i>	<i>Simplified business processes and higher foreign investment inflows.</i>
<i>Governance</i>	<i>Strengthen institutional frameworks and reduce corruption.</i>	<i>Increased efficiency in public spending and governance credibility.</i>

Corrective  
actions



Reform Area	Recommendation	Priority	Workability	Outcome
PPPI Act 2019	Enable OIBN to recruit staff competitively from outside civil service; strengthen civil service investment facilitation expertise.	High	Attainable	Effective; Boost Private Sector Confidence
	Establish a framework for managing PPP-related fiscal commitments and contingent liabilities (FCCLs).	High	Attainable	Effective; Boost Private Sector Confidence
Tax Laws	Amend laws to allow arbitration for tax disputes rather than criminal investigations.	High	Attainable	Effective; Boost Private Sector Confidence
	Align Section 57 of the Income Tax Act with international norms (tax collection upon company sale).	High	Attainable	Effective; Boost Private Sector Confidence
	Eliminate retrospective taxation and clarify conflicting tax laws.	High	Attainable	Effective; Boost Private Sector Confidence
	Expand Double Taxation Avoidance Agreements (DTAAs) and Bilateral Investment Treaties.	High	Attainable	Effective; Attract FDI with Confidence

Reform Area	Recommendation	Priority	Workability	Outcome
FITTA	Streamline foreign investor processes and expand permissible investment structures.	High	Attainable	Effective; Attract FDI with Confidence
	The provision in relation to investment approval for NRN investors shall be granted through automatic route envisaged by Section 42 of FITTA to Non-Resident Nepalis (NRN)	High	Attainable	Effective; Attract FDI from Diaspora with Confidence
	Amend Section 15 (1) of the FITTA shall provide fund-based approval, to support investment from Non-Resident Nepalis (NRN)	High	Attainable	Effective; Attract FDI from Diaspora with Confidence
	Amend Section 2(c) of FITTA Definition of NRN to support investment from Non-Resident Nepalis (NRN)	High	Attainable	Effective; Attract FDI from Diaspora with Confidence
	Amend Section 11(1), 15 (1), 20 (6), 42 of FITTA to support investment from Non-Resident Nepalis (NRN)	High	Attainable	Effective; Attract FDI from Diaspora with Confidence

Reform Area	Recommendation	Priority	Workability	Outcome
<b>Security Registration and Issuance Regulations, 2073</b>	Amend clause 9 of <i>Security Registration and Issuance Regulations, 2073</i> to support investment companies formed through joint collaboration between the Government of Nepal and Non-Resident Nepalis (NRN).	High	Attainable	Effective; Attract FDI from Diaspora with Confidence
	Borrowers with a loan exposure of NRP 1 billion or more and a credit rating of AA or higher should be mandated to issue commercial paper. To enable this, SEBON, in coordination with NRB, is urged to develop comprehensive guidelines and implement a streamlined approval process for commercial paper issuance. This measure will deepen market participation and create an alternative resource planning avenue for creditworthy borrowers.			Effective; Increase Access to Finance
	Bonds in Local Currency Exempt institutions like ADB and IFC from restrictions on offshore local currency bonds issuance.			Effective; Increase Access to Finance
<b>Foreign Lenders</b>	Allow fixed interest rate tenure negotiation for long-term investments (e.g., green bonds).	High	Attainable	Effective; Boost Private Sector Confidence
	Clarify rules for local currency bond subscriptions by foreign investors.	High	Attainable	Effective; Boost Private Sector Confidence
	Introduce innovative financing options such as mezzanine financing and convertible debt.	High	Attainable	Effective; Boost Private Sector Confidence

Reform Area	Recommendation	Priority	Workability	Outcome
<b>Withholding Tax</b>	Equalize withholding tax rates for DFIs and Multilaterals; reduce withholding tax on interest payments.	High	Attainable	Effective; Boost Private Sector Confidence
<b>Investor Exit</b>	Clarify NRB policies for partial exits by foreign BFIs.	High	Attainable	Effective; Boost Private Sector Confidence
	Remove ambiguities regarding lock-in periods for foreign investors.	High	Attainable	Effective; Boost Private Sector Confidence
<b>Ease of Doing Business</b>	Develop a unified insolvency law with efficient restructuring and liquidation regimes.	High	Attainable	Effective; Boost Private Sector Confidence
	Amend civil procedure rules to fast-track commercial cases and injunctions.	High	Attainable	Effective; Boost Private Sector Confidence
	Strengthen commercial mediation and arbitration mechanisms.	High	Attainable	Effective; Boost Private Sector Confidence
	Amend Companies Act to enable online registration and decentralized services.	High	Attainable	Effective; Boost Private Sector Confidence

*Nepalese professionals are increasingly involved in providing consultancy services to international organizations and startups, often receiving compensation in the form of sweat equity—shares granted in exchange for services. However, the absence of a clear regulatory framework leads to legal and financial uncertainty.*

## **Establishing a Regulatory Framework for Sweat Equity in Foreign Company**

### **Proposed Action:**

*Regulators should formally recognize sweat equity arrangements and mandate that all proceeds from the sale of such equity, including capital gains, be repatriated to Nepal*

### **Expected Impact:**

*This policy will empower Nepalese professionals by legitimizing sweat equity as a mode of compensation, while simultaneously boosting the national economy through the inflow of repatriated funds.*

### **Decision needed**

*The Government of Nepal should publish a Gazette under Section 5, Subsection 2 of The Act Restricting Investment Abroad, 1964 (2021 BS) to create a regulatory framework for sweat equity.*

*The Gazette under Section 5, Subsection 2 should allow Nepalese firms and individuals to:*

***Sweat Equity Acceptance:*** Accept up to 40% of professional fees as sweat equity in exchange for services provided to foreign corporate entities or individuals, through technology transfer agreements or professional service agreements.

***Repatriation of Equity Proceeds:*** Mandate that all proceeds from the sale of sweat equity, including capital gains, must be remitted to Nepal after the closure of the deal.

***Cash Compensation:*** Require that 60% of the fees be received in cash, ensuring a balanced flow of monetary income alongside equity-based earnings.

Thank You!

Best regards,  
Kala Legal  
Protecting your creations

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