



# KALA LEGAL

## Economic Outlook Based on October 2025

### Abstract

At Kala Legal, we provide expert guidance to investors navigating evolving markets, helping them leverage opportunities while addressing legal and regulatory complexities.

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**Section 1 Overview 2024/25****1) The Political outlook****Nepalese Economy Post Gen Z Revolution**

Nepal stands at a critical juncture, facing simultaneous political and economic tests that demand both vision and discipline. The aftermath of the Gen Z protest has exposed deep structural weaknesses in governance, fiscal management, and institutional capacity. The country must now navigate a complex period of recovery and reform while preparing for national elections and its upcoming graduation from Least Developed Country (LDC) status in 2026.

**Political and Institutional Context**

On the political front, Nepal's foremost responsibility is to ensure that elections are held within the constitutional timeframe. However, the recent protests have left extensive damage: state facilities have been destroyed, administrative functions paralyzed, and public services disrupted. The lack of clarity among some political actors regarding participation in the electoral process risks undermining the credibility of the transition. To safeguard stability, consensus and broad-based engagement among political forces are essential.

Rebuilding institutions will take time and coordinated effort. Interim measures are needed to restore disrupted government functions even as longer-term reconstruction proceeds. This moment, though difficult, offers a crucial opportunity for decisive leadership and institutional renewal.

Referring to the recent youth-led protests, the IMF observed that "the political landscape in Nepal underwent a change with the youth-led protests — reflecting long-standing grievances related to corruption, governance, and inequality, which were exacerbated by subdued growth and limited job opportunities." The Fund further noted that high levels of emigration continue to constrain domestic demand and labor supply, weighing on medium-term growth prospects.

The World Bank's South Asia Development Update (2025) describes Nepal's situation as one of "deep frustration over governance and lack of economic opportunities," with youth unemployment at 22.7%, the highest in South Asia. Although hydropower, industry, and agriculture have shown resilience, the economy continues to be constrained by rising public debt, weak FDI inflows, and persistent trade imbalances.

To ensure stability and growth, Nepal must pursue coordinated reforms, strengthen institutional capacity, and commit to transparent and predictable governance. With unity, fiscal prudence, and clear communication, today's crises can become the foundation of resilience and renewal. The aspiration of the Nepali people, peace, fairness, and prosperity, must remain at the center of every decision in the days ahead.

**Economic and Fiscal Pressures**

On the economic front, fiscal pressures are mounting rapidly. The government's financing needs now far exceed its capacity, yet policy responses remain fragmented and largely reactive. Populist announcements made without a coherent framework have further amplified uncertainty. The absence of a comprehensive Business Recovery and Reconstruction Plan—along with incomplete damage assessments—continues to delay meaningful recovery efforts.

The private sector, facing losses estimated at over Rs. 100 billion in destroyed assets and 700 borrowers carrying Rs. 154 billion in outstanding loans, is urgently seeking regulatory relief and fiscal support. At the same time, the government requires reconstruction financing equivalent to roughly 12% of GDP—excluding private-sector needs. With revenue collection weakening and public spending capacity eroded, Nepal's GDP is estimated to have contracted by 3.5%, accompanied by declining investor confidence, reduced capital formation, and tighter credit conditions.

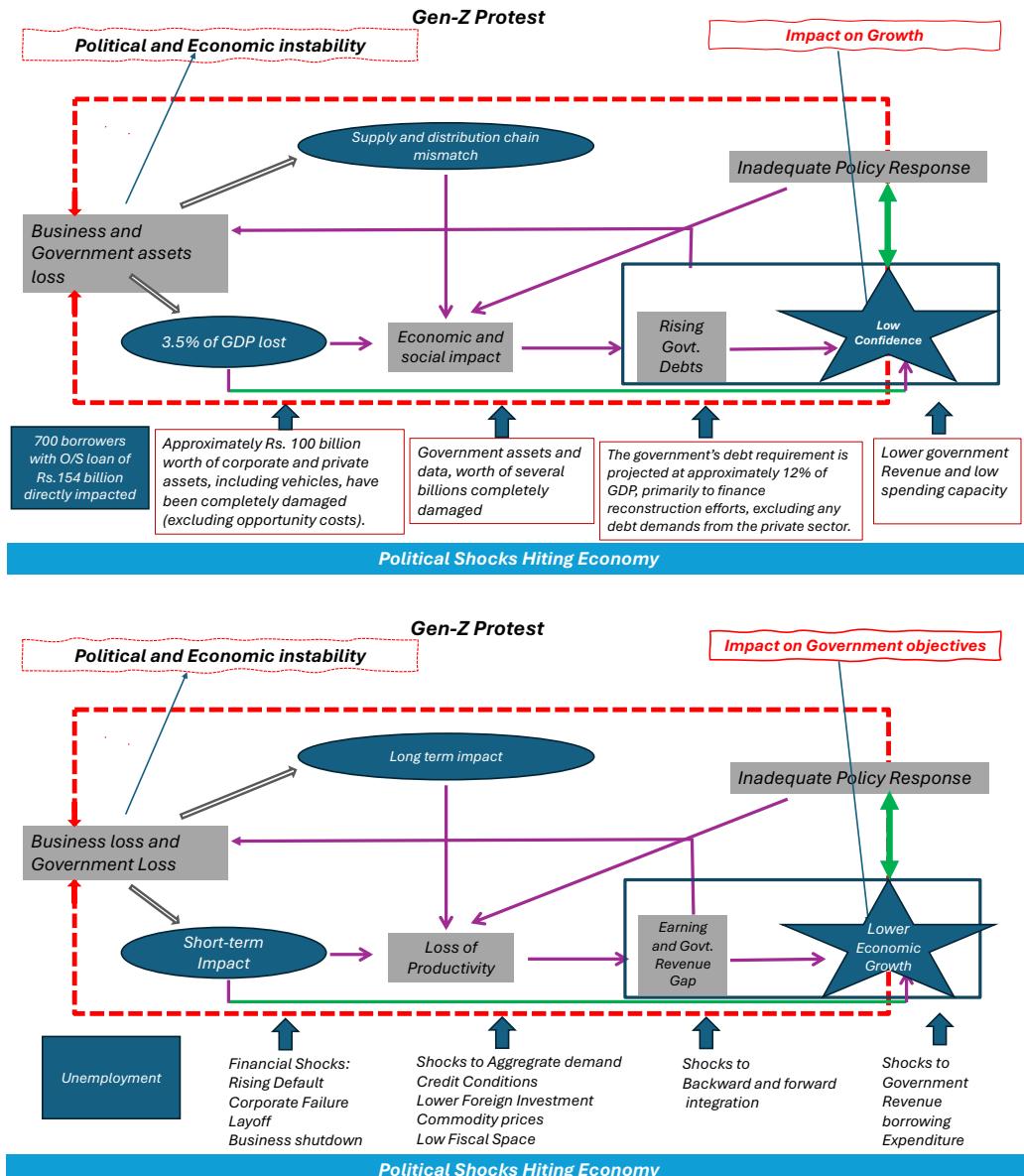
To navigate these overlapping pressures, the state must reallocate resources from fragmented or low-priority projects toward urgent needs—reconstruction, elections, and private-sector recovery. However, such reallocations carry risks of crowding out other sectors and dampening growth momentum. To strike an appropriate balance, the government should also pursue fiscal support from multilateral development agencies and friendly countries through concessional loans and targeted grants.

To build a more resilient and efficient financial system, several policy measures are essential for strengthening regulatory oversight, improving market discipline, and aligning Nepal's financial practices with international norms. A key step is lowering the credit-rating threshold to NPR 25 crore, which will enhance credit discipline and facilitate more accurate differentiation of borrower risk, helping prevent asset-quality deterioration. Harmonizing loan-loss provisioning norms with regional standards will further enhance regulatory clarity and credibility.

For more dynamic capital markets, policymakers could allow banks to participate more actively in the stock market without minimum holding-period requirements, while maintaining prudence through a 30% cap on exposure relative to regulatory capital. Revising the directed lending framework is also necessary to better align credit flows with national priority sectors. Simplifying regulations—such as abolishing the capital redemption reserve requirement for debentures and replacing the CD ratio mandate with a 20% minimum liquidity ratio—would improve liquidity management and ease capital-raising processes.

Additionally, provisioning norms for restructured loans should be reassessed, supported by a dedicated rating framework for such assets to ensure greater transparency and risk accuracy. Linking risk weights directly to credit ratings will further strengthen risk-based capital allocation and reinforce financial-sector resilience.

Collectively, these recommendations aim to support policymakers in shaping a modern, credible, and globally aligned monetary and financial regulatory environment—one that reinforces economic stability and enables sustainable, broad-based growth.

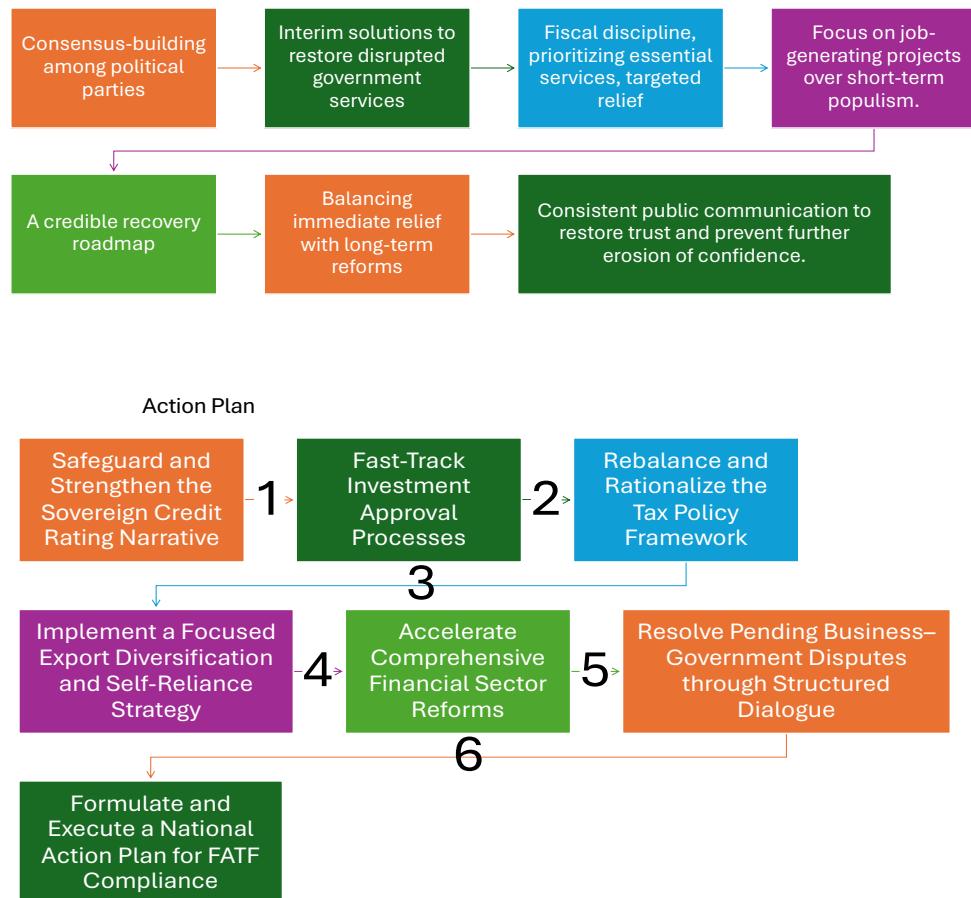


#### Policy Priorities and the Way Forward

The path forward requires a clear and credible Action Plan:

1. Consensus-building among political forces to ensure inclusive participation in the democratic process.
2. Interim solutions to restore government services during the reconstruction phase.
3. Fiscal discipline, focusing on essential services, targeted relief, and job-generating projects rather than short-term populism.
4. A credible recovery roadmap, balancing immediate relief with long-term reforms and communicated transparently to citizens and development partners.
5. Consistent public communication to rebuild trust and prevent further erosion of confidence.

## What is needed now?



### Financial Sector Resilience

The stability of the financial sector has emerged as a cornerstone of Nepal's economic recovery. The rise in loan defaults and credit stress following the Gen Z protest underscores the urgent need for systematic loan portfolio reviews, a reassessment of stringent asset classification norms, and better alignment of NPA management with regional standards. Revising the asset gradation framework and easing the 100% loan loss provision requirement—by extending it to a three-year period for continued NPAs—would help release trapped capital. This, in turn, would enable banks to deploy excess liquidity, issue new loans, and reinvigorate private-sector investment.

### 2) Background and Broader Economic Landscape

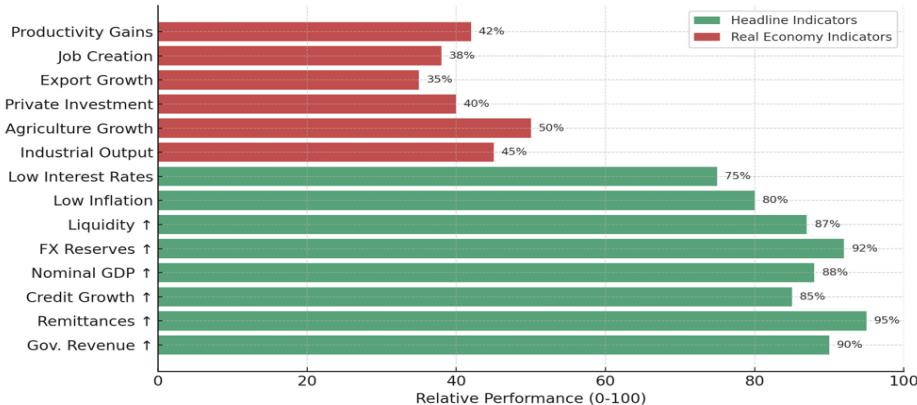
As of September 2025, Nepal's economic landscape presents a blend of opportunity and strain. The twin milestones of national elections and LDC graduation in November 2026 coincide with urgent reconstruction needs following political unrest and flash floods. Priority investments include repairing and upgrading roads, improving connectivity to emerging urban centers, enhancing local governance, developing alternative link routes to Kathmandu and major hubs, and expanding power transmission corridors. These ambitions will require trillions of rupees in infrastructure financing over the next decade.

Despite some positive macroeconomic indicators, stable revenue collection, stable remittances, and stable forex reserves and liquidity, the economy remains structurally weak. Policy execution, capital absorption, and institutional inefficiencies continue to limit broad-based growth. According to the World Bank assessments, GDP growth for FY 2025/26 is projected to grow at 2.1% far below the government's target of 6%. However, the IMF projects economic growth of around 5.2 percent in FY 2025/26, driven by higher capital expenditure, a rebound in domestic demand, and continued structural reforms. Inflation is expected to stay within the central bank's tolerance band (~5 percent). The medium-term

outlook remains positive, supported by the expansion of hydropower capacity, infrastructure investments, and improvements in private-sector competitiveness.

According to IMF economic momentum is expected to strengthen in FY 2025/26, supported by improved project execution, policy measures to boost business confidence, and accommodative credit conditions. Rising investment in physical infrastructure, continued tourism recovery, and increased hydropower exports will provide further impetus to growth. Inflation may rise slightly as demand strengthens but is expected to remain anchored near 5 percent.

### Nepal: Headline Strength vs. Real Economy Weakness



### 3) The roadmap: Prioritizing Economic Stability Amidst Uncertainty

In light of the interim government's mandate to conduct elections within six months and the ongoing political uncertainty, this roadmap offers a strategic approach to maintain economic stability, rebuild public confidence, and lay the groundwork for post-election recovery. The core principle is to prioritize stability, clarity, and fiscal discipline while avoiding policy shocks that could exacerbate existing unrest.

#### A. Immediate Actions (0-1 Weeks): Stabilize Confidence and Limit Downside

1. To prevent market panic and demonstrate fiscal discipline, the government should act swiftly. This phase focuses on clear, time-bound measures that signal a steady hand. Publicly Commit to a Short, Credible "Economic Stability Package": Commit publicly to a focused, time-limited set of measures to maintain economic steadiness. This should include:
  - a promise of no arbitrary new taxes before the elections.
  - Prioritized social cash transfers to the most vulnerable households.
  - A short list of "no-cut" capital projects that will proceed as planned.
  - An overarching economic recovery plan.

Rationale: This prevents market unrest, demonstrates fiscal restraint, and prioritizes aid for the most at-risk groups. It establishes a rapid response mechanism while upholding budgetary discipline.

Initial Steps: Release a one-page declaration outlining (a) no new arbitrary taxes until after elections, (b) targeted cash assistance for vulnerable families, (c) a select group of essential capital projects that will continue uninterrupted, and (d) an outline for economic revival.

2. Protect Foreign-Exchange Credibility and Social Safety Nets: Prevent hasty capital controls to maintain trust in reserves and support systems. Despite strong forex reserves, Nepal's dependence on remittances makes it vulnerable to shocks. The government must reaffirm its commitment to existing FX reserve management rules. Furthermore, it should top up targeted safety nets for food and energy in the poorest municipalities to avoid social distress.

Rationale: While foreign exchange reserves provide a solid buffer, reliance on remittances creates exposure to external disruptions; clear signaling is key to avoiding panic.

Initial Steps: Reaffirm guidelines for managing FX reserves and enhance safety nets for food and energy in the most impoverished areas.

3. Freeze Politically-Sensitive Large New Spending Commitments: To curb fiscal slippage, freeze major new spending. Simultaneously, frontload high-impact, quick-win capital expenditures that are "shovel-ready" and can create jobs immediately. Publish a short "priority list" of 5-7 such projects with clear timelines and budget allocations.

**Rationale:** Poor execution of capital budgets and fiscal overruns; focusing on job-creating, ready-to-start projects addresses these issues efficiently.

**Initial Steps:** Issue a brief "priority list" of 5–7 projects, including timelines and allocated funds, to fast-track implementation.

**Immediate Actions to Protect Financial Stability:** To calm depositors and markets, the Nepal Rastra Bank (NRB) and the Ministry of Finance should issue a joint statement. Issue assurances for smooth banking operations and enhanced monitoring. This statement should:

- a) Publicly guarantee that the banking system is under active monitoring.
- b) Reassure the public that depositors' interests are protected.
- c) Provide a clear timeline for an asset-quality review.

**Rationale:** Increasing non-performing loans and sector pressures are concerns; reassuring markets and depositors is essential to prevent instability.

**Initial Steps:** Coordinate a joint statement from the Nepal Rastra Bank (NRB) and Finance Ministry affirming (a) ongoing vigilant oversight of the banking system, (b) protection of depositor funds, and (c) a defined schedule for asset quality assessments.

#### B. During the Election Period (1-6 Months): Maintain Calm and Avoid Policy Shocks

The goal during the election period is to reduce political uncertainty and prevent it from becoming an economic drag.

1. **Announce a "Economic Continuity" Code of Conduct:** The interim government should convene ministers to endorse a three-point code of conduct. This pledge would reduce investor and consumer anxiety by committing parties to:
  - a) No abrupt fiscal changes.
  - b) No arbitrary expropriations.
  - c) Honoring existing Public-Private Partnership (PPP) and Alternative Investment Fund (AIF) contracts.

**Rationale:** Political volatility hampers growth; a shared commitment from key parties alleviates worries among investors and the public. Analyses point to instability as a primary barrier to confidence.

**Initial Steps:** Gather leaders from major political groups to endorse a simple 3-point pledge: no sudden fiscal shifts, no unwarranted asset seizures, and adherence to existing public-private partnership (PPP) and Alternative Investment Fund (AIF) agreements.

2. **Preserve the Rule of Law for Major Reforms:** To safeguard international credibility and investor confidence, the government must maintain momentum on key reform pipelines. This includes publishing progress milestones on Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) compliance and clarifying hydropower off-taker policy to signal continuity to investors.

**Rationale:** Maintaining international trust is vital; clear policies in hydropower are crucial for foreign direct investment (FDI).

**Initial Steps:** Share updates on AML/CFT progress and a concise policy statement on hydropower procurement to reassure investors of ongoing stability.

3. **Use Targeted Liquidity Support, Not Broad Loosening:** If financial stress spikes, the NRB and Treasury should prepare a contingency line to backstop critical lines of credit for small and medium enterprises (SMEs) and agriculture financing. Broad credit loosening could be misinterpreted as a sign of panic.

**Rationale:** Liquidity levels are ample, but borrowing demand is low; broad measures might signal distress. Assessments note surplus liquidity and ineffective policy transmission.

**Initial Steps:** Develop a backup facility (via NRB and Treasury) to support vital small and medium-sized enterprise (SME) credit and agricultural financing in case of sudden pressures.

#### C. Medium-Term Preparations (1-6 Months): Build a Foundation for Post-Election Recovery

This period should focus on preparing a credible and well-structured plan that the next government can inherit.

1. **Protect the Sovereign Rating Narrative:** To improve Nepal's sovereign rating, the government should publish a six-month "reform calendar." This calendar should outline the explicit sequencing of reforms, such as improvements in tax administration, steps toward setting up an independent fiscal council, and a timetable for the asset-quality review.

**Rationale:** Nepal's fundamentals support potential rating upgrades, but governance and AML issues hinder progress; a clear plan can improve perceptions.

Initial Steps: Release a 6-month "reform schedule" covering tax system enhancements, steps toward an independent fiscal council, and timelines for asset reviews.

2. Fast-Track the Alternative Investment Fund (AIF) and Nepal Development Fund: The AIF is a critical tool for mobilizing long-term capital, especially from the Nepali diaspora (NRNs). The government should fast-track its establishment while ensuring strong governance safeguards. This includes publishing a governance whitepaper outlining board composition and conflict-of-interest rules

Rationale: The AIF is key for channeling long-term funds, especially from non-resident Nepalis (NRNs), into infrastructure, but strong governance is essential for success.

Initial Steps: Draft and publish a governance framework (including board structure, conflict-of-interest protocols, and ESG standards) and begin consultations with stakeholders.

3. Rebalance Tax Policy: To support long-term investment and reduce dependence on import-based revenue, the government should publish a roadmap for tax structure reform. While avoiding immediate hikes, this plan should detail a gradual move toward a broader Value Added Tax (VAT) base and strengthened digital tax collection capacity.

Rationale: Excessive dependence on trade duties is a vulnerability; reforms should promote investment through broader revenue sources.

Initial Steps: Issue a phased plan (deferring any increases until post-elections) to expand the VAT base, reduce inefficient trade tariffs, and improve digital revenue collection.

4. Push a Focused Export Diversification and Self-Reliance Package: The interim government should launch a 90-day public-private task force to identify three key export value chains, such as agro-processing, ICT services, and hydropower-linked exports, and develop a prioritized action plan.

Rationale: Building resilience through agro-processing, service exports (e.g., ICT, education, health tourism), and expanded hydropower capacity.

Initial Steps: Form a 90-day joint public-private task force to pinpoint 3 priority export chains and develop an action plan addressing regulations, logistics, and financing.

5. Accelerate Financial Sector Reforms: Publish a clear timeline for the Loan Portfolio Review (LPR) and commit to milestones for amending the NRB Act. This demonstrates a commitment to strengthening the financial sector's foundation before considering more complex measures like an Asset Management Company.

Rationale: Aligning with IMF requirements and analyses, emphasis is on LPR execution, NRB Act revisions, and sequenced reforms for asset recovery.

Initial Steps: Announce LPR timelines with designated experts, set milestones for NRB Act changes, and test expansions of secured-transaction registries.

#### D. Communication and Governance: A Short Playbook

Use Plain, Regular Updates: The Treasury and NRB should release weekly statements on key performance indicators (KPIs) like foreign exchange reserves and treasury balances to rebuild public trust.

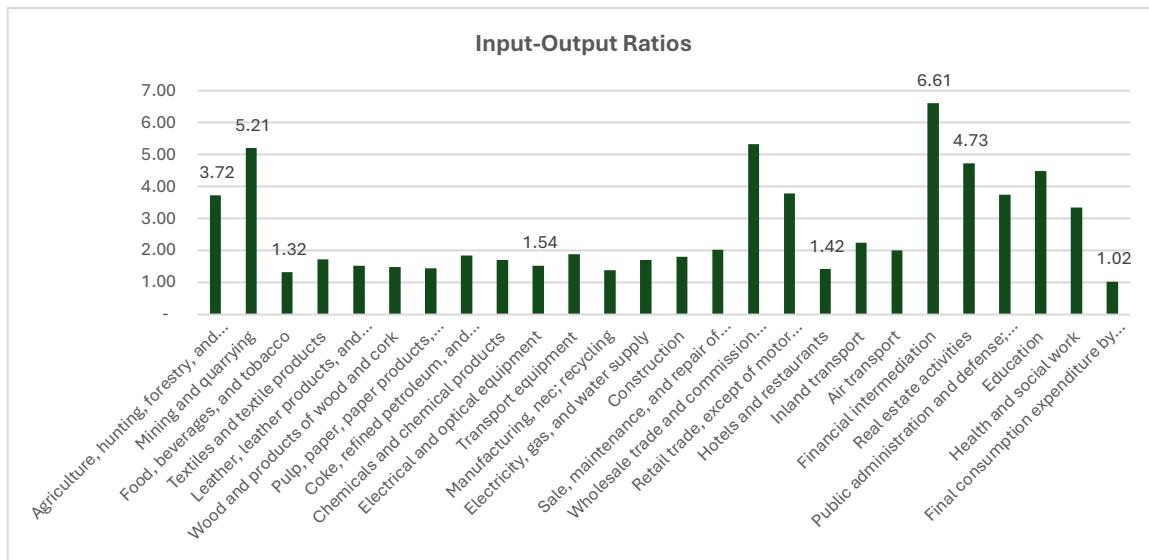
Launch a Transparent "Election-Period Economic Monitoring Cell": This small cell, comprised of a senior civil servant, an independent economist, and private sector representative, would pre-clear any major fiscal decisions, thereby reducing the risk of ad-hoc policymaking.

#### E. Quick Risk Checklist for Ministers:

- a) Do not use economic restrictions as a political shield.
- b) Avoid big policy reversals.
- c) Keep AML/CFT momentum visible to protect market access.

By following this roadmap, the interim government can effectively navigate the period of political uncertainty, reassure citizens and markets, and hand over a stable and credible foundation to the next elected government.

## 4) Input-Output



Nepal's Input-Output chart provide a snapshot of the economy's production, consumption, and trade linkages. Analysis of sectoral output, household demand, exports, imports, and value-added reveals both structural strengths and vulnerabilities. These findings are critical for designing strategies that boost resilience, promote self-reliance, and diversify exports in alignment with Nepal's long-term growth agenda.

## A. Key Findings

## 1) Structural Strengths

- a) Large Output Sectors: Agriculture, Construction, Wholesale Trade, Financial Services, Retail Trade, and Public Administration dominate total output. Together they account for more than half of national production.
- b) Household-driven Demand: Most sectors are highly consumption-oriented, with household demand contributing 40–70% of output in services, retail, and agriculture.
- c) Value-Added Intensity: Sectors like Real Estate, Financial Services, Business Services, and Education show high value-added shares (60–80%), indicating strong domestic contribution with limited import dependency.

## 2) Vulnerabilities

- a) High Import Dependence: Air Transport, Petroleum, Chemicals, and Electricity show import shares exceeding 30–50% of output, exposing the economy to external price shocks.
- b) Weak Export Orientation: Exports remain small relative to output (generally <10%), except for Food & Beverages, Transport Services, and selected manufacturing subsectors.
- c) Low Investment Penetration: Except for Construction (which absorbs large GFCF flows), most industries show minimal investment shares—suggesting undercapitalization.
- d) Agriculture Paradox: While Agriculture contributes the largest share of output, its value-added intensity is declining, and productivity growth is weak compared to services.

## B. Other Major issues

## A. Heavy Reliance on Remittances Without Productive Reinvestment

Remittances increased 29.9 percent in NPR terms and 25 percent in USD terms. Remittance inflow was Rs.177.41 billion in the first month of 2025/26, bolstering forex reserves and liquidity. However, these inflows mainly support consumption and imports, not productive investments in manufacturing or infrastructure, perpetuating a "remittance trap." Though growth has improved from prior years' highs (e.g., 25%+ in 2024/25), amid global uncertainties and fewer migrant departures, risking reserve erosion. This contributes to high informal employment (82%) and brain drain, limiting domestic job creation despite poverty reduction.

## B. Rising Financial Sector Stress from Non-Performing Loans

Private sector credit grew by 7.79% (Rs. 402 billion) by mid-August 2025, focused on Communications and Energy (15.4%) Service Industries (12.79) consumables (13.63%) and construction (11.25%). Yet, NRB data lacks specific NPL figures for different sectors, while earlier trends indicate rising NPLs (4.4–4.9% in Q1-Q2 FY 2024/25), with provisions at 4.62–5.41% and potential additional needs of Rs. 250–285 billion. This signals borrower distress from low demand and post-pandemic effects, eroding bank capital and curbing lending despite excess liquidity (NRB absorbed Rs.3,638.35 billion via auctions).

### C. Low Inflation and Interest Rates Indicating Weak Demand

CPI inflation stood at 1.47 % y-o-y in mid- October 2025 (down from 3.82% corresponding previous year), with food inflation eased at negative 2.54% and non-food increased at 3.80%. Mid-year estimates project 1.40 -2.00% for FY 2025/26 (vs. 5.5% target), but volatility in food prices (negative 15% to 7% spikes) pressures vulnerable groups. Interest rates declined: lending at 7.50% (from 9.33%), deposits at 3.85% (from 5.23%), interbank at 2.75%. These lows reflect subdued activity, low confidence, and migration-driven demand weakness, not robust growth, with unemployment at 15-20%.

### D. Inefficient Fiscal Management and Spending Shortfalls

Government revenue reached Rs.253 billion (tax Rs. 249 billion, non-tax Rs. 4 billion), up 0.07 % y-o-y.

### E. Vulnerability to External Shocks and Limited Diversification

Gross foreign exchange reserves increased 18.65 percent to Rs. 3,112 billion in mid-September 2025 from Rs. 2,677 billion in mid-July 2025. In the US dollar terms, the gross foreign exchange reserves increased 8.7 percent 21.20 billion in mid-July 2025 from to 19.5 billion in mid-July 2025. Yet, reliance on remittances and foreign loans exposes to shocks like disasters and Gen Z protest (3.5% GDP damage in 2025/26 floods) and trade issues. GDP growth for FY 2025/26 is estimated at the range of 1-2% (vs. 6% target), with NSO data showing uneven sectors: agriculture and industry up modestly, services lagging due to tourism slowdowns. Low FDI (<0.5% GDP), FATF Grey List status, and political instability hinder diversification.

### Overall Economic Challenges and Recommendations

Combined data show stability (e.g., current account surplus Rs. 409 billion, low inflation) but underline underperformance: slower recovery, revenue/expenditure shortfalls and implementation gaps. Kala recommends prudent fiscal policies, stronger oversight, inflation controls via monetary tools, and initiatives like NRN investments and sectoral plans (IT, agriculture) to boost confidence, attract FDI, and achieve 4.4-5.1% growth in 2025/26.

Indicator	Up to (Mid- October 2025)	Review (FY 2025/26 Projections)	Why It Doesn't Translate to Improvement
Government Revenue	Rs. 253 billion (+0.7% y-o-y)	14,800 (32.4% increase from actual collections)	Shortfalls due to inefficiencies; Low capital spending (under 60% of budget) limits impact on infrastructure and jobs.
Remittances	Rs. 335 billion (+36% y-o-y)	Stable trends noted	Supports consumption, not investment; deceleration risks reserves.
Private Sector Loans	+7.14% y-o-y (Rs. 377 billion)	12% y-o-y (Monetary Policy target)	Offset by rising NPLs (4.4-4.9%), restricting expansion.
Bad Loans (NPLs)	5.26%	~4.23%	Indicates borrower distress and banking risks, curbing credit expansion. Borrower distress erodes banking stability.
GDP Growth		1.5 % (vs. 6% target)	Modest and uneven; reliant on volatile sectors, not broad-based. Uneven sectors; below pre-pandemic levels.
Forex Reserves	Rs. 3,113 billion (+18.65 %) from mid-July 2025	~Rs. 1,060 billion (Monetary Policy target to cover 7 months imports)	Vulnerable to remittance slowdowns/shocks. Driven by remittances; vulnerable to external shocks and declining inflows.
Liquidity	Excess absorbed Rs. 13,075.95 billion	High (Rs. 2,007-15,355 billion)	Weak demand prevents productive credit flow. Leads to low rates but weak demand prevents investment.
Interest Rates	Lending 7.50%, Deposit 3.85%, Interbank 2.74%	Lending 7.4-8.5%, Deposit 4.19-3.78%	Reflects stagnation, not vibrancy. Reflects low demand, not vibrancy; doesn't spur borrowing amid risks.
Inflation	3.80 % (CPI), Food -2.54 %	1.8 -3.6% (est.), Food likely to spikes 4.99%	Signals weak activity; volatility affects poor. Food prices still pressure vulnerable groups.

### F. Policy Priorities

#### 1. Enhancing Self-Reliance

- Economic recovery: The recent loss of public and private assets due to political unrest and flash floods has underscored the urgency of rebuilding administrative systems, restoring private sector confidence, and addressing critical infrastructure needs.
- Energy Security: Prioritize domestic hydropower and renewable generation to reduce import dependency in petroleum and electricity.

- c. Chemical & Fertilizer Industries: Develop localized production capacity to reduce reliance on imports critical for agriculture and manufacturing.
- d. Transport Linkages: Invest in domestic maintenance and aviation service facilities to reduce the foreign exchange drain from air transport.

## 2. Export Diversification

- a. Agro-processing and Food Industries: Strengthen value chains in high-potential products (tea, coffee, spices, processed food) for regional markets.
- b. Service Exports: Expand ICT, business services, and higher education exports, leveraging Nepal's skilled youth.
- c. Tourism & Air Transport: Position aviation and hospitality as bundled export services, supported by quality and regulatory upgrades.

## 3. Investment Mobilization

- a. Infrastructure-focused Capital Formation: Channel GFCF into construction, logistics, and energy infrastructure to crowd in private investment.
- b. Alternative Investment Funds (AIFs): Expand capital market instruments to attract diaspora financing into productive sectors.
- c. Sector-specific Incentives: Introduce fiscal and credit support for industries with high value-added and export potential.

## G. Strategic Recommendations

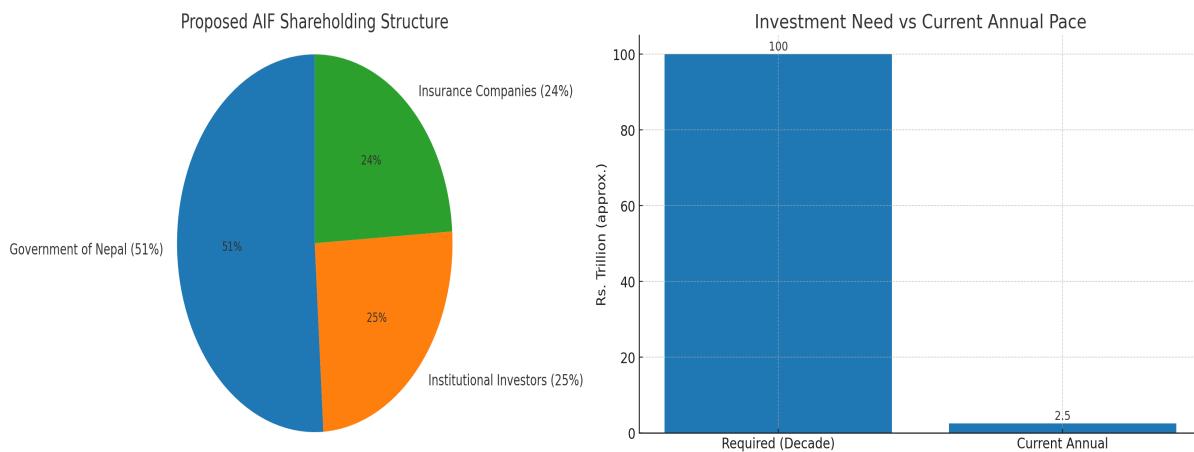
Priority Area	Recommended Action	Expected Impact
Economic recovery	Rebuilding administrative systems, restoring private sector confidence, and addressing critical infrastructure needs.	Expected Government Debts requirement 12% of GDP for reconstruction (excluding private sector debts demand)
Energy & Petroleum	Scale hydropower, introduce biofuels, reduce petroleum imports	Lower trade deficit, energy security
Manufacturing	Develop agro-processing, chemical & fertilizer plants	Higher self-reliance, export base expansion
Services	Promote ICT, education exports, health tourism	Diversified export portfolio
Agriculture	Boost productivity through inputs, irrigation, and storage	Reduce food imports, improve food security
Investment Climate	Expand blended finance, AIFs, PPPs	Mobilize private and diaspora capital
Trade Policy	Negotiate market access under NTPP and SAFTA	Enhance export competitiveness

Nepal's input-output structure highlights a household-driven, import-sensitive economy with limited export diversification. Strategic reforms must focus on reducing import dependency in critical sectors, expanding export-ready industries, and mobilizing investment for productive transformation. A coordinated push across energy, agro-processing, services, and infrastructure will create resilience and unlock Nepal's growth potential.

## 2) The proposed Alternative Investment Fund (AIF) Act and Nepal Development Fund

The proposed Alternative Investment Fund (AIF) Act seeks to establish a sovereign-backed financing institution to mobilize long-term capital for Nepal's large-scale development and infrastructure projects. With an authorized capital of Rs. 100 billion and an initial paid-up capital of Rs. 25 billion, the Fund will be structured with majority ownership (51%) by the Government of Nepal, complemented by contributions from institutional investors such as the Employees' Provident Fund, Citizens' Investment Trust, Social Security Fund (25%), and insurance companies (24%). Over time, the state's shareholding will gradually dilute to encourage greater private and foreign participation. The AIF is designed to bridge the country's vast financing gap, as Nepal requires investments exceeding Rs. 100 trillion in the coming decade, while current annual flows remain limited to Rs. 2-3 trillion. To achieve this, the Fund will mobilize resources through equity, debt, blended finance instruments, bonds, debentures, guarantee schemes, pooled "fund of funds" models, and a dedicated Remittance Investment Fund targeting NRN and migrant savings. Investments will prioritize sectors such as energy generation, transmission and distribution, transport infrastructure (roads, railways, tunnels, airports, ropeways), industrial zones and SEZs, urban development, IT and digital economy projects, tourism, and other high-return ventures with strong employment and economic multipliers. However, the Fund will exclude projects below Rs. 1 billion, those with weak financial viability, or those involving conflicts of interest.

The AIF will operate as an autonomous statutory body with a Board of Directors chaired by the Finance Secretary and include representatives from key ministries, institutional investors, insurers, and independent experts, while its operations will be managed by a Chief Executive Officer supported by specialized subcommittees on investment, audit, and risk management. Strong governance, due diligence, conflict of interest disclosure, and adherence to ESG principles will guide its operations. Strategically, the AIF is envisioned as a transformative financing mechanism to complement traditional banking, reduce Nepal's infrastructure financing gap, attract private and foreign capital including NRN investments, and support national priorities such as the 16th Plan's target of generating 40,000 MW of electricity. Ultimately, the Act aims to provide Nepal with a sustainable, long-term investment platform to drive economic growth, employment generation, and structural transformation.



### 3) Briefing Note for Sovereign Rating

Nepal's macroeconomic fundamentals provide a strong case for a notch rating improvement. Our foreign exchange reserves cover more than 15 months of imports, public debt remains moderate at below 45% of GDP with a highly concessional structure, and remittances—over 25% of GDP, continue to provide a stable cushion for the external sector. Inflation is under control, banking system liquidity is stable, and medium-term growth prospects are supported by hydropower exports, services, and infrastructure investment.

We acknowledge that qualitative overlays, particularly FATF Grey List status and governance concerns, weigh on the assessment. However, these are being addressed through a high-level compliance roadmap and governance reforms. Our immediate focus is to demonstrate fiscal discipline, strengthen financial sector oversight, and advance export diversification. The key message for Fitch is that Nepal's quantitative resilience, combined with ongoing reforms, warrants a more favorable risk assessment. A notch upgrade would align the rating with the country's macroeconomic fundamentals and reinforce investor confidence.

#### A. Fitch Affirms Nepal at 'BB-'; Outlook Stable.

Fitch Ratings has affirmed Nepal's Long-Term Foreign-Currency Issuer Default Rating (IDR) at 'BB-' with a Stable Outlook. This marks the second consecutive year Nepal has received this rating.

#### B. Key Rating Strengths:

The rating affirmation and Stable Outlook are primarily supported by:

1. Low Debt Burden: Nepal maintains low government and external debt burdens, with external debt being on highly concessional terms (long maturities and low interest rates). Government debt is forecasted to stabilize around 46% of GDP, which is below the 'BB' peer median.
2. Strong External Liquidity: The country boasts robust foreign exchange reserves, which provide a significant liquidity buffer against external vulnerabilities. Reserves covered an impressive 13.5 months of current external payments in FY25, far exceeding the 'BB' peer median.
3. Medium-Term Growth Prospects: Nepal has solid medium-term growth potential, largely anchored by continued investment and development in the hydropower sector.
4. External Creditor Position: Nepal maintains a net external creditor position.

#### C. Key Rating Constraints (Why the Rating is not Higher)

The rating is constrained by structural and cyclical weaknesses, including:

1. Underdeveloped Economy: The economy is considered underdeveloped and vulnerable to external shocks and natural disasters.
2. Weak Structural Features: Nepal lags behind 'BB' category peers in terms of structural features, such as low GDP per capita and weaker governance metrics.
3. Political Uncertainty: Lingering political uncertainty following a period of youth-led unrest and the installation of an interim government poses risks to economic and fiscal stability. While elections are scheduled for March 2026, delays or a more fragmented political landscape could undermine policymaking effectiveness.
4. Economic Slowdown: Real GDP growth is forecasted to slow to 2.5% in FY26 (from 4.6% in FY25) due to the disruption from the recent unrest, depressed sentiment, and poor agricultural output.
5. Fiscal Widening: The federal deficit is projected to widen to 3.5% of GDP in FY26 (from 1.7% in FY25) due to subdued revenue collection and increased spending on reconstruction and upcoming elections.
6. Banking Sector Vulnerabilities: Financial soundness indicators are weakening, with Non-Performing Loans (NPLs) rising to 5.2% of gross loans in FY25.

#### D. Future Rating Sensitivities

1. Potential for Upgrade: An upgrade could be supported by sustained strong economic growth, improved governance standards, and successful revenue mobilization.

2. Potential for Downgrade: The rating could come under pressure if political instability deepens, governance standards deteriorate, or external financing weakens.

#### E. Nepal Fiscal Risk Statement and Strategies 2025

The Fiscal Risk Statement (FRS) 2025, published by the Ministry of Finance, highlights potential deviations in fiscal outcomes due to macroeconomic shocks, specific contingent liabilities, and institutional weaknesses. It uses the IMF Fiscal Risk Assessment Tool (FRAT) to quantify risks and propose mitigation strategies.

##### 1. Macroeconomic Risks

Indicator	Avg. Value	Std. Dev. / Volatility	Fiscal Impact	Risk Level
GDP Growth	4%	±2.7 pp	-0.7% of GDP revenue loss; +3.2 pp debt increase	Medium
Inflation	6.9%	±2.2%	Medium (higher spending, slightly higher revenues)	Medium
Interest Rate	7–8% (domestic)	~1% change sensitivity	+0.2% of GDP cost if rates rise 1%	Low
Exchange Rate	4.3% volatility	Moderate	Limited (due to concessional debt)	Low
Debt-to-GDP	22.7% (2016/17) → 42.7% (2023/24)	Projected ~50% by 2028/29	Stable; low distress risk	Low

Mitigation Tools: borrowing limits (5.5% of GDP for domestic debt), medium-term expenditure framework (MTEF), fiscal rules, debt ceilings, stabilization funds.

##### 2. Specific Risks

###### i) Forecasting Errors

Indicator	Forecast Error	% of GDP	Risk Assessment
Tax Revenue	NPR 550 bn/yr	7.2%	High, Probable
Foreign Grants	~50% over-forecast	1.5–2%	Medium, Probable

Mitigation: better analytics, independent reviews, fiscal buffers.

###### ii) Natural Disasters

Event	Frequency	Fiscal Cost	Risk Assessment
Floods/Landslides	Frequent	Up to 2% of GDP	Low Impact, Probable
Earthquakes	Infrequent	22.8% of GDP (2015)	High Impact, Possible

Mitigation: disaster funds, insurance, resilient infrastructure, contingency financing.

###### iii) Sub-National Governments (SNGs)

Risk Indicator	Value	Notes
Dependence on federal transfers	>75% revenue	Structural
Spending execution gaps	Significant underspending	Development delays
Outstanding arrears	NPR 2.7 bn (provinces), NPR 7.3 bn (local)	Fiscal burden

Mitigation: Sub-National Government (SNG) Fiscal Risk Monitoring System, Sub-national Treasury Regulatory Application (SuTRA), better Public Financial Management (PFM), borrowing limits.

###### iv) Government Guarantees

Item	Value	% of GDP	Notes

Outstanding Guarantees	NPR 51.6 bn	0.9%	Mostly Nepal Airlines
Potential Calls	NPR 7 bn/yr	0.1%	Low likelihood

Mitigation: 1% of GDP ceiling, guarantee fees, monitoring, contingency reserves.

v) Public Enterprises (PEs)

Item	Value	% of GDP	Notes
Total Assets	NPR ~3,000 bn	51%	Large footprint
Total Liabilities	NPR ~1,950 bn	33%	High exposure
Net Fiscal Flow (2 yrs)	NPR 102.5 bn positive	-	Mixed performance
Loss-Making PEs	Nepal Airlines, NEA (intermittent)	Medium risk	

Mitigation: restructuring, PPP revival, stronger governance, digital reporting.

vi) Public–Private Partnerships (PPPs)

Indicator	Status	Risk
Active PPPs	Limited portfolio	Low
Risks	Weak structuring, capacity gaps, disclosure issues	Emerging

Mitigation: PPP law, transparent procurement, registry, risk-based fees.

3. Institutional Risks

Risk Factor	Assessment	Mitigation
Forecasting Errors	High impact, probable	Strengthen models, independent review, fiscal buffers
Public Financial Management (PFM)	Weak execution, arrears	PFM reforms, digital systems
Intergovernmental Coordination	Gaps in fiscal rules	Harmonized frameworks, monitoring

4. Consolidated Risk Matrix

Risk Category	Impact	Likelihood	Overall Rating
GDP Volatility	Medium	Possible	<b>Moderate</b>
Inflation	Medium	Possible	<b>Moderate</b>
Interest Rate	Low	Possible	<b>Low</b>
Exchange Rate	Low	Remote	<b>Low</b>
Debt	Low	Remote	<b>Low</b>
Forecast Errors	High	Probable	<b>Critical</b>
Floods/Landslides	Low	Probable	<b>Moderate</b>
Earthquakes	High	Possible	<b>Critical</b>
Sub-National Governments	Low	Low	<b>Low</b>
Guarantees	Low	Remote	<b>Low</b>
Public Enterprises	Medium	Possible	<b>Moderate</b>
PPPs	Low	Remote	<b>Low</b>

## 5. Fiscal Risk Statement 2025 – Nepal

Risk Area	Key Challenges	Policy & Structural Reforms	Lead Agency	Success Metrics (by FY26/27)
Macroeconomic & Debt	GDP growth volatility ( $\pm 2.7$ pp), inflation ~7%, debt rising to ~50% GDP	Amend Financial Procedures and Fiscal Responsibility Act 2019 with fiscal rules & buffer fund Annual The Medium-Term Debt Management Strategy (MTDS) with risk limits Extend yield curve, smooth redemptions	MoF, NRB, Parliament	Buffer $\geq 0.5\%$ GDP Debt stable $\leq 50\%$ GDP
Forecasting & Institutional	Tax forecast error NPR 550 bn (7.2% GDP); optimistic grants	Create Independent Fiscal Council Publish forecast error report Use real-time digital tax/customs data	MoF, IRD, NPC	Tax forecast error $< 5\%$ (MAPE) Public forecast reports published
Natural Disasters & Climate	Floods (~2% GDP), Earthquakes (2015: 22.8% GDP loss)	Adopt Disaster Risk Financing (DRF) strategy (buffers, Catastrophe Deferred Drawdown Option (Cat-DDO), insurance) Climate-proof all new projects Disaster contingency fund	MoF, National Disaster Risk Reduction and Management Authority (NDRRMA), NPC	Emergency funds disbursed $< 14$ days 80% projects climate-screened
Sub-National Governments	High transfer dependence, arrears (NPR 10 bn+)	Issue uniform SNG fiscal rules & debt registry Roll out SuTRA 2.0 with commitment controls	MoF, Financial Comptroller General Office (FCGO), Ministry of Federal Affairs and General Administration (MoFAGA)	Arrears $< 0.1\%$ GDP Capital execution $> 85\%$
State-Owned Enterprise (SOE) & Contingent Liabilities	SOE liabilities 33% GDP, weak governance; guarantees NPR 51.6 bn	Pass SOE Governance Act (boards, IFRS audits) Restructure loss-making SOEs (Nepal Airlines) Guarantee ceiling 1% GDP, risk-based fees	MoF Public Enterprises Division (PE Division), IBN	$> 90\%$ SOEs NFRS-audited Net fiscal flow positive Guarantee provisions $\geq 60\%$ of expected losses
PPPs & Public Investment	Weak structuring, hidden liabilities	Amend PPP Act with Value for Money (VfM) & affordability caps Establish PPP Unit & Project Preparation Facility (PPF)	IBN, MoF, NPC	100% PPPs VfM-tested PPP liabilities $< 0.5\%$ GDP

## F. World Bank November 2025 Economic Performance and Outlook

### 1. Recent Developments (FY25)

1. Economic Growth: Real GDP growth picked up to 4.6% in Fiscal Year 2025 (FY25), recovering from 3.7% in FY24. This rebound was driven primarily by industrial sectors like manufacturing, construction, and hydropower generation.
2. Inflation and Monetary Policy: Headline inflation declined to 4.1% in FY25, falling below the Nepal Rastra Bank's (NRB) 5% ceiling.
3. External Sector and Reserves: The current account surplus widened significantly to 6.7% of GDP in FY25, driven by record-high remittance inflows (28.2% of GDP). This contributed to robust foreign exchange reserves, which reached an import coverage of 15.4 months.
4. Fiscal and Financial Status: The fiscal deficit narrowed to a nine-year low of 2% of GDP. However, the domestic financial sector saw Non-Performing Loans (NPLs) climb to 4.6%.

### 2. Economic Outlook and Challenges (FY26-FY27)

- Projected Growth Slowdown: Real GDP growth is projected to slow sharply to 2.1% in FY26 in the baseline scenario, reflecting the impact of recent unrest and heightened political and economic uncertainty.
- Recovery: Growth is expected to recover to 4.7% in FY27, supported by reconstruction efforts.
- Fiscal Position: The fiscal deficit is projected to widen to 2.8% of GDP in FY26, due to increased spending for reconstruction, elections, and outstanding liabilities.
- Debt: Public debt is projected to increase to 45.2% of GDP in FY26 but is expected to stabilize thereafter, keeping Nepal at low risk of debt distress.

### 3. Key Downside Risks and Upside Potential

The outlook is subject to mixed risks, which include:

#### 1. Key Downside Risks

- Climate and Political Instability:** A rising frequency of natural disasters and persistent political uncertainty could continue to weigh heavily on economic activity.
- Financial Sector Strain:** The domestic financial sector is vulnerable to higher Non-Performing Loans (NPLs).
- International Compliance Issues:** Nepal's continued presence on the Financial Action Task Force (FATF) Grey List poses a risk to international financial dealings and investor confidence.
- Infrastructure Damage:** Damage to public infrastructure from natural disasters or other factors could lead to disruptions to essential public services and core administrative processes.

#### 2. Upside Potential

- A stronger economic recovery is possible if a successful political transition occurs and the government implements sustained macroeconomic management policies. These factors could significantly strengthen investor sentiment and support economic growth.

### 4. Special Focus: Reforms to Accelerate Public Investment

The special focus chapter addresses the structural challenge of persistently low execution of infrastructure projects, which has constrained growth and led to a deterioration of the public capital stock. Consolidated capital spending stood at only 7.9% of GDP in FY24, below the country's estimated infrastructure needs of 10%–15%.

The report identifies and provides recommendations for key bottlenecks in Public Investment Management (PIM) at the federal level:

- Project Readiness: Long delays in processes like:
  - Tree Cutting Clearances: Typically take 22–24 months, partly due to manual surveys and poor quality of Environmental Impact Assessments (EIAs).
  - Land Acquisition: Takes an average of two to three years due to inefficient processes and valuation disputes.
- Budget Execution:** Capital expenditure execution remains sluggish and is heavily concentrated at the end of the fiscal year (over half of capital spending occurred in the final quarter in FY25), raising concerns about project quality.
- Procurement: Nepal has the highest average procurement processing time in the South Asia Region, taking an average of 231 business days for World Bank-funded contracts.

The report recommends implementing the reforms proposed by the High-Level Economic Reform Commission to address these structural issues, focusing on accelerating public capital investments, simplifying tax policy, and tackling corruption.

### G. The World Bank Country Partnership Framework (CPF) for Nepal (FY2025–2031)

Theme	Key Data / Facts	WBG Strategic Focus / Outcomes
Fiscal Policy	Trade taxes: 45% of tax revenue- Fiscal deficit: ~6% of GDP (FY2023)	Improve tax base- Strengthen public financial management- Reform intergovernmental fiscal transfers
Monetary Policy	Inflation target: 6.5% (actuals exceeded in recent years)- Weak monetary transmission	Support macroeconomic stability- Develop financial infrastructure- Promote credit access
Industrial Policy	Export stagnation- Manufacturing shrinking- FDI limited	Business environment reform (DPC)- Support private investment- Target tourism, hydropower, digital sectors
Health	25% of children stunted- Gender gaps in access remain	Integrate health into climate and resilience agenda- Strengthen health delivery at subnational levels

Theme	Key Data / Facts	WBG Strategic Focus / Outcomes
Climate Change	2nd most hazard-prone country globally- Forest cover rose to 46% (2022)	Promote green energy & hydropower- Build resilient infrastructure- Expand climate-smart financing
Education	1/3 of workforce lacks primary education- Youth NEET: 35% (47% for females)	Support quality education- Promote digital & vocational training- Strengthen school-to-work transition
Employment	82% informal employment- Women's labor participation: 24% (vs. men's 53%)	Enhance access to jobs via private sector- Promote gender inclusion- Support MSMEs and digital services
Poverty Reduction	Poverty: 0.37% (int'l extreme poverty line), 20% (national poverty line)- High in Karnali, Sudurpaschim	Reduce regional disparities- Build social protection systems- Promote jobs-led growth

The World Bank Country Partnership Framework (CPF) for Nepal (FY2025–2031) outlines a strategic vision focused on two major development challenges: generating employment-driven growth and building resilience to natural disasters and climate change. The CPF identifies key areas for intervention under four broad policy domains: fiscal policy, monetary policy, industrial policy, and health.

Under fiscal policy, the CPF highlights that Nepal's public finances remain vulnerable, with nearly 45% of tax revenue derived from trade taxes, making it highly susceptible to external shocks. The fiscal deficit peaked near 6% of GDP in FY2023, largely due to import restrictions. The CPF recommends broadening the tax base, strengthening public financial management, and ensuring debt sustainability, with the current debt standing at about 43% of GDP (mostly concessional). It also promotes improved capital expenditure effectiveness and fiscal decentralization, especially at the provincial and local levels, through collaboration between the World Bank and ADB.

On monetary policy, the CPF supports macroeconomic stability and advocates for more flexible exchange rate management and enhanced monetary transmission mechanisms. Despite Nepal Rastra Bank's inflation target of 6.5%, actual inflation has remained persistently above this level. The CPF emphasizes strengthening financial infrastructure, including secured lending frameworks and credit reporting systems—to bolster investment and consumption.

Regarding industrial policy, Nepal faces stagnation in the manufacturing sector and weak export performance, primarily due to high tariffs, regulatory hurdles, and logistical inefficiencies. The CPF stresses the need to improve the business environment, particularly through reforms aimed at attracting foreign direct investment (FDI) and fostering SME growth. It also promotes sectoral support for tourism, hydropower, digital industries, and urban development, along with initiatives to boost industrial productivity through regulatory simplification and infrastructure development. The World Bank and the International Finance Corporation (IFC) are pushing for private capital mobilization and public-private partnerships (PPPs), particularly in the transport, logistics, and tourism sectors.

In the health sector, although Nepal has made progress in maternal and child health, persistent issues of stunting and health inequality remain. Health investments under the CPF are relatively limited but strategically targeted. They focus on developing shock-responsive health systems to address climate-related and disaster risks and improving service delivery coordination across the three tiers of government. Additionally, the CPF aims to enhance human capital through integrated efforts in health, education, and nutrition.

The World Bank's Country Partnership Framework (CPF) for Nepal also places strong emphasis on four interconnected priority areas: climate change, education, employment, and poverty reduction—each critical for achieving long-term resilience and inclusive development. In the area of climate change, Nepal is identified as the second most vulnerable country to multi-hazard mortality risks. The CPF builds on the findings of the Country Climate and Development Report (CCDR) and emphasizes the development of green infrastructure, including roads, energy, and urban systems. It also promotes sustainable hydropower and regional energy trade, as well as climate-smart agriculture, forestry, and disaster risk financing. A key objective is to reduce exposure to air pollution and enhance household and community climate resilience.

On education, despite improved access, Nepal continues to face challenges related to learning outcomes, skill mismatches, and gender disparities. The CPF supports foundational learning and digital skills, along with the reform of Technical and Vocational Education and Training (TVET) to improve youth employability. It also focuses on strengthening the school-to-work transition and enhancing subnational education delivery systems. In the area of employment, the CPF highlights that 82% of employment in Nepal remains informal, with youth not in education, employment, or training (NEET) at 35%, and even higher at 47% for young women. Under its "More and Better Jobs" pillar, the CPF promotes labor market reform, MSME growth, and improved access to finance. It also emphasizes support for gender-inclusive employment in sectors such as tourism, digital, and care work, while encouraging apprenticeships and demand-driven skill development programs.

Regarding poverty reduction, Nepal has made remarkable progress in reducing extreme poverty (measured at US\$2.15/day), which declined from 55% in 1995 to just 0.37% in 2022. However, using the national poverty line of 2023, poverty still affects 20% of the population, with disproportionately high rates in Sudurpaschim (34.2%) and Karnali (26.7%) provinces. The CPF prioritizes targeted interventions, robust social protection systems, and jobs-led growth, particularly aimed at marginalized groups. While remittances have played a key role in poverty alleviation, they have not led to sustained productive employment, highlighting the need for deeper structural reforms.

**CPF Outcomes and Indicators (WBG Strategy)**

CPF Outcome	Indicators
1. More and Better Jobs	Private investment as % of GDP- Wage employment share- Students supported- Financial service access (esp. for women)
2. Connected Communities	People connected to sustainable transport- People with electricity- Digital service access
3. Green Planet and Resilient Populations	People with improved climate resilience- Reduced exposure to air pollution

**H. The Sixth Review of the IMF and Government of Nepal's Commitment**

The IMF completed the Sixth Review under the Extended Credit Facility (ECF) Arrangement for Nepal in late 2025, allowing for a disbursement of approximately US\$43 million. The review notes that Nepal has made tangible progress in structural reforms, which has supported economic recovery and preserved macroeconomic stability, despite intensified domestic and external risks.

**1. Future Outlook**

The medium-term outlook for Nepal is judged to be favorable but subject to uncertainty.

- a) Growth: Economic recovery is projected to continue in FY2025/26, with forecasts placing real GDP growth around 4.7% to 5.2%. This recovery is expected to be underpinned by the government's efforts to boost public capital expenditure execution, continued strong remittance inflows, and strategic investments in the hydropower sector.
- b) Inflation: Inflation is expected to remain within the Nepal Rastra Bank's target (around 5%), supported by prudent monetary policy.
- c) External Position: The external position remains strong, backed by robust remittance inflows, which provide a substantial liquidity buffer and support the long-standing peg with the Indian Rupee.

**2. Major Risks**

Downside risks to the outlook have intensified and are multi-faceted:

- a) Political & Social Uncertainty: Lingering political uncertainty and the risk of renewed social discontent (such as the recent youth-led unrest) could undermine the effectiveness of policymaking and further weaken governance standards.
- b) Financial Sector Vulnerabilities: Rising Non-Performing Loans (NPLs) in the banking sector and the deteriorating health of savings and credit cooperatives (SACCOs) pose risks to financial stability.
- c) Policy Implementation: The persistent structural problem of under-execution of public capital projects continues to constrain growth, leading to delays in key infrastructure investments.
- d) External and Climate Shocks: Nepal remains vulnerable to natural disasters (like floods) and potential global headwinds, including trade tensions, which could affect tourism and remittances.

**3. Mitigation Strategies & Government Commitment**

The Government of Nepal's reform program, supported by the ECF, focuses on mitigating these risks through key commitments:

- a) Strengthening Governance & Anti-Corruption: The government is committed to structural reforms to strengthen the anti-corruption framework and improve governance. This includes enhancing the investment climate and addressing the root causes of social grievances.
- b) Financial Sector Stability: Authorities are focused on implementing the planned Loan Portfolio Review (LPR) and formulating a comprehensive strategy to resolve issues within problematic SACCOs.
- c) Fiscal Prudence & Efficiency: Commitment to growth-friendly fiscal consolidation, which involves accelerating capital expenditure while maintaining overall fiscal discipline and enhancing the efficiency of public investment management (PIM). The recently adopted Domestic Revenue Mobilisation Strategy aims to bolster revenues for development spending.
- d) AML/CFT Compliance: Stressing the urgency of strengthening the Anti-Money Laundering and Counter-Financing of Terrorism (AML/CFT) framework to address international compliance concerns (like the FATF Grey List).
- e) Disaster Resilience: Implementation of mitigation actions, including improved disaster early warning systems and strengthening public infrastructure resilience.

**4. IMF Support Strategies**

The IMF's role through the ECF is to support a gradual economic recovery while safeguarding macroeconomic stability. Key policy advice and strategies include:

- a) Fiscal Strategy: Encouraging sustained fiscal consolidation to stabilize debt, ensuring adequate revenue mobilization to finance essential capital spending, and expanding social protection (e.g., child grants) to shield vulnerable groups.
- b) Monetary Policy: Maintaining a cautious and data-driven monetary policy stance that remains accommodative to support recovery while preserving price and external stability.
- c) Institutional Reform: Urging the government to pass amendments to the Nepal Rastra Bank (NRB) Act to strengthen the central bank's independence, governance, and accountability.
- d) Financial Sector Reform: Calling for the prompt completion of the LPR and emphasizing that any potential regulatory forbearance must be limited, targeted, and time-bound.

- e) Structural Reform: Supporting reforms aimed at diversifying exports, enhancing productivity and competitiveness, and reducing the high cost of doing business.

Nepal's economy is gradually recovering, with real GDP growth estimated at 4.3 percent in FY 2024/25, supported by a rebound in industry, construction, hydropower expansion, and a favorable agricultural harvest. Inflation has remained contained at around 5 percent, within the Nepal Rastra Bank's target, while the external sector has strengthened on the back of resilient remittance inflows, revived tourism, and steady export growth.

Looking ahead, the IMF projects economic growth of around 5.2 percent in FY 2025/26, driven by higher capital expenditure, a rebound in domestic demand, and continued structural reforms. Inflation is expected to stay within the central bank's tolerance band (~5 percent). The medium-term outlook remains positive, supported by the expansion of hydropower capacity, infrastructure investments, and improvements in private-sector competitiveness. However, the IMF cautions that downside risks remain elevated, including under-execution of public investment, vulnerabilities in the banking and cooperative sectors, exposure to natural disasters, and persistent social and political uncertainty.

#### Political and Social Developments

Referring to the recent youth-led protests, the IMF observed that "the political landscape in Nepal underwent a change with the youth-led protests — reflecting long-standing grievances related to corruption, governance, and inequality, which were exacerbated by subdued growth and limited job opportunities." The Fund further noted that high levels of emigration continue to constrain domestic demand and labor supply, weighing on medium-term growth prospects.

#### Fiscal and Social Commitments

The Government of Nepal's FY 2025/26 budget maintains social protection initiatives, including the child grant program in 25 districts with low socio-economic indicators and the expansion of the public school midday meal scheme. While the indicative target for child allowance spending was missed, the government has committed to increasing the per-beneficiary allowance and expanding coverage to meet the social protection goals.

#### Outlook and Policy Priorities

Economic momentum is expected to strengthen in FY 2025/26, supported by improved project execution, policy measures to boost business confidence, and accommodative credit conditions. Rising investment in physical infrastructure, continued tourism recovery, and increased hydropower exports will provide further impetus to growth. Inflation may rise slightly as demand strengthens but is expected to remain anchored near 5 percent.

The current account deficit is projected to widen moderately as imports recover and remittance inflows stabilize, while foreign exchange reserves will remain at an adequate level.

#### Risks and Financial Sector Reforms

The IMF and the Government jointly recognize that domestic risks remain tilted to the downside. Key concerns include weak project execution, political fragility, and growing financial sector stress. Aggregate non-performing loans (NPLs) rose to 5.2 percent as of April 2025, and could increase further amid subdued demand and recovery challenges.

To address these risks, the government is developing a comprehensive NPL management strategy and preparing a legal framework for an Asset Management Company (AMC) to expedite NPL recovery. The Nepal Rastra Bank (NRB) is advancing amendments to the Bank Resolution Regime and the NRB Act, aligned with international standards and the 2023 Financial Sector Stability Review (FSSR) recommendations.

Reforms to the Bank and Financial Institutions Act (BAFIA) are also underway, including adjustments to related-party lending (RPL) provisions. The NRB will phase in the Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR) standards to strengthen liquidity management and overall financial resilience. Risk-based supervision will be further enhanced, regulatory forbearance reduced, and working capital loan guidelines refined to prevent misuse.

#### Fiscal and External Policies

The government reaffirmed its commitment to sound fiscal management, focusing on growth-oriented capital and social spending while avoiding procyclical expenditure cuts. Enhanced revenue mobilization remains central to sustaining fiscal space for development priorities.

Externally, authorities remain alert to global trade disruptions and commodity price volatility, maintaining adequate foreign exchange buffers to absorb shocks. If external pressures exceed domestic capacity, Nepal stands ready to seek development partner support to safeguard macroeconomic stability.

#### Climate and Social Resilience

Recognizing its high vulnerability to climate change and natural disasters, the government emphasized the importance of climate-resilient infrastructure, sustainable food systems, and protection for vulnerable populations. Despite its minimal global carbon footprint, Nepal faces significant climate-related risks that could impact agriculture, poverty reduction, and long-term growth.

#### Partnership with Development Partners

*Nepal will continue to work closely with the IMF, World Bank, Asian Development Bank, and other partners to mobilize financing and technical assistance for its reform agenda. IMF disbursements under the Extended Credit Facility (ECF) will continue to support the national budget and policy implementation.*

*The Government reaffirmed its unwavering commitment to macroeconomic stability, structural reform, and inclusive growth, guided by data-driven fiscal and monetary policies aimed at maintaining stability, enhancing resilience, and promoting sustainable recovery.*

#### I. ADB Country Partnership Strategy. 2025-2029:

1. ADB Country Partnership Strategy. 2025-2029 Key Issues in Nepal's Development Context Nepal's economy is significantly remittance-driven, with remittances contributing approximately 25% of GDP. While this inflow supports household consumption and reduces poverty, it also discourages domestic production and undermines the competitiveness of the export and manufacturing sectors. This over-reliance has made the economy vulnerable to external shocks and limited long-term sustainable growth.
2. The country also suffers from weak private sector competitiveness. High tariffs and logistics costs, coupled with a strong real exchange rate, have created an unfriendly business environment. Moreover, around 50% of enterprises operate informally, limiting access to finance, regulatory protection, and productivity-enhancing opportunities.
3. Agricultural productivity remains low due to fragmented land holdings, insufficient irrigation coverage, poor rural infrastructure, and limited connections between farming and agribusiness markets. This has constrained income growth in rural areas and reduced the sector's potential to support broader economic development.
4. There are also significant gaps in education and skilled labor. The current education system, particularly Technical and Vocational Education and Training (TVET), is misaligned with market needs, leading to a mismatch in supply and demand for labor. Additionally, basic skill deficits continue to hinder workforce readiness and employability.
5. At the institutional level, Nepal faces challenges in administrative capacity, especially at the sub-national level. The transition to a new federal governance structure has exposed weaknesses in coordination, planning, and service delivery across provincial and local governments.
6. Lastly, geographic and climate vulnerabilities pose persistent risks. Nepal's landlocked status increases trade costs, while its exposure to natural disasters—such as earthquakes and floods—threatens economic resilience and development gains. Addressing these multifaceted challenges is critical for achieving sustainable and inclusive growth.
7. **Critical Review and Suggested Actions for Nepal's Development Agenda**

Area	Suggested Action
<i>Implementation capacity</i>	<i>Strengthen local financial management, service delivery, and project implementation capacity at sub-national level.</i>
<i>Private-sector environment</i>	<i>Cut trade and regulatory barriers; implement PPPs outside hydropower (e.g., logistics, agri-processing).</i>
<i>Agriculture</i>	<i>Invest in irrigation, cooperative farming, rural infrastructure, and support agribusiness financing.</i>
<i>TVET</i>	<i>Align TVET curricula with market demand; scale apprenticeship and skill-upgrading schemes.</i>
<i>Financial innovation</i>	<i>Support local rupee bonds, improve investor confidence, and leverage pension and insurance funds.</i>
<i>Climate action</i>	<i>Require climate-risk proofing for all investments; scale adaptation measures (retrofitting, water security).</i>
<i>Regional trade links</i>	<i>Develop trade corridors and logistics links with India and China; align with regional trade bodies.</i>

- a. To address the pressing development challenges, Nepal must take targeted actions across key policy and implementation areas. A primary concern is the country's limited implementation capacity at the sub-national level. Strengthening local financial management systems, improving service delivery, and enhancing project implementation capabilities are essential to ensure effective federalism and accelerate development outcomes.
- b. Improving the private-sector environment is also critical. This requires reducing trade and regulatory barriers that hinder business activity, while expanding public-private partnerships (PPPs) beyond the traditional focus on hydropower. Sectors such as logistics and agro-processing offer strong potential for PPP-based development.
- c. In agriculture, increasing productivity and rural income demands significant investment in irrigation systems, promotion of cooperative farming models, and the expansion of rural infrastructure. In parallel, financing support for agribusinesses must be strengthened to connect farmers to markets and value chains.

- d. Nepal's Technical and Vocational Education and Training (TVET) system must be realigned with market demand. Updating curricula to match evolving industry needs and scaling up apprenticeships and skill-upgrading programs will help close the labor market mismatch and enhance workforce readiness.
- e. To advance financial innovation, Nepal should promote the development of local currency (rupee-denominated) bond markets, boost investor confidence, and mobilize long-term capital from pension and insurance funds. These reforms can provide sustainable financing options for infrastructure and development projects.
- f. On climate action, the government must integrate climate-risk proofing into all public and private investments. Scaling up adaptation efforts—such as retrofitting infrastructure and ensuring water security, will be crucial in building long-term resilience to climate shocks.
- g. Lastly, enhancing regional trade linkages will require the development of efficient trade corridors and logistics networks with India and China. Strengthening Nepal's alignment with regional trade bodies will further facilitate cross-border commerce and economic integration.

ADB's CPS is comprehensive and well aligned with national goals and global frameworks. Its strength lies in multi-sector coordination, driving growth through private investment, human capital, public service quality, and climate resilience. However, its success critically depends on strengthening local implementation capacity, delivering deep structural reforms, and transforming current dependency models, especially remittance dependence, agricultural stagnation, and weak TVET systems.

Most importantly, a sharper focus on execution, across federal structures, private sector ecosystems, vocational education, and finance innovation, will determine whether the CPS achieves its bold aims for a green, resilient, inclusive, and employment-intensive future for Nepal.

#### J. Additional Areas of Focus beyond IMF, ADB, and World Bank recommendations

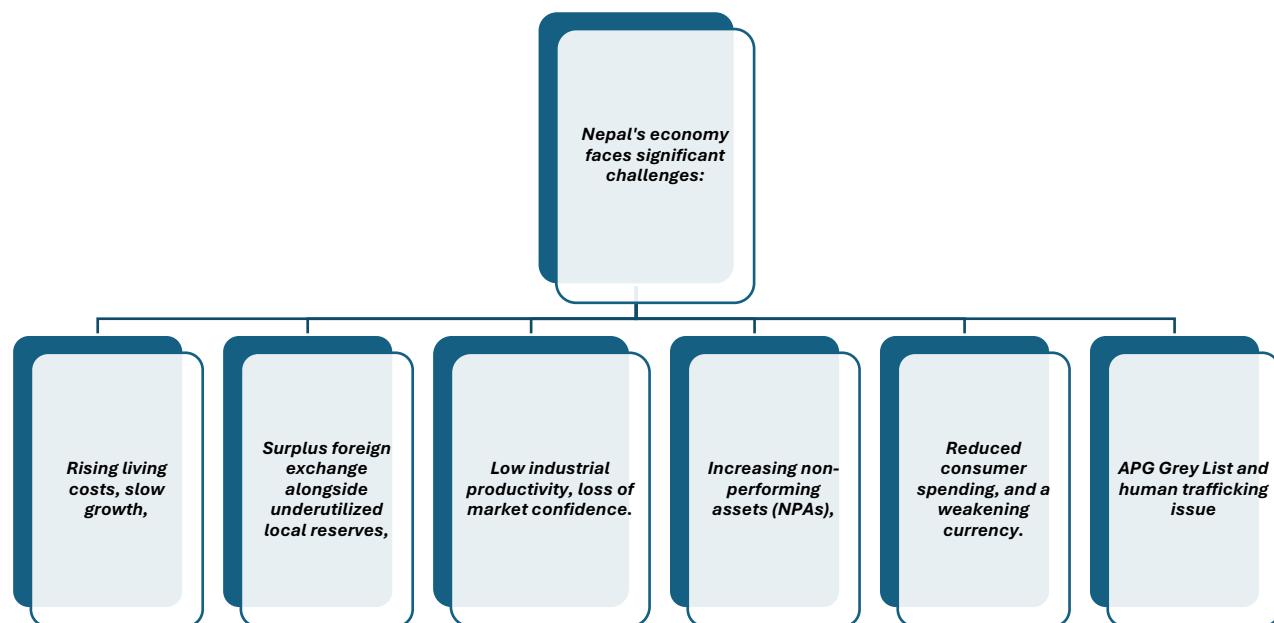
While the guidance from institutions like the IMF, ADB, and World Bank provides a strong foundation for economic reform in Nepal, several additional areas require targeted attention to ensure long-term resilience and inclusive development.

- 1. In the **financial sector**, there is a pressing need to expand access to credit, particularly through digital financial platforms. Strengthening secured transaction frameworks and modernizing payment systems will enhance financial inclusion and support private sector growth.
- 2. On **AML/CFT and FATF compliance**, Nepal must reinforce the capacity of the Financial Intelligence Unit (FIU-Nepal) by adopting a risk-based supervision approach. This includes stricter enforcement of Know Your Customer (KYC) norms, full disclosure of Ultimate Beneficial Ownership (UBO), and capacity building across law enforcement, prosecutors, and the judiciary to combat financial crimes effectively.
- 3. Following its removal from the **FATF Grey List**, Nepal must remain vigilant by improving the quality and timeliness of Suspicious Transaction Reports (STRs), and ensuring that new anti-money laundering (AML) legislation is fully aligned with global FATF standards to avoid relapse and restore global financial credibility.
- 4. To address **corruption and governance** challenges, the government should enforce transparency in public procurement through expanded use of the electronic Government Procurement (e-GP) platform. Streamlining land acquisition and environmental clearance processes is also crucial for accelerating infrastructure development. Moreover, prioritizing civil service reforms is necessary to enhance administrative efficiency and service delivery.
- 5. In tackling **human trafficking**, Nepal should expand support services for survivors and increase the presence of labor attachés in destination countries to protect migrant workers. Additionally, monitoring and regulation of recruitment agencies and brokers must be strengthened to prevent exploitation and trafficking.
- 6. With the rapid growth of the digital economy, **digital regulation** must be updated. This includes enacting robust cybersecurity and privacy laws, regulating digital lenders and fintech startups, and improving cybercrime enforcement mechanisms to safeguard consumers and ensure responsible innovation.
- 7. Lastly, a forward-looking **migration policy** should integrate labor market planning with migration strategies. Developing returnee skill certification systems and employment programs for returning migrant workers will help reintegrate talent and reduce long-term dependency on foreign labor markets.

## Section 2 Market outlook

### 1) Growth trend

- 1) Based on data from Nepal's Central Bureau of Statistics (CBS), the country's economic growth trajectory over the past decade reveals both resilience and structural challenges. The GDP for the fiscal year 2024/25 is projected to grow by 4.61%, marking a steady recovery from the pandemic-induced slump. Key drivers of this growth include the electricity and gas sector, which is projected to grow by 13.82%, reflecting ongoing expansion in hydropower and increased energy exports. The transportation and storage sector is another major contributor, with 9.45% growth, signaling recovery in logistics and infrastructure development. Tax revenues (net of subsidies) also surged by 9.89%, indicating increased economic activity or tax reforms.
- 2) The manufacturing sector, which had experienced negative growth in recent years, shows signs of recovery with a 3.78% increase. Meanwhile, the accommodation and food service sector continues to perform well, posting a 5% growth rate after peaking at 21.03% in the previous year, highlighting the ongoing rebound of Nepal's tourism industry. However, some sectors remain sluggish. Construction, traditionally a key employer, is recovering slowly (2.21%) after two years of contraction. Public services such as education (1.98%) and public administration (2.24%) show limited growth, suggesting stagnation or inefficiencies. Agriculture, forestry, and fishing - a vital sector for employment - remains stable with modest growth at 3.28%, indicating a need for modernization to enhance productivity.
- 3) The COVID-19 pandemic had a significant impact on the economy, with GDP shrinking by 2.37% in 2019/20. Sectors such as tourism, trade, and transportation were hit hardest, with accommodation and food services contracting by nearly 37%. While the economy began recovering in 2020/21 with a 4.84% growth rate, momentum slowed in subsequent years. Non-agricultural sectors are now leading the recovery, contributing to a more balanced growth profile in recent years.
- 4) Overall, Nepal's economic recovery after the September protest and flash flood should be driven by a combination of private sector supportive fiscal and accommodative nonmonetary stance. The loss suffers by energy sector need proper attention, revived tourism need some economic boost and the reconstruction effort on damaged of road infrastructure and government administrative building may speed up government sector demand. However private sector confidence needs to be improved by regulatory reform transportation and manufacturing. However, ongoing challenges in agriculture, construction, and public services may slow the growth. Structural reforms, investment in infrastructure, and productivity-enhancing measures across sectors will be essential to sustaining long-term growth.



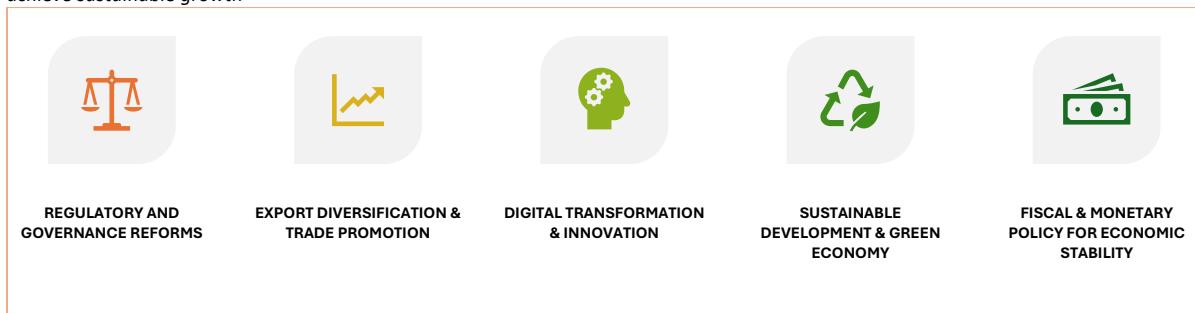
Key Challenges	
Rising Living Costs:	• Inflation has rendered essential goods and services increasingly unaffordable.
Slow Economic Growth:	• Structural inefficiencies hinder Nepal's economic potential.
Underutilized Resources:	• Surplus foreign exchange reserves coexist with unproductive local resources.
Low Industrial Productivity:	• Limited innovation and skill gaps impede industrial growth.
Overleveraged Corporate Sector:	• Rapid expansion, overreliance on borrowing from BIFs, and long cash conversion periods from corporate trading activities.
Non-Performing Assets (NPAs):	• Growing NPAs jeopardize the financial sector's stability.
Reduced Consumer Spending:	• Declining purchasing power has weakened demand and overall economic activity.
Weakening Currency:	• Depreciation of the Nepalese rupee raises import costs and strains the economy.

2) Nepal's economic landscape, highlighting key challenges and opportunities:

1. Economic recovery: "Economic Continuity" Code of Conduct: The interim government should convene ministers to endorse a three-point code of conduct. This pledge would reduce investor and consumer anxiety by committing parties to:
  - i) No abrupt fiscal changes.
  - ii) No arbitrary expropriations.
  - iii) Honoring existing Public-Private Partnership (PPP) and Alternative Investment Fund (AIF) contracts.
2. Structural Issues: Persistent challenges such as excessive bureaucracy, outdated regulations, and weak governance are identified as barriers to business stability.
3. Emerging Risks: The emerging risks that could threaten business stability, underscoring the need for proactive measures.
4. Emerging Risks: The emerging risks that could threaten business stability, underscoring the need for proactive measures.

2) Strategic Plan for Nepal's Economic Growth

Nepal can implement the following strategies and action plans to strengthen its economic resilience, enhance competitiveness, and achieve sustainable growth



1) Strategies for Nepal's Economic Development

Regulatory and Governance Reforms:	Export Diversification:	Digital Transformation:	Sustainable Development:	Strategic Monetary and Fiscal Policies:
Address structural issues by streamlining bureaucracy, updating outdated regulations, and strengthening governance to create a more business-friendly environment.	Develop and implement policies that enhance the export sector, focusing on products where Nepal has a competitive advantage to increase foreign exchange earnings.	Invest in digital infrastructure and promote innovation to improve efficiency and global competitiveness.	Incorporate environmental sustainability into economic planning to ensure long-term resilience and inclusive growth.	Implement prudent financial management practices to navigate economic challenges effectively.

## 2) Outlook for Nepal: Navigating Uncertainty with Urgent Action and Long-Term Vision

1. As Nepal finds itself at a pivotal crossroads. Mounting political and economic headwinds, both domestic and international, are fueling uncertainty and raising the specter of another downturn. A confluence of risks is intensifying, demanding urgent and strategic action. At home, political instability and the erosion of public and investor confidence are compounding economic vulnerabilities.
2. The government's continued dependence on import-based revenue and elevated direct and indirect tax burdens, combined with rising public expenditure and a lack of structural reforms, further strain the economic landscape.
3. Meanwhile, the economy is facing a troubling disconnect, muted consumer demand alongside surplus capacity. Despite historically low interest rates, productivity remains stagnant, and private sector momentum has failed to pick up. Yet, amidst these challenges, there is room for cautious optimism.
4. With decisive leadership and well-targeted reforms, Nepal can still course-correct and lay the foundation for sustainable growth. Immediate stabilization measures are necessary, but so too is a bold medium-term reform agenda that strengthens institutions, boosts competitiveness, and improves living standards.
5. Key Recommendations for the Year Ahead:

### i) Financing Reconstruction in a Commercial Way

In light of the devastation caused during the recent protests and the limited fiscal space available to the Government, it may be worth considering an innovative financing mechanism for the timely reconstruction of damaged properties. Instead of relying exclusively on direct budgetary allocations, the Government could monetize select assets and invite private investors, both domestic and foreign, to provide upfront financing for reconstruction. The Government could then gradually repay investors over a 10–15 year horizon, with interest linked to the prevailing 365-day Treasury bond rate. Such an approach could:

- (1) Conserve government resources for other pressing social and developmental priorities.
- (2) Accelerate reconstruction by reducing delays often associated with lengthy procurement processes.
- (3) Secure long-term quality, with private partners responsible for structural maintenance for at least five years.

There are precedents of similar approaches internationally:

- (1) **United Kingdom:** Public–Private Partnerships (PPPs) under the Private Finance Initiative have funded schools, hospitals, and transport infrastructure through long-term repayment models.
- (2) **India:** Cities like Pune and Ahmedabad have successfully raised municipal bonds and adopted PPP models for infrastructure, with costs recovered through government payments or user charges.
- (3) **Philippines:** Following Typhoon Haiyan, hybrid PPPs were mobilized for rapid reconstruction of public facilities.
- (4) **Kenya:** Road annuity programs enabled private contractors to finance roads, with government repayment spread over 8–10 years, benchmarked to bond rates.

A tailored model of this kind could be piloted in Nepal's reconstruction program. It would not only bridge the immediate resource gap but also strengthen public–private trust, while ensuring sustainable quality and efficiency in delivery.

- ii) Safeguard International Credibility
- iii) Take urgent diplomatic and legal steps to ensure compliance with APG standards and address human trafficking concerns proactively.
- iv) Stimulate Domestic Demand
- v) Support small businesses, expand access to affordable credit, and incentivize local production to invigorate the real economy.
- vi) Reform the Tax Structure
- vii) Reduce over-reliance on import-based taxation by creating a fairer, growth-oriented tax regime that promotes investment and entrepreneurship.
- viii) Strengthen Public Financial Management
- ix) Improve efficiency, transparency, and targeting of government spending to maximize impact and maintain fiscal discipline.
- x) Rebuild Confidence and Stability
- xi) Foster political stability, regulatory consistency, and a clear, credible reform roadmap to restore public trust and attract long-term investment.

Nepal's path forward will not be without difficulty, but with focused effort and genuine political will, 2082 can mark the beginning of a more resilient, inclusive, and prosperous economic era.

Industrial Classification	2077/78	2078/79	2079/80	2080/81 R	2081/82 P	Compare to last year
	2020/21	2021/22	2022/23	2023/24	2024/25	
<b>Agriculture, forestry and fishing</b>	<b>2.85</b>	<b>2.35</b>	<b>3.02</b>	<b>3.35</b>	<b>3.28</b>	<b>DOWN</b>
<b>Mining and quarrying</b>	<b>4.65</b>	<b>8.84</b>	<b>0.91</b>	<b>3.23</b>	<b>1.99</b>	<b>DOWN</b>
<b>Manufacturing</b>	<b>8.66</b>	<b>6.70</b>	<b>-1.70</b>	<b>-2.02</b>	<b>3.78</b>	<b>UP</b>

Industrial Classification	2077/78	2078/79	2079/80	2080/81 R	2081/82 P	Compare to last year
	2020/21	2021/22	2022/23	2023/24	2024/25	
Electricity and gas	4.18	52.68	19.76	10.96	13.82	UP
Water supply; sewerage and waste management	1.35	3.08	3.22	1.27	2.09	UP
Construction	7.00	6.93	-1.48	-2.20	2.21	UP
Wholesale and retail trade; repair of motor vehicles and motorcycles	6.64	7.42	-4.10	-0.36	3.30	UP
Transportation and storage	4.44	4.60	1.45	13.43	9.45	DOWN
Accommodation and food service activities	10.73	12.56	18.03	21.03	5.00	DOWN
Information and communication	3.67	4.19	4.15	4.91	4.81	DOWN
Financial and insurance activities	4.66	6.91	7.92	7.94	6.29	DOWN
Real estate activities	2.77	1.72	2.91	2.43	2.72	UP
Professional, scientific and technical activities	1.51	3.50	3.93	4.15	3.98	DOWN
Administrative and support service activities	2.30	1.58	5.03	4.04	3.97	DOWN
Public administration and defence; compulsory social security	3.38	4.08	5.46	4.27	2.24	DOWN
Education	3.92	4.66	3.93	2.15	1.98	DOWN
Human health and social work activities	6.60	6.99	6.57	5.31	4.77	DOWN
Other Services	3.38	4.48	5.64	4.27	3.92	DOWN
Agriculture, Forestry and Fishing	2.85	2.35	3.02	3.35	3.28	DOWN
Non-Agriculture	5.21	6.54	1.98	3.36	4.28	UP
Gross Domestic Product (GDP) at basic prices	4.49	5.28	2.29	3.36	3.99	UP
Taxes less subsidies on products	8.03	8.75	-0.60	6.36	9.89	UP
Gross Domestic Product (GDP)	4.84	5.63	1.98	3.67	4.61	UP

### 3) Economic Growth and Inflation

1. GoN set GDP growth target rate at 6% for FY 2025/26: Expected to remain low at 1-2%
2. For FY 2025/26 the GoN set target rate of inflation at 5.5% September 2025 inflation 1.87 within NRB target.

### 4) Growth Projections

1. Our provisional assessment suggests that GDP growth for FY 2025/26 will likely range between 1% and 2.0%, falling well short of the government's 6% target. Although we anticipate some demand recovery from the third quarter, Nepal's growth is expected to remain below earlier projections, likely hovering around 0.8%. Navigating these challenging times will require continued focus on strategic reforms and sustainable development.
2. The GDP growth forecasts for Nepal provided by key institutions such as the World Bank, ADB, IMF, and CBS reveal a dynamic and often shifting outlook. These projections are revised frequently, reflecting changes in both domestic and global economic conditions. The constant adjustments show how uncertain and volatile economic forecasting can be, and how numbers alone can sometimes be misleading without understanding the context behind them.
3. For instance, the World Bank initially projected Nepal's GDP growth for FY 2024/25 at 4.6% in April 2024. This was later revised upward to 5.1% in October 2024, only to be lowered to 4.9% by April 2025. A similar trend was observed for FY 2025/26, where forecasts peaked at 5.5% and later edged down to 5.4%. These fluctuations suggest a cautious optimism tempered by emerging economic data and possibly concerns over sustained recovery in key sectors. The World Bank's latest *South Asia Development Update* revised its growth forecast for 2025/26 to 2.1%, (from previous 5.4%) reflecting the adverse impact of recent unrest.
4. ADB also adjusted its projections considerably. While it forecasted 4.9% growth for FY 2024/25 in September 2024, this estimate dropped to 4.4% by April 2025. These changes reflect the bank's sensitivity to developments such as slower-than-expected industrial growth or weaker domestic consumption. Even more stark are the revisions made by the IMF, which initially projected a robust 4.9% growth for FY 2024/25 in May 2024, but revised it down to around 4.0% in January 2025, before slightly increasing it to 4.2% in March. These changes reflect how susceptible Nepal's economy remains to external shocks, policy adjustments, and global market trends.

5. Meanwhile, the Central Bureau of Statistics (CBS), which bases its estimates on actual data, reported a modest recovery, with growth improving from 2.16% in FY 2022/23 to 3.2% by the end of FY 2023/24. The early quarters of FY 2024/25 showed further improvement, with Q2 and Q3 estimates at 5.1% and 4.6%, respectively. Although these figures offer a more grounded view of Nepal's growth trajectory, they still align broadly with the revised projections of other agencies.
6. This volatility highlights the importance of looking beyond the figures to understand the underlying assumptions, risks, and policy environments that shape Nepal's economic future.

#### World Bank

<b>1. April 2024</b>	<b>4.6% FY 2024/25 projections</b>
➤ Oct. 2024	<b>5.1% (0.5% Improved from April 24 for 2024/25)</b>
➤ January 2025	<b>5.1% (no change from Oct. 2024 for 2024/25)</b>
➤ April 2025	<b>4.9% (0.2% down from January 2025)</b>
➤ June 2025.	<b>4% (0.9% down from April 2025)</b>
<b>2. April 2024</b>	<b>5.3% FY 2025/26 projections</b>
➤ Oct 2024	<b>5.5% (0.2% Improved from April 24 for FY 2025/26)</b>
➤ January 2025	<b>5.5% (no change from Oct. 2024 for 2025/26)</b>
➤ April 2025	<b>↓5.4% (0.1% down from January 2025)</b>
➤ Oct. 2025	<b>↓2.1% (3.3% down from April 2025)</b>

#### ADB

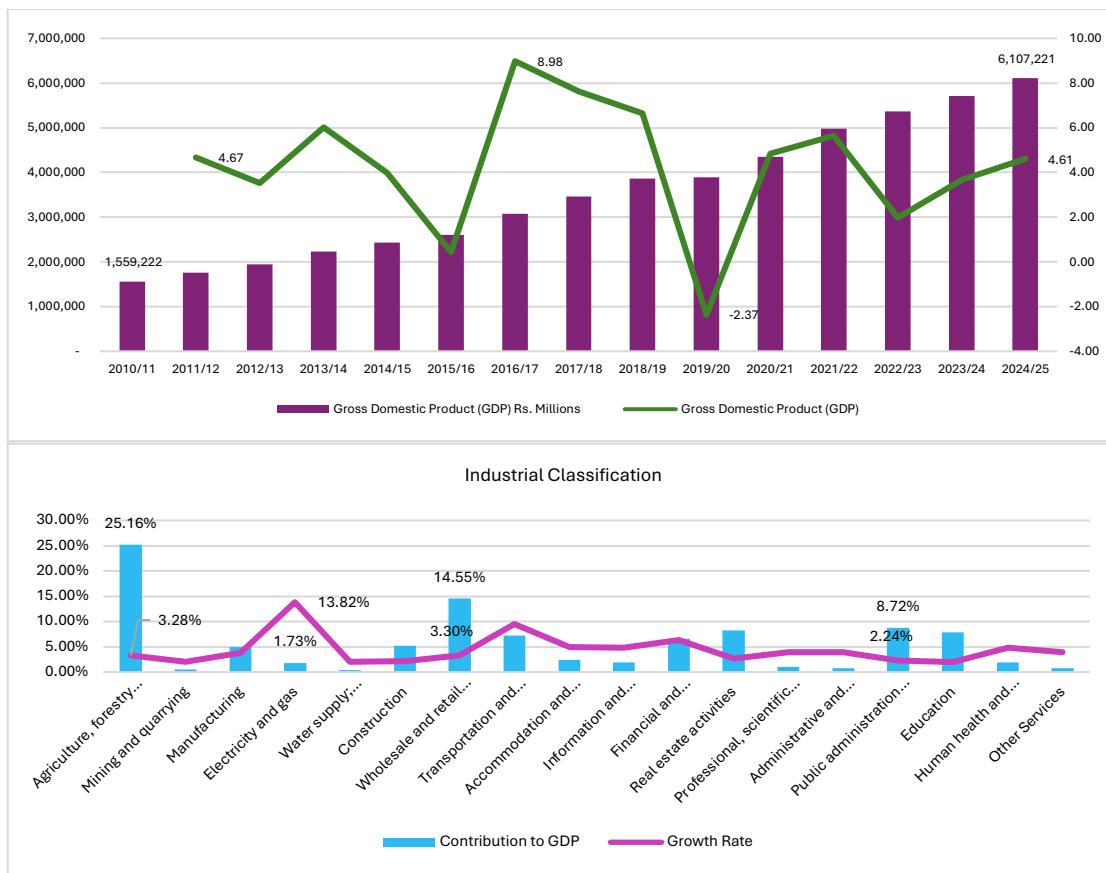
<b>1. April 2024.</b>	<b>3.6% - FY 2023/24 projections</b>
➤ Sept. 2024.	<b>3.90. 0.60% up from previous for FY 2023/24</b>
<b>2. April 2024.</b>	<b>4.8% - FY 2024/25 projections</b>
➤ Sept 2024.	<b>4.9% 0.1% up from April 2024 for 2024/25</b>
➤ April; 2025	<b>↓ 4.4% 0.5% down from Sept 2024 for 2024/25</b>
<b>3. April 2025</b>	<b>5.1% FY 2025/26 Projection</b>

#### IMF

<b>1. Oct 2023.</b>	<b>0.80 % 4.3 % down from Jan 2023 (FY 22/23)</b>
<b>2. Dec 2023.</b>	<b>3.5 % Forecast for 2023/24</b>
➤ May 2024.	<b>3.9%. (0.4% improved from Dec. 2023 for 2023/24)</b>
<b>3. May 2024</b>	<b>4.9% FY 2024/25 projections</b>
➤ January 2025	<b>↓ ~4% (0.90% down from May 2024)</b>
➤ March 2025	<b>↑ 4.2%. (0.2% improved from Jan 2024 for 2024/25)</b>
➤ Oct 2025.	<b>5.2% Satisfactory outlook for 2025/26</b>

#### CBS

• April 2023	2.16% 2022/23
• April 2024	3% FY 2023/24
• Oct. 2024	3.2% FY 2023/24 Estimate Q IV
• Jan 2025	3.4% 2024/25 Estimate Q I
• March 2025	5.1% 2024/25 Estimate Q II
• July 2025	4.6% 2024/25 Estimate Q III



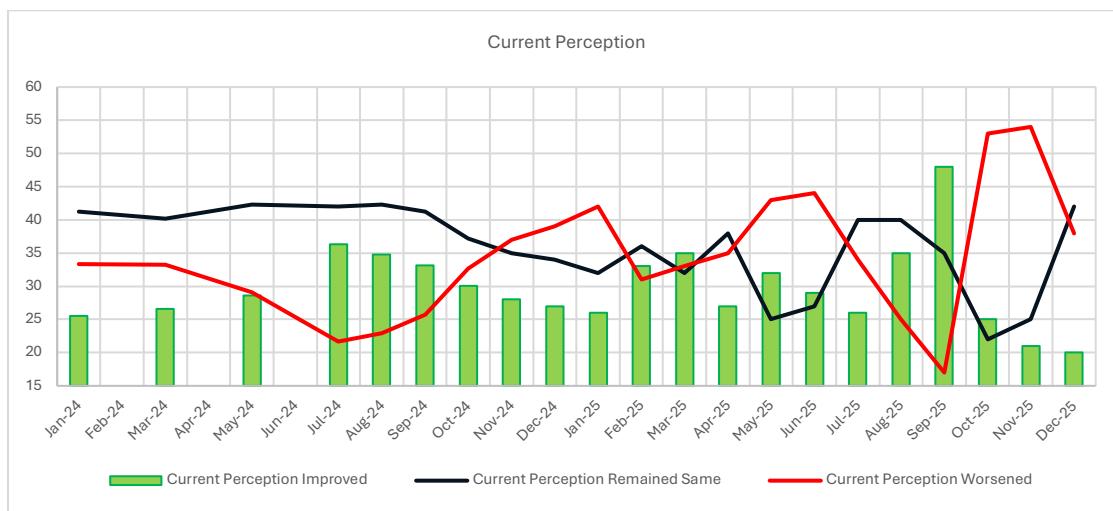
- Nepal's economic growth in 2024/25 is increasingly being powered by dynamic service sectors and productive middle-tier industries, while growth in large traditional sectors remains muted. Sectors like transport, finance, energy, and ICT are becoming new growth poles, but their scale is still developing. Meanwhile, public sector and agriculture dominate the structure but lack transformative momentum.
- To ensure balanced and sustainable economic development, Nepal should:
  - Scale up high-growth sectors through investment and policy support.
  - Modernize agriculture and public services to raise productivity.
  - Strengthen manufacturing and logistics, which combine scale and dynamism
  - Promote digital, green, and inclusive growth models to align emerging sectors with national development goals

##### 5) Nepal's Financial and Energy Sectors at a Critical Juncture

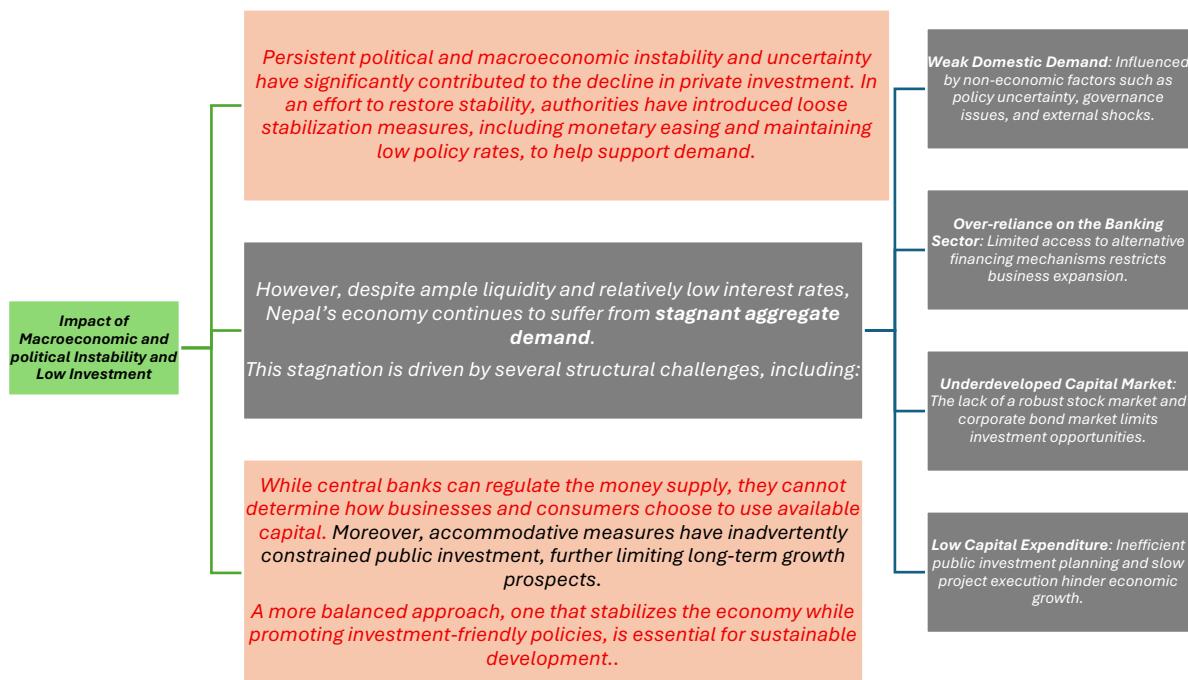
- Nepal's financial sector stands at a pivotal moment. The placement of the country on the FATF Grey List due to deficiencies in its anti-money laundering and counter-terrorist financing (AML/CFT) framework has underscored the urgency of comprehensive reform. At the same time, the World Bank's Country Partnership Framework (CPF) for FY2025–2031 offers a roadmap for fostering inclusive growth, strengthening institutional resilience, and advancing financial stability. Against this backdrop, the Nepal Rastra Bank (NRB) has taken a pivotal step by establishing a high-level Financial Sector Reform Committee, charged with addressing systemic gaps and guiding the financial sector towards a more resilient, trustworthy, and competitive future.
- The CPF identifies a range of long-standing structural constraints within Nepal's economic landscape. Remittances comprise approximately 25.3% of GDP, highlighting their central role in the national economy, yet domestic investment and formal job creation remain subdued. Private investment has plateaued at roughly 22% of GDP, over 80% of the workforce operates in the informal sector, and women's participation in the labor market is just 24%, compared to 53% for men. Meanwhile, capital budget execution has been a persistent challenge, with only 63.5% of allocations utilized in FY2024. These indicators point to deep-seated institutional, regulatory, and financial access bottlenecks that require urgent attention. In response, NRB's Financial Sector Reform Committee has been mandated to address critical areas, including strengthening AML/CFT compliance and enforcement, aligning supervisory practices with international standards, and deepening financial inclusion. The Committee aims to design a dedicated national AML/CFT mechanism, refine legal provisions for financial and non-financial institutions, and foster stronger cross-border regulatory collaboration. It will also emphasize post-merger oversight of financial institutions, expand rural and underserved access, integrate gender-responsive financial literacy, and lay the groundwork for a more open and competitive financial sector.

3. These priorities are well-aligned with the World Bank's vision for a digital, climate-resilient, and inclusive financial ecosystem. Yet experience suggests that reform efforts in Nepal often stumble due to institutional fragmentation, political interference, and a lack of accountability. To break this cycle, the Committee must operate with a focus on transparency, clearly defined milestones, robust inter-agency collaboration, and strong legal underpinnings. Amendments to critical legislation, such as the NRB Act, must be prioritized to reinforce the central bank's independence and enforcement authority. With disciplined execution and sustained political will, this initiative has the potential to position Nepal's financial sector as a trusted, resilient, and investment-ready engine of growth — one that serves its people, especially women, MSMEs, and underserved communities, while aligning with global standards and best practices. Simultaneously, Nepal's hydropower sector faces its own critical challenge. The shift from a "take or pay" to a "take and pay" model threatens to disrupt the country's long-standing strategy for harnessing its hydropower potential, estimated at over 100,000 MW, and realizing its vision of converting "water into watts" and "watts into wealth." Without predictable, secure, and transparent policies, this vision may remain an unrealized slogan rather than an economic reality.
4. The NRB should review its productive sector lending policies, especially the mandatory lending quotas for the hydropower sector. At a time when uncertainty surrounding the role of the sole energy off-taker threatens to categorize the sector as high-risk, such policies must be re-evaluated. To preserve and deepen investor confidence, regulatory clarity and long-term stability must be priorities. By providing a sound policy environment, Nepal can secure the financing required to fully unlock its hydropower potential, ensuring long-term energy security and robust economic growth.

#### 6) Consumer perception



1. Consumer perception throughout 2024 and 2025 reveals a volatile yet broadly pessimistic trend. While modest improvement was recorded during mid-2024, coinciding with relative political calm and post-monsoon recovery, sentiment began to deteriorate sharply toward the end of the year.
2. In early 2025, despite an improvement in liquidity conditions and a decline in interest rates, consumer confidence failed to rebound, underscoring the persistence of weak aggregate demand. This disconnect highlights Nepal's structural vulnerabilities, including sluggish domestic consumption, policy uncertainty, governance bottlenecks, and exposure to global shocks.
3. In November 2025, amid political instability, widespread protests, and flood-related disruptions, consumer confidence fell to its lowest level on record, with 54% of respondents expressing a worsening outlook.
4. A brief improvement emerged in December 2025, when the share of respondents who perceived conditions as "stable" rose sharply to 42% from 25%, reflecting temporary, cautious optimism, likely driven by short-term policy interventions or capital inflows. This cautious optimism was rooted in continued political uncertainty, balanced by a growing hope for political reconciliation.
5. Nepal's continued overdependence on the banking sector, combined with an underdeveloped capital market, remains a key structural constraint. The limited diversification of financing channels continues to suppress business expansion and private investment, reinforcing a cycle of low confidence and subdued economic activity.



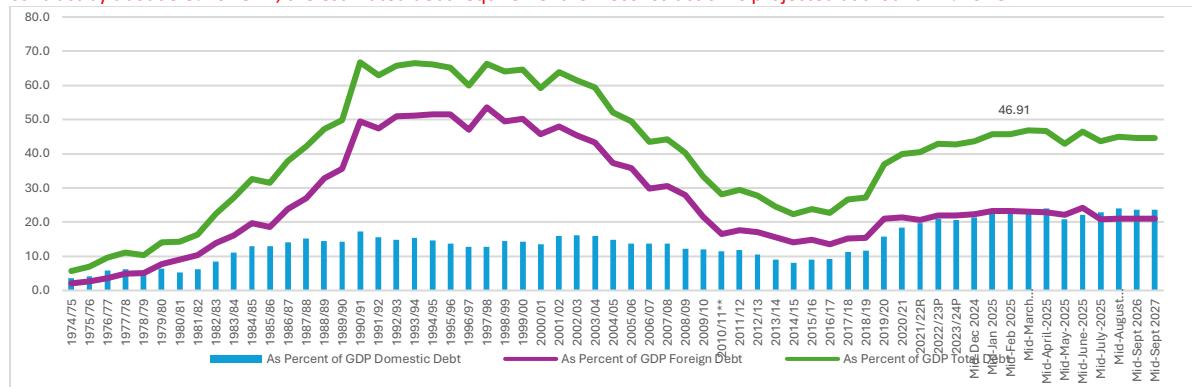
## 7) Interest rates and Inflation



**Interest rates remain low, and inflation is expected to stabilize; however, credit growth is likely to remain subdued.**

## 8) Debts to GDP

Starts above 66% of GDP, decreases to around 60% by 2009/10. Stabilizes, then rises from 2015/16 onwards, ending at 42.9% in 2019/80. Overall, foreign debt remains stable with a slight increase, domestic debt increases significantly, and total debt shows an increasing trend followed by a recent rise. **For every 0.7% decline in GDP, the debt level increases by approximately 3.5%. Given that the economy is expected to contract by about 3.5% of GDP, the estimated debt requirement for reconstruction is projected at around 12% of GDP.**



## 9) Risk Matrix

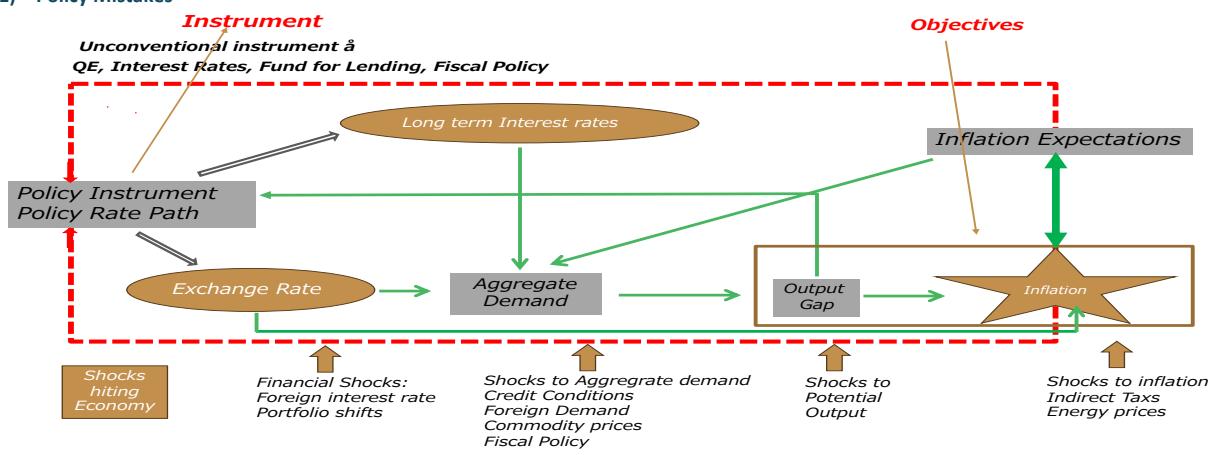
Risks	Likelihood	Impact	Mitigation Measures
Political Instability	High	High	<i>Strengthen governance frameworks and prioritize key projects.</i>
Increasing debts burden	High	High	<i>For every 0.7% decline in GDP, the debt level increases by approximately 3.5. Monetize Government Assets</i>
Climate Disruptions	High	High	<i>Invest in disaster management and climate-resilient infrastructure.</i>
Weak Spending Execution and Revenue Mobilization	High	High	<i>Streamline budgetary processes and enhance accountability in capital expenditure and revenue moralization.</i>
Declining Private Sector Confidence	Medium	High	<i>Implement tax incentives, regulatory reforms, and ease of doing business measures.</i>
External Shocks (e.g., remittance or export decline)	High	Severe	<i>Nepalese government revenue heavily relies on customs duties. However, the risk of reciprocal tariffs from trading partners and a potential reduction in grants from friendly nations could threaten fiscal stability. To mitigate these challenges, Nepal should focus on boosting local production, reducing government expenditures, downsizing the government structure, and increasing investment in research and development.</i>
Rising Non-Performing Assets (NPAs)	Medium	High	<i>Recalibrate the loan loss provisioning norms and establish AMC</i>

## 10) Factor of risk

	Condition	Related effect	Trend	Risk
Low Investment/low domestic income/ High migration	Weak wholesale and retail operations.	Aggregate demand	Decline	Low
	High unemployment	Aggregate demand	Decline	High
	Increasing Corporate cash recovery/low productivity	Firm Investment	Decline	High
	Failure of SACCOs	Disposable saving	Decline	High
Trade war	Increasing commodities prices	Import Bill	Increase	High
	Energy Price	Cost of production	Increase	High
Interest Rates outlook	Excess Liquidity	Deposit rates go below inflation	Decline	High
Informal Economy	Erode trust among investors and consumers	Government Revenue	Decline	High
FDI inflow Outlook	Excessive bureaucracy, outdated regulations, weak governance	FDI inflows	Decline	High
Level of loan Default	NPA reaching all time high	Pressure on Capital	Increase	High
Demand for Working capital	Low consumer confidence	Unutilized liquidity	Low	High
Inflation outlook	Lower consumer demand	Cost of living	Decline	Low

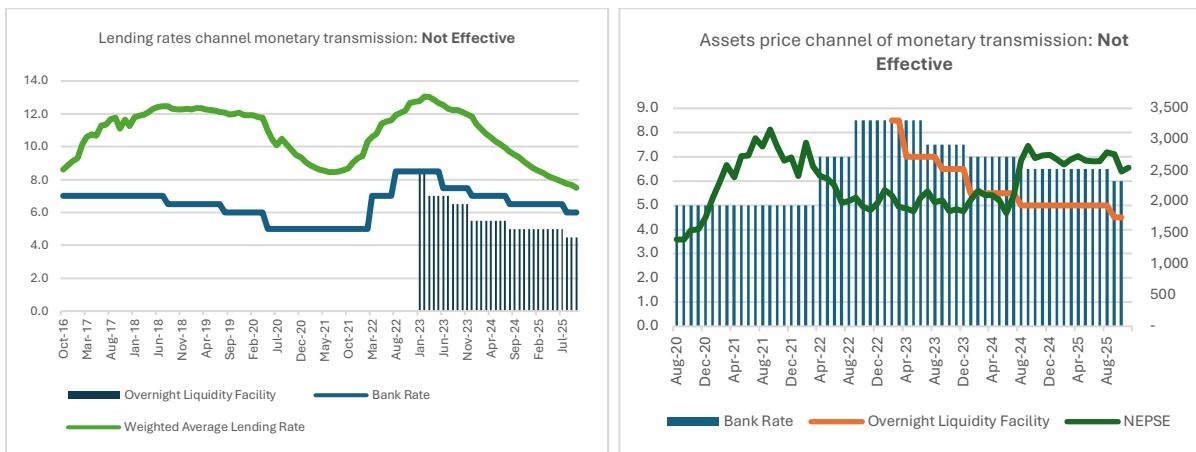
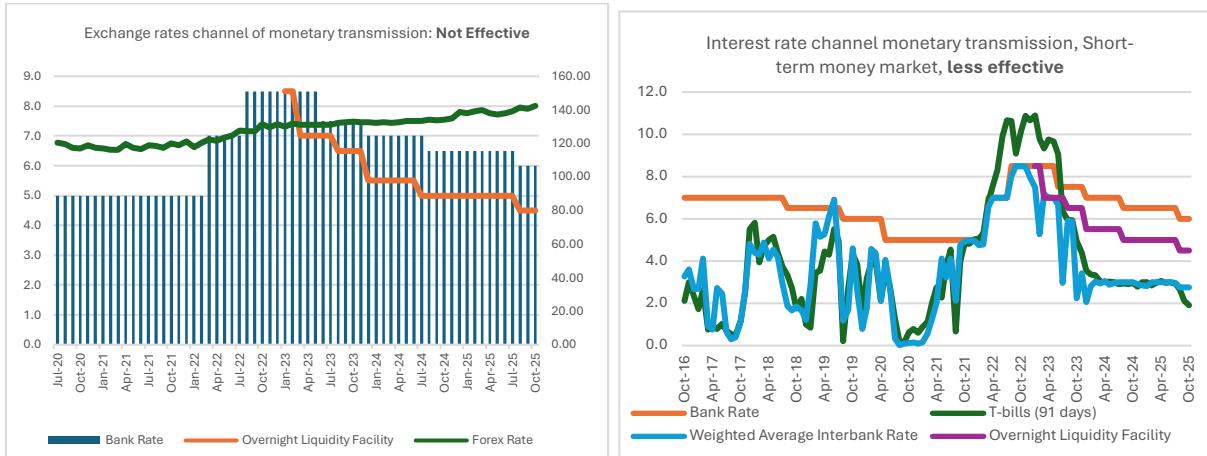
These risks, individually and collectively, pose significant threats to Nepal's economic resilience. Immediate, coordinated policy actions are necessary to strengthen institutional capacity, diversify the economic base, and protect fiscal and financial stability. Leadership commitment, strategic investments, and evidence-based policymaking will be key to navigating these challenges.

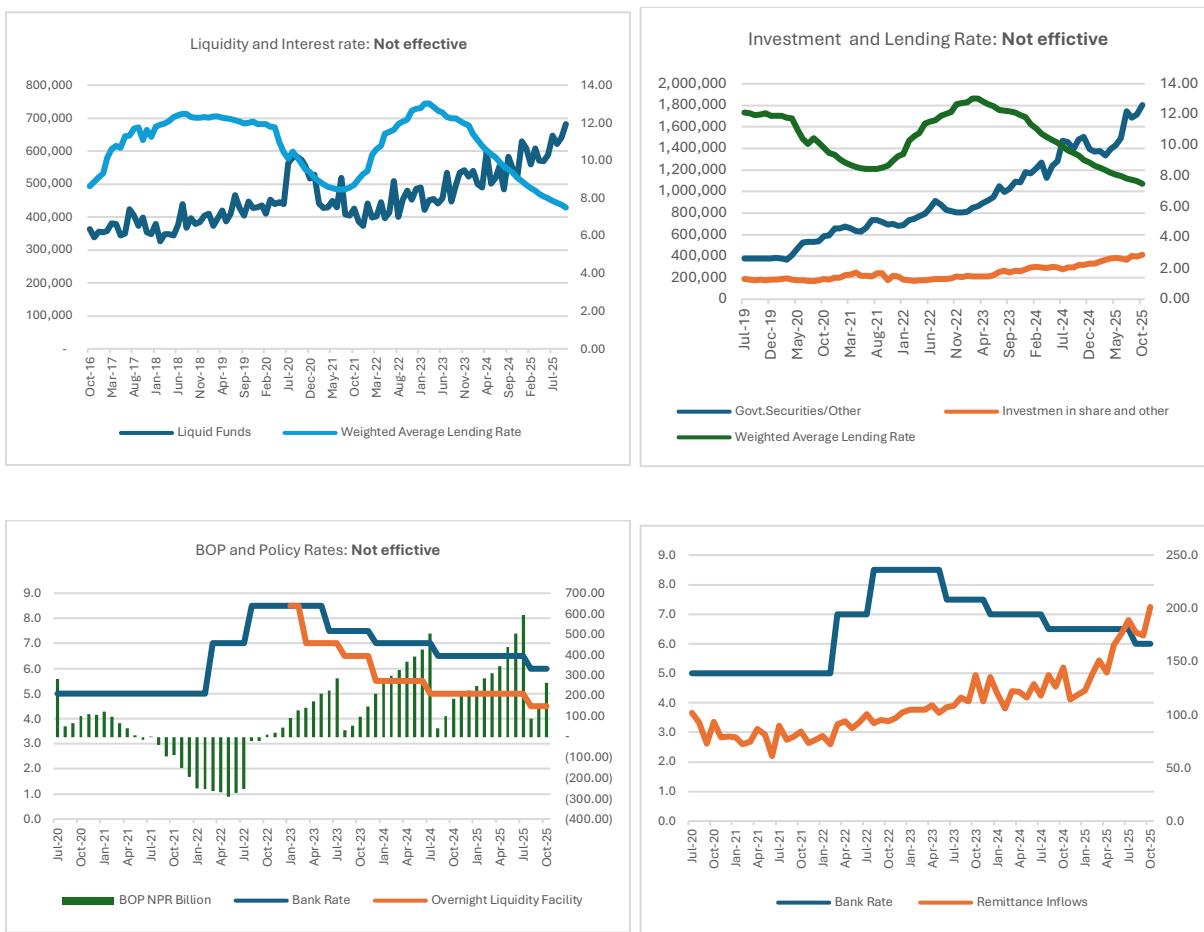
## 11) Policy Mistakes



a) 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





**b) Consumer Price Inflation (CPI)**

**1. Consumer Price Inflation (CPI)**

Consumer price inflation exhibited considerable volatility from 2019 to 2025. The initial years saw relatively high inflation rates, which moderated slightly during the pandemic but surged again in the subsequent years.

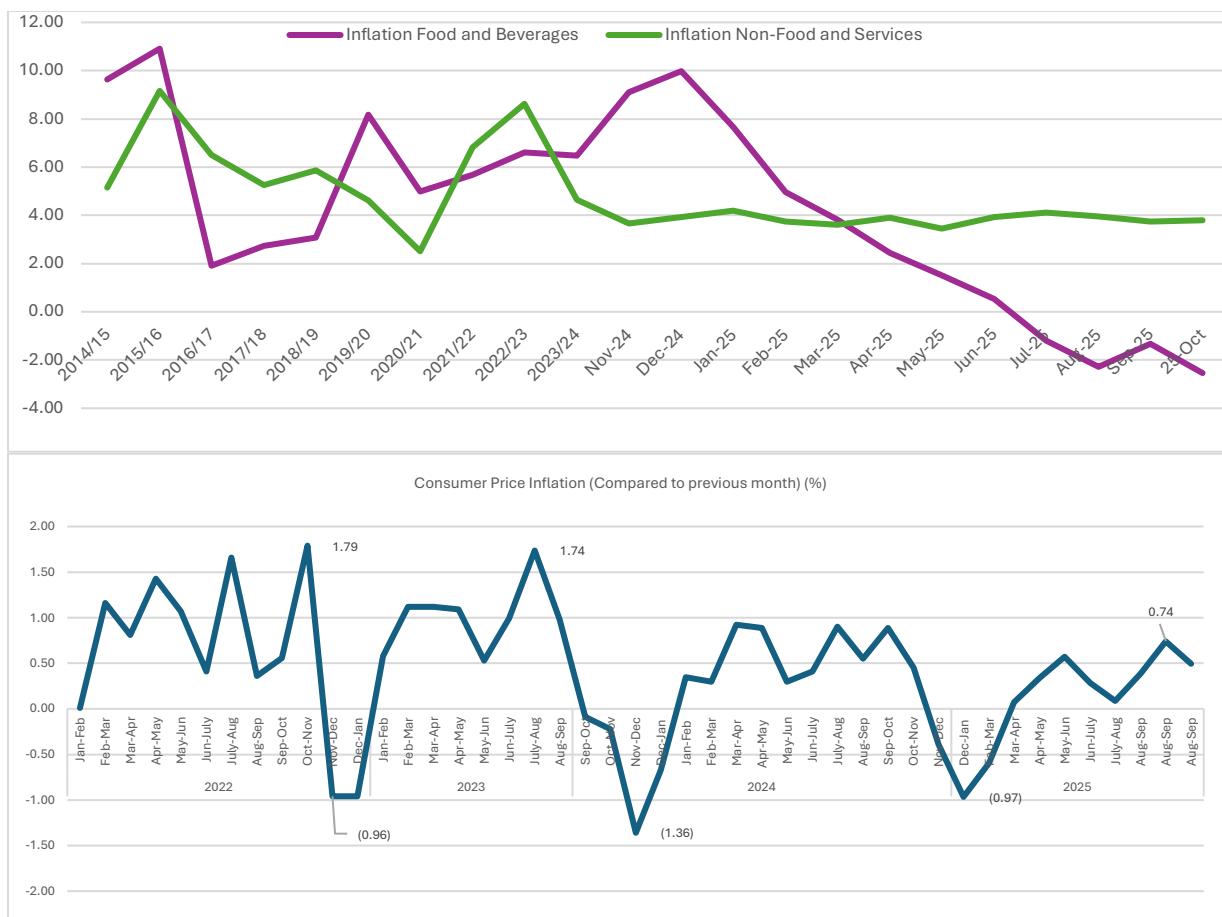
- 2019-2021: CPI fluctuated between 4.44% and 6.95%.
- 2022: A decline in CPI, reaching a low of 2.70% in Jan-Feb, reflecting subdued demand during the pandemic.
- 2023-2025: Inflation surged, peaking at 8.56% in 2023 before stabilizing around 1.47% by October 2025.

**Policy Mistakes:**

- **Reactive Inflation Control:** Sudden interest rate adjustments intended to control inflation have added to economic instability. Nepal's Consumer Price Index (CPI) is largely driven by price fluctuations in the Indian market, making it relatively unresponsive to the Nepal Rastra Bank's (NRB) policy rate. In October 2025, the CPI declined to 1.47 % from 4.82% in October 2024, primarily due to improved supply chain conditions and lower consumer demand. Persistence low inflation can be strong signal of the deflationary pressure.

**Recommendations:**

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



c) **The Kathmandu vegetable market**

**Vegetable and Fruit Price Movements (November 2025)**

The latest comparison of Kathmandu's vegetable and fruit prices between October 25 and November 24, 2025, 2082 shows overall average inflation of 13.37 percent, but with extremely high volatility across individual items. Tomatoes experienced the sharpest increase, with small local varieties rising by 264 percent and tunnel-grown tomatoes by 188 percent, reflecting severe off-season shortages and import dependence. Several off-season vegetables and gourds—such as okra, kurilo, ghiraula, and hybrid beans, also recorded price surges of 80 to 130 percent. In contrast, winter leafy vegetables including mustard greens, palungo, rayo saag, and chamsor saag saw significant price declines of 30 to 60 percent due to new seasonal harvests entering the market. Items such as onions, bananas, lemons, and fresh fish remained largely stable with minimal changes. Potato and radish prices showed mixed trends depending on variety and origin. Fruits displayed moderate fluctuations, with Nepali oranges increasing by nearly 47 percent, while avocados and kiwis became cheaper. Overall, the market reflects strong seasonal effects, supply-chain fragility, and dependence on Indian imports, resulting in sharp price swings ranging from a 60 percent drop to a 260 percent increase within just one month.

**Policy Recommendations**

1. **Strengthen Cold Chain & Storage Infrastructure:** Investment in warehousing and cold storage facilities could reduce post-harvest losses and stabilize supplies, particularly for perishables like cucumbers, leafy greens, and chilies.
2. **Promote Market Linkages & Transport Efficiency:** Enhancing farm-to-market logistics and digital trading platforms could bridge the rural, urban supply gap, preventing both gluts at the farmgate and shortages in cities.
3. **Seasonal Price Stabilization Mechanisms:** Government could pilot buffer stock or minimum support systems for highly volatile items, cushioning both farmers and consumers from extreme swings.
4. **Encourage Off-Season & Greenhouse Production:** Policies supporting controlled-environment agriculture (CEA), tunnels, and hydroponics could mitigate seasonality and stabilize supply of high-demand vegetables.
5. **Data-Driven Monitoring:** Regular publication of real-time market intelligence on prices and stocks would enable policymakers, traders, and consumers to make informed decisions.

The sharp 4.66% average rise in just one day demonstrates that Nepal's food markets are highly vulnerable to volatility, particularly in vegetables and spices. Without structural interventions in storage, logistics, and production planning, such fluctuations will continue to fuel short-term food inflation, erode household purchasing power, and undermine farmer incomes. Policymakers must prioritize market integration and infrastructure to ensure both consumer affordability and farmer sustainability.

**d) Overall inflation**

- a) Overall inflation fluctuated significantly, peaking at 9.92% in FY 2015/16 due to the 2015 earthquake and trade blockades, while reaching its lowest at 3.60% in FY 2020/21, reflecting subdued economic activity during the COVID-19 pandemic.
- b) Food and beverages inflation shows greater volatility, often exceeding non-food inflation, particularly during crises such as FY 2015/16 and FY 2019/20, driven by supply chain disruptions, seasonal shortages, or rising import prices. Conversely, years like FY 2016/17 and FY 2020/21 saw food inflation dip significantly, likely due to improved agricultural output or lower global food prices.
- c) Non-food and services inflation, however, remained relatively stable and typically lower than food inflation, except in FY 2022/23, when it surged past food inflation (8.62% vs. 6.62%), suggesting steady demand for services and non-perishable goods.
- d) In FY 2023/24, inflation moderated to 5.44% compared to the previous year, though food inflation remained elevated at 6.47%. Notably, food inflation spiked sharply in November and December 2024, reaching 9.10% and 9.99%, respectively, likely due to seasonal factors or supply disruptions. In contrast, non-food inflation remained low, ranging between 3.65% and 4.19%, indicating limited price pressures in non-food categories. **However, in October 2025, non-food inflation decreased by 1.21%, while food inflation decreased by 0.6%.**
- e) Overall, food inflation appears more susceptible to shocks from natural disasters, supply chain disruptions, or global price fluctuations, while non-food inflation demonstrates relative stability, indicating controlled service sector pricing and steadier demand.

**e) Export and Import**

**2. Exports and Imports**

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

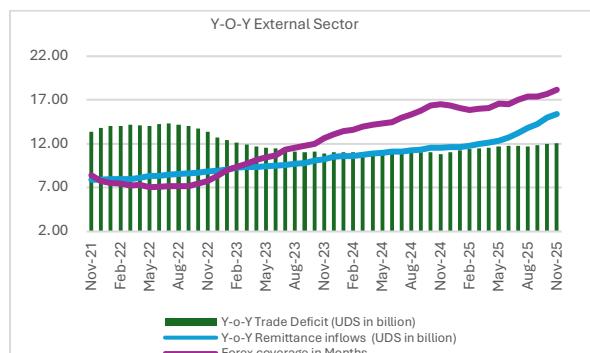
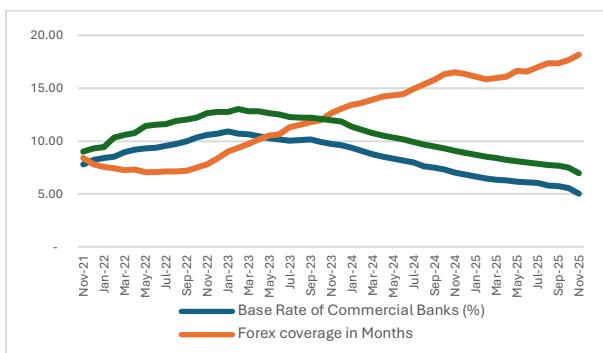
• Exports have shown a consistent upward trend, rising from NPR 8.6 billion in early 2019 to NPR 13.33 billion by December-January 2024, and further climbing to NPR 24.7 billion by mid-January 2025. In contrast, imports experienced a substantial surge—from NPR 112.5 billion in early 2019 to NPR 188.1 billion by December 2021. To contain this sharp rise, the Government of Nepal (GoN) introduced import restrictions. Although these measures were later relaxed, imports recovered slowly, leading to a large accumulation of foreign exchange reserves sufficient to cover 17 months of imports—well above the Nepal Rastra Bank's benchmark of seven months. By mid-November 2025, imports decreased at NPR 141 billion from previous month 162 billion, while exports decline to NPR 20 billion from previous month NPR 26 billion. **Looking ahead, imports are expected to rise in the coming months, driven by increased demand during the wedding seasons.**

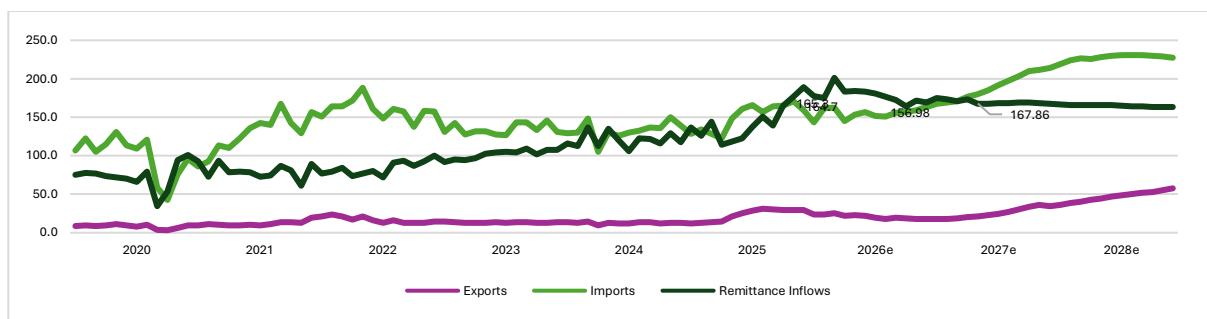
**Policy Mistakes:**

- 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. **To mitigate these challenges, Nepal should focus on boosting local production, reducing government expenditures, downsizing the government structure, and increasing investment in research and development.**





#### f) Government Expenditure

##### 3. Government Expenditure

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

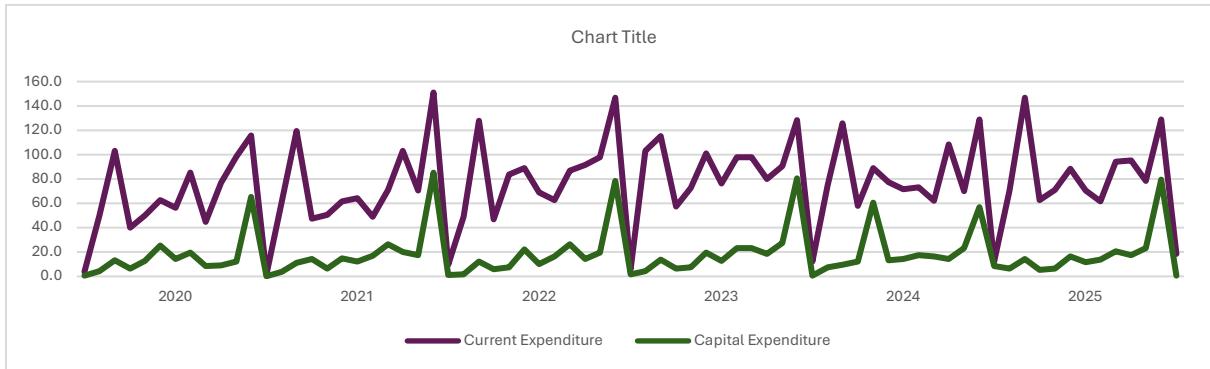
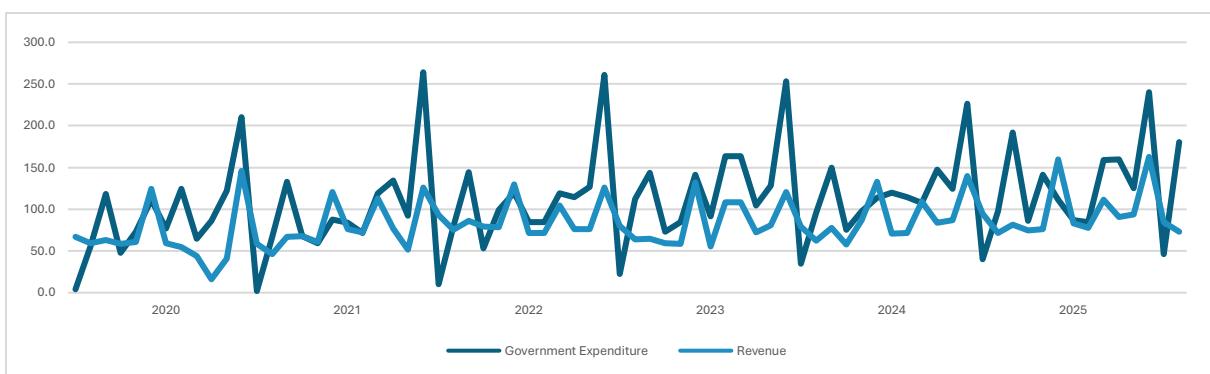
- 2019-2021: Varied widely, peaking at NPR 260.6 billion in Jun-Jul 2021.
- 2022-2025: Continued to fluctuate, reaching NPR 226.7 billion by Jun-Jul 2024 and NPR 79 billion Oct. 2025.

##### 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.



## g) Private sector Credit

**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 the end of FY 2024/25.

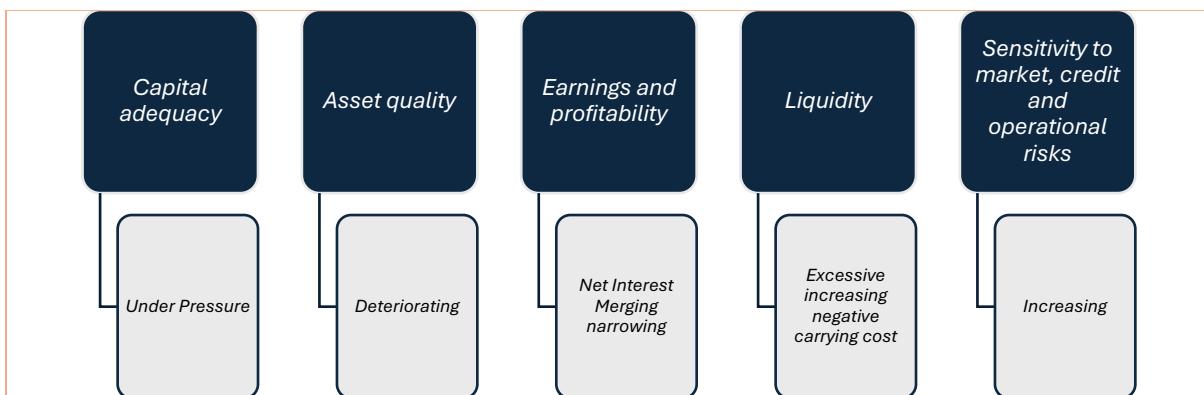
**Policy Mistakes:**

- *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.
- To address these challenges, Nepal Rastra Bank's working capital guidelines require structural reform, and a review of asset classification and provisioning norms is essential to align with the realities of muted GDP growth and ensure financial stability.
- *The stability of the financial sector has emerged as a cornerstone of Nepal's economic recovery. The rise in loan defaults and credit stress following the Gen Z protest underscores the urgent need for systematic loan portfolio reviews, a reassessment of stringent asset classification norms, and better alignment of NPA management with regional standards. Revising the asset gradation framework and easing the 100% loan loss provision requirement, by extending it to a three-year period for continued NPAs, would help release trapped capital. This, in turn, would enable banks to deploy excess liquidity, issue new loans, and reinvigorate private-sector investment.*

## 1. A core set of financial stability indicators for banks:



## 2. If all problem, loan become bad

Amount in Rs Billion	Mid-Oct	%age
Gross Loan	5,672.55	100.00%
Good loan	5,230.93	92.21%
Problem Loan	441.62	7.79%
Provision made	284.03	5.01%
Additional provision required if all become Bad	157.60	2.78%
Paid up Capital and Statutory Reserves	631.05	11.12%
Total capital to loan	837.74	14.77%
Net capital if all problem loan becomes bad	473.46	8.35%
Total capital if all problem loan becomes bad	680.14	11.99%

- a. As of mid-September 2025, Nepal's gross loan portfolio totals NPR 5,672 billion, with 92.21 % classified as good loans (NPR 5,230.93 billion) and 7.79% as problem loans (NPR 441.62 billion). While this indicates relatively healthy loan quality, it underscores the importance of careful handling of the banking sector's risk profile. Provisions currently amount to NPR 284 billion (5.01% of gross loans), serving as a buffer against defaults. However, if all problem loans were to turn bad, an additional NPR 157.60 billion in provisions would be required, raising the total provisioning requirement to 7.79%.
- b. The banking system is supported by NPR 631 billion in paid-up capital and statutory reserves, equivalent to 11.12% of gross loans. With additional reserves, total capital reaches NPR 837.74 billion, or 14.77% of the loan portfolio. In a stressed scenario where all problem loans turn bad, net capital would drop to NPR 473.46 billion (8.35% of gross loans), falling below the minimum capital threshold. When Tier 1 capital breaches this threshold, banks lose their lending capacity, reducing investment and slowing economic activity. However, total capital would remain at NPR 680.14 billion (11.99%), demonstrating resilience while emphasizing the need for vigilance.
- c. This challenging scenario also presents opportunities for reform. With timely action, the regulator can review and update policies to fortify the financial system. Introducing robust insolvency laws to expedite loan resolution and encouraging the development of asset reconstruction companies (ARCs) could create a more efficient recovery framework. The Nepal Rastra Bank (NRB) is well-positioned to take proactive steps by re-evaluating asset classification and provisioning approaches. Transitioning to a loss-given-default model, rather than time-based provisioning norms, could better reflect actual risks. Lenders must also implement stricter asset classification guidelines and accurately assess provisioning needs to enhance preparedness.
- d. By aligning Nepal's provisioning framework with regional best practices and fostering collaboration among stakeholders, the country can address financial challenges effectively and strengthen its banking sector. These measures would contribute to a more stable and resilient financial system capable of withstanding future shocks.

### 3. Total Loan Loss Provision

	Mid-July					Mid-Oct.
Provision for Risk Rs in billion	2022	2023	2024	2025	2025	
<b>Opening</b>		110.30	168.12	230.01	284.03	
<b>Addition</b>		85.63	105.41	112.88	43.94	
<b>Less Write Back</b>		27.56	43.24	58.46	15.28	
<b>Less Recovery from Written off Loan</b>		0.25	0.29	0.41	0.15	
<b>Closing</b>	110.30	168.12	230.01	284.03	312.54	
<b>Gross Loan Loss Provision</b>	2.27%	3.33%	4.26%	4.83%	5.22%	

### 4. Risk Assets Classification

<b>Gross loan</b>			<b>2025</b>		
<b>Risk Assets Classification</b>			<b>Mid-Oct.</b>		
<b>Pass Loan</b>	4,809.63	4,809.63		84.79%	
<b>Watch List</b>	421.30	421.30	5,230.93	7.43%	92.21%
<b>Special Mention Loan</b>	371.82	371.82		6.55%	
<b>Other specified Loan</b>	69.80	69.80	441.62	1.23%	7.79%
<b>Gross Loan</b>	5,672.55	5,672.55		100.00%	100.00%

5. Key Considerations: Can Asset Reconstruction Companies (ARCs) Help Solve Nepal's Debt Problem?

*Key Considerations: Can Asset Reconstruction Companies (ARCs) Help Solve Nepal's Debt Problem?*

**1. Valuation & Market Readiness**

- Should banks accept reasonable valuations for only a fraction of their non-performing assets (NPAs)?
- Banks must mark down asset values to levels acceptable to the market and ARCs.

**2. Transparency & Governance**

- Establish a clear and transparent methodology to prevent collusion and allegations of wrongdoing.
- Engage private sector participants through an open and competitive bidding process.

**3. Regulatory Oversight & Financial Stability**

- Nepal Rastra Bank (NRB) should conduct periodic Asset Quality Reviews to assess financial institutions' health.
- NRB must introduce measures to improve price discovery and facilitate efficient credit risk transfer.

**4. Legal & Structural Reforms**

- Reduce legal barriers and roadblocks that hinder asset resolution and recovery.
- Develop policies to enable ARCs to issue security receipts (SRs) or "hope notes" as part of debt resolution mechanisms.

**5. Government & Institutional Support**

- Define the extent and form of government financial backing for ARCs.

**h) Commercial Bank's Loan Composition and Growth Trend**

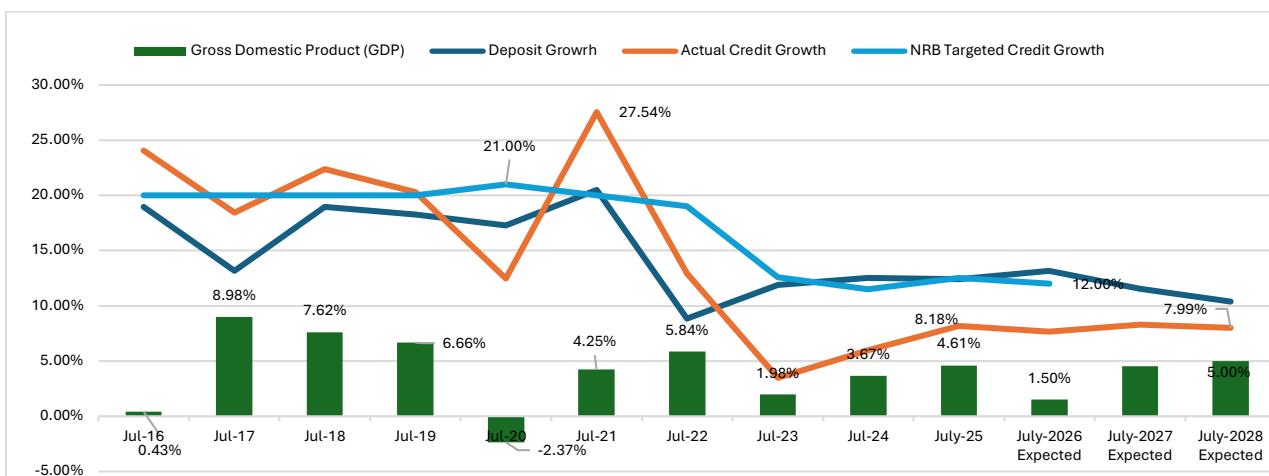
Heading	(Rs. in million)	2025		Trend	Growth
		Oct (P)	Share		
Agriculture	413,284.4	7.28%	Down	-1.10%	
Mines	11,306.6	0.20%	Down	-3.77%	
Productions	905,224.8	15.96%	Up	2.59%	
Construction	238,109.6	4.20%	Up	3.23%	
Metal Productions	75,179.1	1.33%	Up	3.00%	
Transportation	54,833.4	0.97%	Up	4.82%	
Communications and Energy	488,230.6	8.61%	Up	2.81%	
Wholesaler and Retailers	1,047,740.6	18.47%	Up	1.45%	
Finance, Insurance, and Real Estates	443,206.5	7.81%	Up	0.62%	
Service Industries	487,214.1	8.59%	Down	-0.31%	
Consumable Loan	1,169,991.2	20.62%	Up	1.80%	
Local Government	1,227.9	0.02%	Down	-0.50%	
Others	337,602.2	5.95%	Up	2.47%	
Total	5,673,151.0	100.00%	Up	1.57%	

**i) Loan Securities Composition and Growth Trend**

H Heading	(Rs. in million)	2025		Trend	Growth
		Sept. (P)	Oct. (P)		
			Share	Share	
Gold/Silver	85,810	86402.5	1.52%	Up	
Government Securities	4,603	4601.5	0.08%	Down	
Non-Government Securities	139,147	138145.6	2.44%	Up	
Fixed A/c Receipt	36,252	34729.8	0.61%	Down	

Asset Guarantee	4,993,549	5029633.0	88.66%	Up
Lands and Buildings	3,620,632	3645868.8	64.27%	Up
Machinery and Tools	200,684	200062.4	3.53%	Up
Furniture and Fixture	2,157	2383.1	0.04%	Up
Vehicles	156,693	155910.7	2.75%	Up
Other Fixed Assets	165,450	175998.3	3.10%	Up
Current Assets	847,934	849409.8	14.97%	Up
Agricultural Products	64,091	66176.4	1.17%	Up
Other Non-Agricultural Products	783,842	783233.4	13.81%	Up
On Bills Guarantee	55,110	50752.9	0.89%	Down
Domestic Bills	5,340	4652.8	0.08%	Down
Foreign Bills	49,771	46100.2	0.81%	Up
Guarantee	172,231	184953.6	3.26%	Down
Credit Card	6,500	6733.8	0.12%	Up
Others	134,358	137198.3	2.42%	Up
Total	5,627,560	5673151.0	100.00%	Up

j) Growth Trend



- The data from FY 2016 to FY 2027 reveals not just economic trends but deeper structural and policy dynamics in Nepal's financial system. A critical analysis of the period—especially surrounding the COVID-19 pandemic—highlights how policy responses, external shocks, and domestic structural weaknesses have influenced credit growth, deposit mobilization, and broader macroeconomic stability.
- During the early COVID-19 period (FY 2020), Nepal experienced a historic contraction in GDP by -2.37%, accompanied by a significant drop in credit growth to 12.46%, down from 20.28% the year before. In response, the government and the Nepal Rastra Bank (NRB) implemented aggressive monetary and fiscal stimuli to support the economy. This included refinancing facilities, interest subsidies, loan moratoriums, and relaxed regulatory measures. These interventions, while critical in the short term, had profound side effects. By FY 2021, credit growth surged to 27.54%, far exceeding the NRB's target of 20%, as banks deployed liquidity into the economy at unprecedented rates. However, the economic rebound in GDP was only moderate (4.25%), revealing a possible mismatch between credit expansion and real economic activity. Much of the credit appears to have flowed into non-productive sectors such as real estate and margin lending, inflating asset prices rather than generating broad-based economic growth.
- As the COVID stimulus unwound post-FY 2021, the NRB began tightening monetary policy to rein in inflationary pressure and financial risks. This policy reversal coincided with a sharp deceleration in both credit and deposit growth. Credit growth dropped to 12.91% in FY 2022 and collapsed further to just 3.48% in FY 2023, despite a moderate GDP expansion. Deposit growth, the foundation of financial intermediation, also declined significantly, from 20.5% in FY 2021 to just 8.84% in FY 2022. This suggests not just liquidity tightening but a deeper erosion in public trust and saving capacity, partly driven by inflation, falling remittances in real terms, and economic uncertainty.
- One of the key structural failures contributing to this decline is the crisis in Nepal's savings and credit cooperatives (SACCOS). Traditionally a significant source of local credit and deposit mobilization, these cooperatives have suffered from poor regulation, governance failures,

and mismanagement of funds. The collapse or insolvency of several cooperatives in recent years has severely undermined confidence in the informal financial system, pushing more pressure onto the formal banking sector. This has likely contributed to the reluctance of both savers and borrowers, further weakening financial intermediation.

- e. Compounding these economic issues is ongoing political instability. Frequent changes in government, inconsistent policy direction, and delays in budget implementation have all hampered the effectiveness of economic reforms. The absence of a credible long-term economic vision and weak institutional execution capacity have further aggravated investor uncertainty and discouraged long-term credit demand and investment. As a result, even as NRB has tried to stabilize the economy through calibrated credit growth targets (down to 11.5% by FY 2024 and projected 12% in FY 2026), actual credit growth remains tepid. **The expected figures for FY 2025–FY 2027 indicate a gradual recovery in credit growth, but still below historical norms. Interestingly, the projected credit growth (around 7%) remains consistent to the deposit growth (falling to 8% by FY 2027), suggesting a potential structural liquidity mismatch or continued reliance on alternative funding sources such as external borrowing or NRB refinancing. This imbalance, if not managed carefully, may create systemic risks or constrain credit availability in the future.**
- f. In summary, the post-COVID period in Nepal is marked by the challenge of transitioning from stimulus-driven liquidity to a more disciplined, growth-oriented credit environment. While NRB has responded with tighter policy frameworks, the overall effectiveness is limited by broader structural issues, including political volatility, institutional mistrust following the cooperative crisis, and a fragile depositor base. For sustained recovery, Nepal will need not only macroprudential discipline but also deep structural reforms in financial governance, cooperative regulation, and political accountability to rebuild confidence in both the banking system and the broader economy.

#### k) Interest Rates

### 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 4.75% in January 2025. 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 7.50% October 2025.
- **Base Rates of Commercial Banks:** Gradually decreased over the period, indicating the impact of excess liquidity and loss of confidence in the market.
- **Liquidity remains high, foreign reserves are strong, but average credit demand has stagnated at ~5.8% for three years. Rising NPAs are eroding banking capital, and Tier 1 capital is nearing the minimum threshold. Businesses are highly leveraged, limiting new investments.**

#### Policy Mistakes:

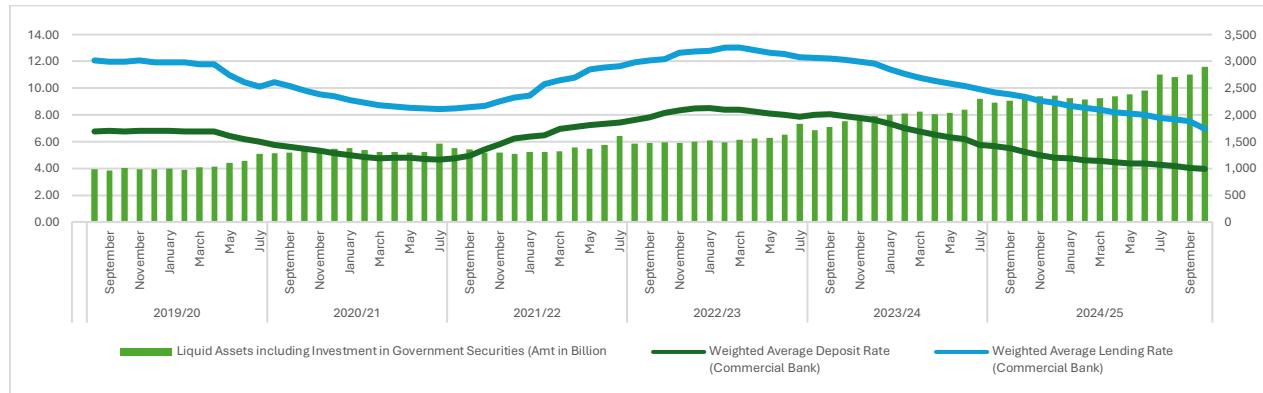
- **Overemphasis on Monetary Measures:** Relying solely on interest rate adjustments without tackling broader economic challenges proves insufficient. Excessive focus on working capital guidelines, risk weightage, and asset classification fails to align with the subdued growth dynamics of the economy.

#### Recommendations:

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

- a. The relationship between deposit rates, lending rates, and liquidity in Nepal's banking sector reflects critical dynamics impacting the sector's overall health and economic growth. **Over the observed period, deposit and lending rates have shown a consistent decline. For instance, the weighted average deposit rate dropped from 6.77% in August 2019 to 3.85% in October 2025, while lending rates decreased from 12.08% to 7.50%.** This trend indicates an easing monetary policy environment or competitive efforts by banks to reduce funding costs. Simultaneously, banks' liquid assets, including investments in government securities, rose significantly from NPR 989 billion in August 2019 to NPR 2751 billion by September 2025. This increase in liquidity highlights a trend of banks holding more liquid assets, driven by subdued credit demand and regulatory liquidity requirements.
- b. Despite falling interest rates, loan demand has not increased proportionately due to several factors. Economic uncertainty, such as the effects of the COVID-19 pandemic, has reduced business confidence and borrowing appetite. Structural bottlenecks like bureaucratic delays and insufficient infrastructure, combined with borrowers' risk aversion and a lack of viable investment opportunities, have further constrained loan growth. Additionally, banks' cautious approach to lending due to perceived credit risks has limited credit expansion. As a result, excess liquidity has been funneled into low-risk government securities, which yield lower returns compared to loans, compressing banks' net interest margins and affecting profitability.

c. To address these challenges, banks should diversify their loan portfolios by targeting emerging sectors like renewable energy, technology, and export-oriented industries. Fiscal policy measures, such as increased government spending on infrastructure and subsidies for small and medium enterprises (SMEs), can stimulate economic activity and boost credit demand. Strengthening financial intermediation by streamlining loan evaluation and disbursement processes, coupled with promoting financial literacy to encourage productive borrowing, is essential. A coordinated approach involving both fiscal and monetary policies is critical to overcoming these structural and demand-side issues, ensuring that declining interest rates translate into meaningful economic growth and financial stability.



### Section 3 Reforms agenda

#### 1) Key Considerations:



1) To enhance financial transparency and prevent illicit activities, Nepal should centralize the AML reporting system under a single regulatory authority. This will streamline reporting, reduce redundancy, and ensure consistent enforcement of AML regulations across financial institutions and businesses.:

a. Strict Implementation of AML Regulations:

Strengthen oversight to prevent financial crimes while maintaining a balanced approach that does not overburden legitimate businesses.

- b. Encouraging Voluntary Reporting of Suspicious Transactions:  
Businesses should be incentivized to report suspicious activities proactively. A safe harbor provision can be introduced to protect businesses that voluntarily disclose transactions in good faith.
- c. Reducing Compliance Costs:  
Current AML compliance requirements create a heavy financial and administrative burden on businesses. Simplifying reporting procedures, digitalizing compliance processes, and providing clear guidelines will reduce costs and ensure smoother operations.
- d. Enhanced Coordination Among Agencies:  
Establish a centralized digital platform for AML reporting, allowing banks, financial institutions, and businesses to submit reports efficiently without duplication.
- e. Capacity Building and Awareness Programs:  
Train businesses and financial institutions on AML best practices, ensuring they understand regulatory expectations and compliance requirements.

By adopting these measures, Nepal can strengthen its AML framework while maintaining a business-friendly environment, ensuring that financial integrity and economic **growth go hand in hand**.

2) BAFIA Amendment

Nepal should proactively leverage the opportunity created by the Reserve Bank of India's (RBI) new provision that allows Authorised Dealer (AD) banks to extend lending in Indian Rupees (INR) to persons resident outside India. The RBI, under the Foreign Exchange Management Act, has been steadily liberalising its framework to promote cross-border trade settlements in INR and local currencies. As part of this initiative, India aims to enhance INR liquidity and make it accessible to neighbouring economies. In line with this, AD banks in India and their overseas branches will now be permitted to provide INR-denominated loans to residents and financial institutions in Bhutan, Nepal, and Sri Lanka to support cross-border trade and related transactions.

The forthcoming regulatory amendments are expected to formalise this decision, offering Nepal a timely opportunity to deepen its financial linkages, ease trade settlements, and reduce transaction costs through greater use of INR financing mechanisms.



*The Government of Nepal has introduced amendments to the **Banking and Financial Institution Act (BAFIA)**, particularly focusing on redefining "**Financial Interest**" and "**Related Persons**" under Section 2 and tightening prohibitions on **related party transactions** under Sections 52 and 52a.*

*1. The intent of these changes is to strengthen governance, reduce conflict of interest, and align Nepal's financial sector with international best practices. However, given the historical structure of Nepal's banking sector, where business and banking interests are often interlinked, the implementation of these reforms could pose systemic risks, including credit stagnation, increased compliance burden, and potential disruption in capital mobilization.*

*Critically assesses their implications, and recommends a phased implementation framework to mitigate transitional risks.*

**Background**

*1. Nepal Rastra Bank (NRB), in its role as the regulator, has consistently aimed to modernize and safeguard the stability of the financial sector. The proposed amendments under Section 2, 52, and 52a of the BAFIA are designed to prevent related-party transactions that may lead to poor credit discipline, insider lending, and governance failures.*

**Content of the Proposed Amendments**

**Section 2: Definitions**

**Clause (kaya): Financial Stakeholder (Substituted)**

*"Financial Interest" means a person who is a director, a shareholder holding 1% or more shares or chief executive or his/her family or an individual authorized to appoint a director, or an entity or firm holding 10% or more of paid-up capital either individually or jointly, or having significant interest or control in such institution. **This includes persons or entities with less than 1% shareholding but having substantial control or influence in the financial dealings of the institution as designated by the bank from time to time.**"*

a. **Clause (kana): Related Person (Substituted) "Related Person" now includes the following (abridged for clarity):**

Description	Data Availability / Remarks	Risk to Financial Sector Stability
Founders, directors, officials of BFIs, or their family members having single or joint ownership of 10% or more in any entity.		Medium
Single or joint ownership of at least 10% in any other entity, as per Clause 3.3.1.	Data consolidation is difficult	Medium
Entities where BFI officials are involved in management or have authority to appoint or remove directors.	Subjective, cannot be quantified	High
Entities with authority to appoint or remove BFI directors, or where they are board members, office bearers, or hold 10%+ shareholding in BFIs.	Data consolidation is difficult	Low
Chief Executive Officer of a BFI.		High
Directors, officials of BFIs, or individuals/entities receiving guarantees from them.		High
Natural or legal persons with direct or indirect legal/ownership links with BFI shareholders.	Subjective, cannot be quantified	Medium
Persons or shareholders who can influence BFI management or board decisions.	Subjective, cannot be quantified	Low
Entities in which such shareholders or their relatives hold 10% or more.	Data consolidation is difficult	Medium
Entities significantly owned by BFIs or by individuals/families holding 10%+ in such entities.	Data consolidation is difficult	Medium
Entities where shareholders with significant BFI ownership serve as office bearers.	Data consolidation is difficult	Medium
Entities holding 1% or more shareholding in BFIs, individually or jointly.	Data consolidation is difficult	Medium
Entities with less than 1% BFI ownership but control over governance (e.g., directors, office bearers, or their families).	Subjective, cannot be quantified	Low
Parent company officials influencing BFI decisions, directly or indirectly.	Subjective, cannot be quantified	Low
Entities where the BFI holds 10% or more shareholding.	Subjective, cannot be quantified	Low
Entities with less than 10% BFI shareholding but influence on BFI board decisions.	Subjective, cannot be quantified	Low
Executives of BFI subsidiary companies.		Low
Other persons or entities as designated by Nepal Rastra Bank (NRB).		
For government-owned BFIs, any officials designated by NRB.		

**Section 52 and Section 18: Prohibition on Transactions and Activities and Directorship**

- **Loan Ban:**
  - Banks shall not be allowed to provide any type of loan facilities to affiliated person of that bank or financial institution or to the person holding significant ownership in any bank.

**Exceptions:**

- Loans backed by 100% cash margin guarantees.
- Loans secured with institutional fixed deposits.
- Loans backed by Nepal Government or NRB bonds.
- Home loans, as per NRB guidelines.

**Prohibited Section 52 and Section 18:**

- **Section 52: Transactions and Activities:-** Related persons are barred from providing legal, tax, accounting, valuation, or auditing services to the concerned bank.
- **Section 18 (Cha 1): Directorship:-** The total business loans obtained by the individual concerned, their family members, or any company or institution affiliated with them, exceeding one percent of the core capital of the bank or financial institution to which the individual is being proposed for appointment as a director.

**Section 52a: Maintenance of Related Party List**

- **Initial List:** New institutions must prepare and submit a related persons list to NRB upon establishment.
- **Existing Institutions:** Must prepare and submit within 35 days of fiscal year end when the section comes into force.
- **Annual Update:** The list must be updated annually and any changes reported within 35 days.

**b. Critical Analysis and Implications**

1. Governance and Risk Management Improvements
  - i. Encourages better risk management and transparency.
  - ii. Aligns with Basel principles and international banking standards.
  - iii. Restricts undue influence by insiders and affiliated parties.
2. Downsides and Practical Challenges
  - i. Structural Incompatibility
    1. Nepal's banking sector was historically built on a symbiotic relationship between bankers and businesses.
    2. Many promoters and board members are also business borrowers, making a clean separation impractical in the short term.
  - ii. Credit Flow Constraints
    1. An overly broad definition of "related persons" may restrict legitimate credit transactions, especially in SME and industrial sectors where ownership overlaps are common.
  - iii. Compliance Burden
    1. Maintaining and updating extensive related-party lists requires dedicated human and technological resources
    2. Ambiguity around what constitutes "significant influence" or "substantial control" may lead to inconsistent interpretations and regulatory friction.
  - iv. Risk of Overregulation
    1. Could discourage capital investment in banks if shareholders perceive reduced access to financial services.
    2. May push credit activities outside the formal sector, increasing systemic vulnerability
  - v. Recommendations
    1. Phased Implementation: Provide a transition window (e.g., 10–15 years) for compliance and restructuring of governance practices.
    2. Clarification Guidelines: NRB should issue operational guidelines to define "significant influence," "substantial control," and how these will be determined.
    3. Regulatory Sandbox: Allow a trial phase where banks can report related party exposures while continuing operations under existing norms.
    4. Capacity Building: Provide training and digital infrastructure support for banks to manage compliance.
    5. Stakeholder Consultation: Engage banks, promoters, and private sector representatives to design a practical enforcement roadmap.
- c. Conclusion
  1. While the proposed amendments represent a bold regulatory effort to insulate banking institutions from conflicts of interest and insider control, their blanket implementation could disrupt Nepal's traditionally integrated banking-business model. To ensure reform without destabilization, a balanced approach that blends enforcement with institutional strengthening and gradual transition is essential.
  2. The proposed amendments to Section 2, Clause (kaya) and (kana), and the enforcement of Sections 52 and 52a of the Banking and Financial Institution Act (BAFIA), in Nepal indicate a sweeping redefinition of "Financial Interest" and "Related Persons," greatly expanding the scope of individuals and entities restricted from receiving credit or providing professional services to banks. While this aligns with global prudential norms aimed at minimizing conflict of interest and enhancing transparency, it also introduces serious downside risks for Nepal's banking sector. The rigid prohibition under Section 52 on lending to a vast and ambiguously defined network of related parties could paralyze credit flow, particularly in a banking ecosystem historically rooted in closely intertwined banker-business relationships. From inception, Nepal's banking sector has grown within a framework where promoters, shareholders, and directors often overlap with major borrowers, and the sector lacks the institutional and governance maturity to abruptly transition into a fully segregated model.
  3. The immediate implementation of such stringent provisions without transitional safeguards, capacity development, or ownership restructuring, may lead to a credit crunch, underutilization of capital, and erosion of promoter confidence. Furthermore, the compliance burden introduced by Section 52a, requiring banks to continuously track and update complex related-party relationships, adds operational strain without commensurate support mechanisms. Thus, while the intent of the proposed act is commendable from a regulatory standpoint, the Nepalese banking sector is currently not structurally prepared for such a stark separation of banker and business, risking regulatory overreach that may stifle private sector-led growth.

## 3) Human Trafficking and Transportation (Control) Act, 2064

The Government of Nepal has introduced amendments to the Human Trafficking and Transportation (Control) Act, 2064. Some key changes.

Here are the major amendments in the bill to amend the Human Trafficking and Transportation (Control) Act, 2064:

1. **Expansion of Jurisdiction:** The amendment ensures that offenses committed by Nepali citizens outside Nepal or against Nepali citizens abroad fall under the act's jurisdiction.
2. **Clear Definitions:** New definitions for terms like "exploitation," "provincial committee," and "district committee" are introduced to align with international standards.
3. **Inclusion of Internal Trafficking:** The amendment includes internal human trafficking within Nepal under the legal framework, treating the movement of people for exploitation within Nepal as trafficking.
4. **Protection of Victims' Identity:** The act strengthens confidentiality measures, preventing the disclosure of victims' identities.
5. **Increased Punishment & Fines:**
  1. Harsher penalties, including increased prison terms and fines for traffickers.
  2. Higher fines and jail terms for those found guilty of child trafficking.
  3. Expanded punishment for those involved in abetting, conspiring, or attempting trafficking.
6. **Asset Seizure & Passport Confiscation:** The law allows for the freezing of assets and passports of traffickers who are fugitives.
7. **Legal Support for Victims:** Victims now have the right to a translator if they do not understand the court language.
8. **Mandatory Rescue and Rehabilitation:** The law mandates government authorities to rescue victims and ensure their rehabilitation and reintegration.
9. **Decentralization:** The law establishes provincial, district, and local-level committees to handle human trafficking cases more effectively.
10. **International Coordination:** The amendments align Nepal's laws with international anti-human trafficking protocols, ensuring cross-border cooperation.

## 4) Prompt Corrective Action (PCA)

1. In addition to the existing Prompt Corrective Action (PCA) guidelines, the NRB should consider introducing supplementary provisions to address the growing risks in the banking sector. If the net NPA level remains below 7%, no further intervention is necessary; however, once it exceeds 7% but stays below 9%, BFIs should be restricted from sanctioning new loans. Crossing the 9% threshold would trigger the second tier, requiring BFIs to refrain from accepting new deposits, while a net NPA of 11% or above should place the institution under formal PCA measures. To complement these measures, the allowable provisioning charged to the Profit and Loss (P&L) statement under the Income Tax Act should be raised from the current 5% to 9%, ensuring that banks maintain adequate buffers against potential losses. At the same time, the NRB should conduct a comprehensive review of the risk weightage assigned to different assets and liabilities on the balance sheet, recalibrating them in line with their inherent risks so that regulatory requirements more accurately reflect actual exposures, thereby fostering prudence and long-term financial stability.
2. The need for such reforms has become increasingly urgent in the context of Nepal's rising levels of non-performing assets (NPAs) and the associated risk of blacklisting by international monitoring bodies. Over the past few years, economic slowdown, sluggish private sector credit absorption, and weak corporate governance have contributed to a steady build-up of stressed assets in BFIs. At the same time, lapses in compliance and inadequate supervisory responses have heightened Nepal's vulnerability to being flagged for weak financial discipline and governance. If left unaddressed, this trend not only erodes public confidence in the banking system but also increases the risk of Nepal being blacklisted, which would severely undermine its international credibility, deter foreign investment, and isolate its financial sector from global markets. Strengthened PCA measures, higher provisioning requirements, and a recalibrated risk-weighting framework are therefore critical steps to restore resilience and prevent systemic instability.

#### Section 4 External Sector

1. **The Silent Killer:** Currency depreciation is silently reshaping Nepal's economic landscape, eroding purchasing power, discouraging investment, and straining an already fragile system. Addressing these structural challenges is essential for long-term stability. Despite signs of recovery in customs revenue, Nepal's import-driven economy faces a growing concern: the depreciation of the Nepalese rupee. Since 2020, the NPR has weakened from 1 USD = 119 to 1 USD = 142 in 2025, marking a 19.33% decline. This depreciation has increased import costs while providing only marginal improvements in export competitiveness. The export growth recorded in the second quarter of FY 2024/25 appears to be driven more by duty advantages than by currency depreciation.
2. Nepal's foreign trade balance from F.Y. 2022/23 to F.Y. 2024/25 (Mid-April) shows a persistent trade deficit, but with some encouraging signs of improvement. The trade deficit as a percentage of GDP has been gradually declining, from 20.56% in 2022/23 to 18.36% in 2024/25, indicating a slight improvement in Nepal's external trade position. Imports, which dominate the country's trade, decreased in 2023/24 (-1.21%) but rebounded in 2024/25 (+13.31%), maintaining a high share of over 86.7% of total trade. Exports, on the other hand, fell by 3.30% in 2023/24 but saw a significant 82.05% growth in 2024/25, increasing their share of total trade to 13.13%. Despite this improvement, Nepal's Export-to-Import Ratio remains at 1:10, meaning the country still imports 10 times more than it exports, reflecting a continued trade imbalance.

##### 1) Imports and Remittance outlook.

The initial results appeared promising, but this seemingly strong performance masked deeper structural weaknesses that remained unresolved. Nevertheless, we remain optimistic that authorities will refine policies to tackle these challenges. Additionally, we anticipate that electricity exports will contribute to improving overall export performance.

Between July 2020 and September 2024, Nepal's economic indicators exhibited significant fluctuations in the bank rate, overnight liquidity facility (OLF) rate, balance of payments (BoP), exchange rate, and remittance flows. The bank rate remained steady at 5% until early 2022, when it was raised to 7% amid inflationary pressures, peaking at 8.5% in August 2022 before decreasing to 2.72% by June 2025. The OLF rate followed a similar trend, starting at 8.5% in mid-2022 and dropping to 5% by June 2024, reflecting improved liquidity conditions. The BoP shifted from a positive surplus of NPR 282.40 billion in Nov. 2020 to significant deficits starting in July 2021, reaching lows of around NPR -292.24 billion in May 2022. However, by 2023, the BoP began to recover, ultimately achieving a surplus of NPR 595 billion in July 2025 and NRR 237.59 billion during the October 2025.

The exchange rate of the Nepali Rupee against the US Dollar saw depreciation, starting at NPR 120.37 per USD in July 2020 and reaching NPR 142 by Oct. 2025. Remittances and export proceed are crucial components of Nepal's foreign exchange earnings, fluctuated during this period, impacting both the BoP and forex reserves. Overall, these trends indicate a period of monetary tightening, liquidity management, and gradual improvement in Nepal's foreign currency balance amid fluctuating economic conditions.

Between November 2021 and August 2025, Nepal's trade indicators reveal persistent structural imbalances and evolving external sector dynamics. Imports consistently exceeded exports, reflecting a large and persistent trade deficit. For instance, imports ranged from USD 0.80–1.31 billion across the period, while exports remained modest, ranging only USD 0.08–0.24 billion. Consequently, the trade deficit remained substantial, fluctuating between USD 0.72 billion and USD 1.09 billion, indicating Nepal's ongoing reliance on imports and limited export capacity.

Remittance inflows showed a steady upward trajectory, increasing from USD 0.61 billion in Nov 2021 to USD 1.55 billion in October 2025. USD 0.22 billion increase from previous month, providing a crucial buffer against the persistent trade deficit. These inflows have been instrumental in supporting domestic consumption and maintaining foreign exchange liquidity.

Forex reserves mirrored these inflows, demonstrating a steady accumulation over the period. From NPR 1,506 billion in Nov. 2020, reserves increased to NPR 3,157 billion by Oct. 2025, signaling strong external sector resilience despite the trade gap. The growth in reserves reflects the combined effect of robust remittances, aid, and foreign currency inflows supporting macroeconomic stability.

Overall, the period reflects a structurally trade-deficit economy cushioned by rising remittances, resulting in substantial foreign exchange accumulation and external sector stability. While exports remain limited and imports continue to dominate, the steady remittance inflows have played a critical role in maintaining foreign exchange reserves and supporting Nepal's balance of payments.

## 2) Monthly indicators

Particulars Amount in NPR Billion	2024		2025									
	Nov-Dec	Dec-Jan	Jan-Feb	Feb-Mar	Mar-Apr	Apr-May	May-Jun	Jun-Jul	July-Aug	Aug-Sep	Sep-Oct	
<b>Consumer Price Inflation (y-o-y) (%)</b>	6.05	5.41	4.16	3.75	3.39	2.77	2.72	2.20	1.68	1.87	1.47	
<b>Consumer Price Inflation (Compared to previous month) (%)</b>	(0.39)	(0.97)	(0.60)	0.07	0.34	0.57	0.28	0.08	0.39	0.74	0.50	
<b>Food and Beverage (%)</b>	(1.54)	(3.05)	(2.26)	(0.40)	0.73	0.57	0.06	-0.17	0.62	1.43	0.67	
<b>Non Food and Service (%)</b>	0.28	0.23	0.32	0.32	0.13	0.58	0.41	0.22	0.26	0.37	0.41	
<b>Exports</b>	20.99	25.13	28.42	30.97	30.02	29.72	29.66	29.46	23.93	23.39	25.47	
<b>Imports</b>	148.1	160.9	166.2	157.0	164.0	164.7	170.6	159.3	143.0	162.11	162.9	
<b>Travel Income</b>	8.3	6.7	7.4	7.5	9.8	9.2	6.5	6.3	5.4	6.21	7.6	
<b>Travel Spending</b>	16.7	16.9	14.0	32.2	22.3	14.4	18.9	20.5	21.7	25.61	17.3	
<b>Remittance Inflows</b>	118.8	122.7	137.5	151.2	139.5	165.3	176.3	189.1	177.4	174.67	201.2	
<b>Government Expenditure</b>	141.1	111.5	87.3	84.5	159.2	159.4	125.1	240.2	46.3	180.17	184.4	
<b>Current Expenditure</b>	71.0	88.5	70.6	61.5	94.0	95.1	78.4	128.8	18.5	95.71	142.6	
<b>Capital Expenditure</b>	6.3	16.1	11.5	13.9	20.6	17.5	23.0	79.3	0.7	5.62	12.8	
<b>Revenue</b>	76.4	160.0	83.2	77.5	111.1	91.0	93.7	162.7	84.5	73.06	91.5	
<b>Deposit Mobilization</b>	22.5	66.7	6.3	31.9	91.2	31.3	117.8	293.9	-55.8	144.44	185.9	
<b>Private Sector Credit</b>	49.8	87.3	17.9	21.4	56.2	7.6	38.9	16.1	-2.9	52.17	33.7	
<b>Weighted Average Deposit Rate (%)</b>	4.78	4.75	4.62	4.54	4.45	4.37	4.29	4.19	4.02	3.96	3.85	
<b>Weighted Average Lending Rate (%)</b>	8.90	8.69	8.55	8.40	8.22	8.11	7.99	7.85	7.76	7.66	7.50	
<b>Base Rate of Commercial Banks (%)</b>	6.82	6.65	6.46	6.34	6.29	6.17	6.09	6.02	5.78	5.72	5.56	

In 2025, Nepal's economy exhibited a notable disinflationary trend. Year-on-year consumer price inflation peaked at 6.05% in November–December 2024 but gradually declined to 1.47% by October 2025. However, we estimate that inflation will slightly uptick early 2026. The easing of inflation was largely driven by volatile food prices, which saw significant month-to-month declines, while non-food and service prices remained relatively stable. This indicates a low-inflation environment, primarily supported by falling food costs and subdued domestic demand.

The external sector continued to reflect structural challenges. Exports grew steadily until February–March, reaching NPR 30.97 billion, but stagnated afterward, ending at 23.4 billion in July–October. Imports remained consistently high, ranging between NPR 122.6 billion and 170.6 billion, resulting in a persistent trade deficit. Remittance inflows, however, surged from NPR 114.3 billion in October–November 2024 to NPR 196.34 billion in July–August 2025, providing a critical buffer to external imbalances. Tourism continued to show a negative net balance, as outbound travel spending consistently exceeded travel income, peaking at NPR 32.2 billion in February–March.

On the fiscal front, government expenditure was uneven, with significant outlays in September–October (NPR 180 billion) and June–July (NPR 240.2 billion), followed by a sharp drop in July–August. Capital expenditure remained modest for most of the year, except for a spike in June–July, reflecting a year-end spending pattern, while revenue collection was inconsistent, peaking twice during the year.

The financial sector showed signs of easing. Deposit mobilization was highly volatile, with substantial inflows in June–July and negative growth in October–November and July–August. Private sector credit expanded in most months but contracted during October–November and July–August, indicating weak investment demand despite falling interest rates. Weighted average deposit and lending rates declined steadily, with the base rate of commercial banks falling from 7.02% in October 2024 to 5.56% in October, reflecting an accommodative monetary stance.

Overall, Nepal's economy in 2025 is characterized by low inflation, robust remittance inflows, and easing financial conditions, but continues to face structural trade imbalances, weak private sector investment, and uneven fiscal management. Consumption and remittances remain the main drivers of growth, highlighting both resilience and vulnerabilities in the economic structure.

### 3) Our view on the current level of External vulnerabilities

Nepal's foreign trade balance over the past four fiscal years shows a persistent dependence on imports, with imports consistently accounting for over 80% of total trade. In F.Y. 2023/24, exports represented only 9.1% of trade, resulting in a wide trade deficit of 1.80 (4.44% of GDP). The situation worsened in 2023/24 as exports fell by 9%, pushing the export-import ratio to 1:11, though the deficit as a share of GDP eased slightly to 3.96%.

A notable turnaround occurred in 2024/25, when exports doubled and their share in total trade declined by 5%, improving the export-import ratio to 1:11 imports also rising by 1%. Revenue collections increased steadily across the period, supported by higher imports and exchange rate depreciation from NPR 125 to NPR 130 per USD. Overall, while the trade deficit persists, the rebound in exports in 2024/25 signals some positive momentum toward reducing external imbalance, though Nepal's structural reliance on imports remains the key vulnerability.

F.Y. 2025/26 Mid-November.

- a) Imports rose to \$ 4.69 billion (up 18.73%), but exports surged to \$ 0.73 billion (a 75.61% jump).
- b) As a result, the trade deficit widened to \$ 3.97 billion, but relative to GDP it stabilized at 8.59%.
- c) Export share in total trade slightly decreased from previous month 13.46% to 13.31% (up from 75.61% the previous year).
- d) The export-import ratio improved sharply to 1:6.51, showing better diversification in trade.
- e) Revenue surged to 1.21 (8.04% increase).

Current year shows a remarkable recovery in exports, while imports also grew. The export contribution to trade doubled, making the trade structure more balanced, although the deficit persists.

- a) Persistent Trade Deficit – Nepal continues to run a structural trade deficit, though as % of GDP it has slightly improved.
- b) Exports Rebound in 2025/26 – as in 2024/25, exports doubled in 2025/26, showing potential gains from policy reforms, improved competitiveness, or favorable external demand.
- c) High Import Dependency – Imports consistently account for over 86% of total trade, underscoring vulnerability to external shocks and foreign exchange pressure.
- d) Exchange Rate Depreciation Effect – The fall in the NPR from 125 to 142 per USD increased import costs but boosted customs revenue collection.
- e) Revenue Growth Linked to Trade – Government revenue from foreign trade is rising, but it is still highly dependent on import volumes rather than export-led growth.

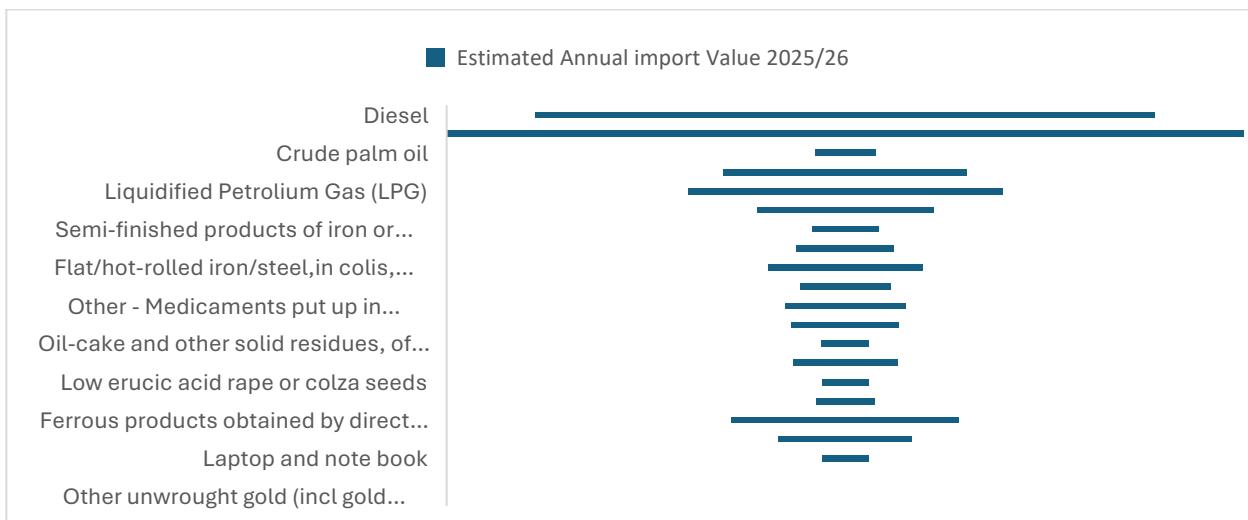
Foreign Trade Balance of Nepal \$ in billion	Total Imports	Total Exports	Trade Deficit	Total Trade	Export: Import Ratio		Revenue	Exchange factor
F.Y. 2023/24 (Mid-Oct)	3.94	0.39	3.55	4.33	1.00	10.10	1.05	1 USD= 125NPR
Share % in Total Trade	90.99	9.01						
Trade deficit % GDP	8.76%							
F.Y. 2024/25 (Mid-Oct.)	3.95	0.41	3.54	4.36	1.00	9.63	1.12	1 USD= 130 NPR
Share % in Total Trade	90.60	9.40					Up	
Trade deficit % GDP	7.66%							
F.Y.2025/26 (Mid- Oct)	4.69	0.72	3.97	5.41	1.00	6.51	1.21	1 USD= 130 NPR
Share % in Total Trade	86.69	13.31					Up	
Trade deficit % GDP	8.59%							
Percentage Change in F.Y. 2023/24 compared to same period of the previous year	0.25%	5.13%	-0.28%	0.69%			6.67%	
Percentage Change in F.Y. 2024/25 compared to same period of the previous year	18.73%	75.61%	12.15%	24.08%			8.04%	

Trade to GDP	As a positive sign of improved resilience in the external sector, the Department of Customs announced that the <b>Year-on-Year</b> trade deficit as a percentage of gross domestic product (GDP) saw an increased to 25.96 % by mid-Oct 2025, compared to the 25.75 % reported in the immediate previous month.
Trade Deficit	In the fourth month of fiscal year 2025/26, the monthly trade deficit declines at \$0.93 billion. However, compared to the same period in FY 2024/25, there was a year-on-year increase in the trade deficit to \$12.18 billion, indicating a slight reversal from the \$12 billion recorded in the immediate previous month.
Import Pressure	Heavy reliance on imported raw materials, capital goods, and consumer products. Limited potential for export growth. Sending unskilled manpower abroad as a primary export. Limited international transportation connectivity. Untapped natural resources.
Observations	Presently, Nepal maintains strong foreign exchange reserves, which cover over 16.63 months of imports and service payments based on the year-on-year import ratio. The Nepalese economy is stable, aided by the decreasing prices of imported energy and food. Despite the transition in monetary policy from tightening to a more accommodative stance, there hasn't been a significant increase in aggregate demand. However, there is optimism about continued growth in remittance inflows, which is expected to provide relief to the balance of payments in the coming months. Although there has been a noticeable increase in the import of specific goods, the risk of a major reversal in this trend has not significantly escalated, contributing to overall economic stability.

#### 4) Trade Directions

Trade Indicators	Sep-25	Oct-25	Nov-25	Y-o-Y	Remakes	%age
Imports (UDS in billion)	2.35	3.60	4.69	14.62	UP	6.04%
<b>Monthly Imports</b>	1.25	1.25	1.09			
Exports (UDS in billion)	0.36	0.56	0.72	2.44	UP	26.50%
<b>Monthly Exports</b>	0.18	0.20	0.16			
Trade Deficit (UDS in billion)	1.99	3.04	3.97	12.18	UP	3.88%
<b>Total Foreign Trade (UDS in billion)</b>	2.71	4.16	5.41	17.06	UP	7.82%
<b>Monthly Import Revenue</b>	0.32	0.33	0.28			
Total Import revenue	0.60	0.93	1.21	3.77	UP	2.79%
<b>Monthly Remittance</b>	1.34	1.55	1.41			
Remittance inflows	2.79	4.34	5.75	14.99	UP	15.65%
<b>Imports/Exports Ratio</b>	6.53	6.43	6.51	5.99	Down	-5.01%
<b>Exports Share to Total Trade (%)</b>	13.28	13.46	13.31	20.03	UP	77.18%
<b>Imports Share to Total Trade (%)</b>	86.72	86.54	86.69	79.97	Down	-7.37%
<b>Monthly Trade Deficit (UDS in billion)</b>	1.07	1.05	0.93			
<b>Trade deficit % GDP</b>	4.31%	6.58%	8.59%	25.96%	UP	6.05%
<b>Change in Monthly Trade Deficit %</b>	30.84%	-1.90%	-12.90%			

The country grapples with a persistent trade deficit, as imports consistently outstrip exports, though the deficit's growth is slowing, and its share of GDP is declining, signaling potential stabilization in trade dynamics. The trade indicators dataset for the fiscal years 2024/25 to 2025/26 reveals a persistent trade imbalance characterized by a significant trade deficit, with imports consistently outpacing exports. Monthly imports fluctuated between \$0.80 billion and \$1.59 billion, stabilizing around \$1.0–\$1.5 billion in recent months.



##### 5) Expected Annual Imports of Major Items

Description \$ in million	2023/24 Annual Import Value	Annual Import Value 2024/25	Nov-25	Estimated Annual import Value 2025/26	Import Direction	Monthly Movement 2024 VS 2025	EXPT. Annualized Movement 2025/26
Diesel	1,108	990	245	1,061	Growth	9.87%	7.22%
Crude soya-bean oil	103	838	292	1,364	Growth	430.91%	62.72%
Crude palm oil	82	52	29	105	Growth	141.67%	101.94%
Petrol	524	493	172	417	Growth	3.61%	-15.32%
Liquidified Petroleum Gas (LPG)	428	481	139	541	Decline	-4.14%	12.38%
Smartphones	221	273	124	304	Growth	20.39%	11.18%
Semi-finished products of iron or non-allo steel, <025% carbon, nes	107	106	26	116	Growth	36.84%	8.97%
Gold	182	132	121	168	Growth	1000.00%	26.92%
Flat/hot-rolled iron/steel,in colis, width >=600mm, not pickled,<3mm thickness	266	254	78	267	Decline	-21.21%	5.04%
Other coal, not agglomerated, nes	176	166	42	157	Growth	7.69%	-5.68%
Other - Medicaments put up in measured dos s or in forms or packing for retail s	211	233	68	206	Decline	-11.69%	-11.66%
Maize (excl seed)	108	141	30	184	Growth	20.00%	30.56%
Oil-cake and other solid residues, of soyabean	130	98	27	81	Decline	-25.00%	-17.08%
Crude sunflower oil	137	223	39	181	Decline	-47.30%	-18.61%
Low erucic acid rape or colza seeds	83	115	21	80	Decline	-38.24%	-30.72%
Bar & rods, hot-rolled circular cross-sect on measuring <=8mm in diameter	80	90	27	101	Decline	-6.90%	12.50%
Ferrous products obtained by direct reduct on of iron ore,in lumps,pellets or si	300	375	131	391	Growth	6.50%	4.17%
Others Paddy	93	157	28	230	Growth	40.00%	46.31%
Laptop and note book	58	68	25	80	Growth	13.64%	17.24%

## Other Major Imports

Description	Imports Value
<b>Diammonium hydrogenorthophosphate (diammonium phosphate)</b>	132
<b>Fertilizer Grade</b>	58
<b>ATF</b>	50
<b>Unassembled Motorcycles with piston engine of capacity exceeding 50 not exceeding 125CC</b>	43
<b>Electric car, jeep &amp; van 51KW to &lt;=100KW</b>	37
<b>Dyed knitted or crocheted fabrics of synthetic fibres, nes.</b>	32
<b>Other Rice Semi-milled or wholly milled rice, whether or not polished or glazed</b>	31
<b>Other potatoes, fresh or chilled</b>	31
<b>Unwrought silver (incl silver plated with gold or platinum)</b>	30
<b>Apples, fresh</b>	29
<b>Powder of silver</b>	27
<b>Petroleum bitumen</b>	25
<b>Polypropylene, in primary forms</b>	25
<b>Aeroplanes and other aircraft, of an unladen weight &gt;2000kg but &lt;=15000kg</b>	24
<b>Non-alloy pig iron containing, &lt;=05% phosphorus, in pigs, blocks or other primer</b>	22
<b>Unassembled Motorcycles with piston engine of capacity exceeding 125 not exceeding 200 CC</b>	21

Description	Unit	Exports_Value2
<b>Soya-bean oil (excl. crude) and fractions</b>	Kg	295.62
<b>Big Cardamon (Alaichi) neither crushed nor ground</b>	Kg	30.57
<b>Carpets and other textile floor coverings, of wool or fine animal hair, knotted.</b>	SQM	25.11
<b>Sunflower-seed and safflower oil (excl. crude) and fractions thereof</b>	LTR	21.02
<b>Unbleached woven fabrics of jute or of other textile bast fibre of heading 5303.</b>	SQM	16.56
<b>other Felt, whether or not impregnated, coated, covered or laminated. nes .</b>	Kg	16.27
<b>Refined bleached deodorized palm olein</b>	LTR	15.88
<b>Single yarn, with &gt;=85% polyester staple fibres, nprs</b>	Kg	13.57
<b>Mixtures of juices, unfermented, not containing added spirit.</b>	LTR	11.92
<b>Shawls, scarves, mufflers, mantillas, veil, etc, of wool or fine animal hair</b>	PCS	10.87
<b>Other black tea (fermented) and other partly fermented tea</b>	Kg	10.64
<b>Other yarn, &lt;85% polyester staple fibres, with artificial staple fibres, nprs</b>	Kg	9.70
<b>Veneer sheets and sheets for plywood and other wood, &lt;6mm thick, nes</b>	FTK	8.51
<b>Sacks and bags, used for packing goods, of jute or of other textile bast fibres</b>	Kg	8.46
<b>Dog or cat food, put up for retail sale</b>	Kg	7.97
<b>Oil-cake of low erucic acid rape or colza seeds</b>	Kg	7.95
<b>Woven fabrics obtained from synthetic straw or the like</b>	SQM	7.78
<b>Other pasta, nes</b>	Kg	7.38
<b>Cetechu of acacia (Kattha)</b>	Kg	6.41
<b>Women's or girls' trousers, breeches, etc, of cotton</b>	PCS	6.37

The import data from July to November 2025 reveals a mixed trend across major commodities, indicating both structural shifts in consumption and changes in trade behavior. Diesel, Nepal's largest import item, saw a increase of 7.22% year-on-year with an estimated annual value of USD 1,061 million, suggesting increasing business activities or increased industrial mobility despite of political uncertainty. Imports of edible oils—

particularly crude soybean oil—surged sharply, with a 403% during November 2025 on y-o-y basis, signaling a sharp rise in export to India. Crude palm oil and maize imports also rose substantially, while crude sunflower oil and low erucic acid rapeseed imports fell, reflecting supply realignments in the edible oil segment. Imports of petrol witness an upward movement while and LPG showed moderate decrease, with petrol increased 3.61% and LPG decline by 4.14%, hinting at stabilized domestic fuel demand. Gold imports rebounded strongly by 1000%, due to relaxed import restrictions, surge in prices and increased safe-haven demand. In the industrial segment, semi-finished iron and steel imports maintained growth (36%), other coal also recorded growth while medicaments recorded mild declines. Imports of consumer electronics such as smartphones grew by 20% and laptops by 13.64%, reflecting resilient urban consumption and digital adoption. Overall, the projected annual import value for FY 2025/26 indicates an uneven pattern—strong rebounds in agro-based and consumption goods, moderate declines in fuels and raw materials, and emerging growth in tech-related imports—suggesting a gradual normalization of trade dynamics following the economic disruptions earlier in the fiscal year.

Construction-related imports such as iron, steel, and ferrous products have shown mixed trend, reflecting ongoing infrastructure and industrial demand. Meanwhile, rising imports of smartphones, laptops, and pharmaceuticals indicate increasing consumer demand, digital adoption, and healthcare needs. Smaller but strategic imports include fertilizers, unassembled motorcycles, onions, apples, and petrochemicals.

On the export side, Nepal continues to rely on a narrow range of products. The largest share comes from processed vegetable oils, particularly soybean oil (USD 295million) and palm and sunflower derivatives, which together account for the bulk of total export earnings. However, as noted, this export surge is largely driven by re-exports linked to India's tariff regime, leaving Nepal exposed to policy reversals. Traditional exports such as carpets, wool textiles, tea, cardamom, jute products, and handmade shawls continue to provide niche markets but remain small in value. Industrial exports such as polyester yarns, plywood, veneer, and cement are slowly emerging, but they remain limited in scale compared to import volumes.

Overall, Nepal faces a widening structural trade deficit, with imports concentrated in high-value essentials like fuel, oils, and medicines, while exports remain low-value and dependent on trade preferences. This creates multiple risks: food insecurity due to reliance on imported edible oils and cereals, exposure to global energy price shocks, rising healthcare costs, and vulnerability in exports if tariff benefits are withdrawn or India alters its import policy. Addressing these issues requires strategic reforms. Nepal should diversify its export base beyond edible oils by promoting high-value agro-processing sectors such as tea, coffee, spices, and herbal products. Investments in domestic oilseed and maize production are critical to reduce food import dependency. On the energy front, accelerating electric vehicle adoption and expanding renewable energy will help curb petroleum imports. Industrial policy must support local production of iron, steel, pharmaceuticals, and ICT-related products, while trade diplomacy should focus on maximizing access under programs such as the US Nepal Trade Preference Program (NTPP) and the EU's GSP scheme.

In conclusion, while Nepal's imports are shifting from diesel toward edible oils as the largest burden, exports remain narrow and highly dependent on temporary arbitrage opportunities created by India's tariff regime. Without structural reforms, the trade deficit will persist. The way forward lies in strengthening agriculture, advancing energy transition, promoting industrialization, and diversifying exports to ensure sustainable and resilient trade growth.

## 6) Nepal's FDI Landscape: A Look at Progress and Persistent Challenges

Nepal is actively positioning itself as a prime investment destination, as highlighted in the "FDI Trends and Investor Guideline 2025" report. With a BB- sovereign credit rating from Fitch Ratings and legal reforms like the new Investment Related Act, the government is making strides to attract foreign capital. The establishment of the One Stop Service Centre (OSSC) is a commendable step toward streamlining processes. Recent data shows strong FDI commitments, with India, China, and the USA leading the way, demonstrating growing international interest. Top FDI Commitments (FY 2081/82)

- India: 3,745.54 million NRs.
- China: 3,212.19 million NRs.
- USA: 1,511.23 million NRs.
- 

However, a closer look reveals a significant gap between these commitments and actual investment inflows. The flow of capital-intensive FDI remains a persistent challenge. While the government has introduced new legal frameworks, the lack of timely issuance of corresponding regulations often creates a climate of uncertainty for investors.

Why is Nepal still lagging behind its neighbors?

- Political and Bureaucratic Hurdles: Frequent political instability and a slow, cumbersome bureaucracy create a "wait-and-see" approach among investors, despite government efforts.
- Infrastructure Deficit: Poor transportation infrastructure and land acquisition issues increase the cost and complexity of setting up large-scale projects, making Nepal less competitive compared to countries like India and China with more developed infrastructure.
- Lack of Implementation: While new laws and acts are passed, the slow pace of implementation and inconsistent enforcement of regulations erode investor confidence. This is particularly true for complex projects that require coordination across multiple government agencies.
- Small Domestic Market: Nepal's relatively small market size does not always justify the large-scale, capital-intensive projects that investors in sectors not vulnerable to demand shock might consider.

To truly unlock its potential, Nepal must focus on bridging the gap between policy and practice. By translating legal reforms into tangible, efficient processes, and by prioritizing the development of robust infrastructure, the country can move beyond mere commitments to attract the sustained, high-impact investments its needs for long-term growth.

#### Key FDI Data and Sectoral Performance

Analysis of recent FDI data from the Department of Industry reveals a detailed breakdown of FDI approvals by sector for the months of July and August 2025. The data shows a notable increase in the number of projects, though with significant monthly fluctuations in value.

FDI Approved by the Department of Industry (Mid-October 2025)

Category	Number of FDIs Up to Mid-Oct 2025		
	No. of Project	Amount in USD	Monthly Growth in %age
Manufacturing	21	12.71	33%
Energy	1	1.42	33%
Agro and Forestry Based	13	166.14	0%
Tourism	118	51.48	1%
Mineral	1	-	34%
Service	23	21.65	100%
Infrastructure	1	-	10%
ICT	205	4.33	0%
<b>Total</b>	<b>383</b>	<b>254.55</b>	<b>55%</b>
<b>Repatriation Amount</b>	<b>-</b>	<b>22.37</b>	<b>11%</b>
<b>Outflow / Inflow ratio</b>	<b>-</b>	<b>0.09</b>	<b>0%</b>

## Section 5 Financial Sector highlights

### 1) Persistent Stagnation in Bank Credit Growth Despite Lower Lending Rates

*Economic activity in Nepal remains subdued despite a few encouraging signs.*

As of August 2025, consumer spending showed only a marginal uptick, supported mainly by higher remittance inflows and a modest decline in borrowing costs. However, the manufacturing sector, a cornerstone of industrial growth, continues to face stagnation on the supply side, with limited new investments and production disruptions. The September unrest and flash floods brought unprecedented loss of life and property, further eroding business confidence and disrupting regional trade and logistics. In this fragile environment, the market is anxiously awaiting coordinated fiscal and monetary stimulus to restore confidence, revive private sector activity, and stabilize the overall economic outlook.

*Migration and urbanization trends have continued to dampen rural demand, which is expected to remain below the levels recorded in FY 2024/25. In the current fiscal year (2025/26), the weighted average lending rate has fallen by 10 basis points to 7.76%, marking an all-time low from the peak of 13.03% observed in February 2023. This sharp decline in borrowing costs has stimulated a modest recovery in urban demand, particularly for domestically produced capital goods, as reflected in recent 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 in October 2025 has fallen to a record low, reflecting deepening economic uncertainty. The investment outlook remains weak, weighed down by multiple factors — including political unrest, subdued credit demand from corporates (particularly in manufacturing), persistently low government capital expenditure, and the strained balance sheets of both banks and businesses. Compounding these challenges are reduced capacity utilization and a sharp decline in business sentiment.*



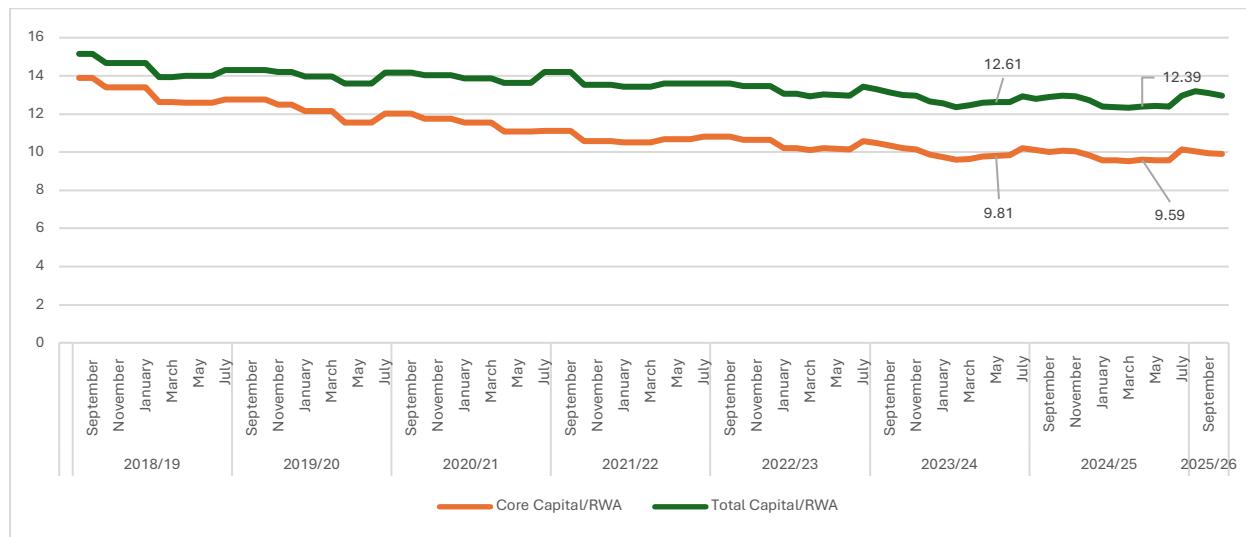
### 2) Non-Performing Loans (NPL)

The chart presents data on GDP growth and the ratio of Non-Performing Loans (NPL) to total loans for various quarters from 2016/17 to 2024/25. Over this period, GDP growth fluctuated significantly, with the highest growth recorded in Q1 2016/17 at 12.9%, and the lowest contraction in Q4 2019/20 at -11.2%, largely due to the impact of the COVID-19 pandemic. After the sharp decline in 2019/20, the economy began to recover, although growth remained moderate and volatile. Some quarters showed slower growth or even negative growth, particularly in 2022/23. Despite this, there were signs of gradual recovery, with Q4 2020/21 marking a strong rebound at 11.2%.

The NPL ratio, on the other hand, exhibited an overall decline in the earlier years, from 2.25% in Q1 2016/17 to 1.48% in Q4 2020/21, signaling improved loan quality and a lower default risk in the banking sector. However, starting in 2021, the NPL ratio began to rise, peaking at 3.98% in Q3 2023/24. This increase suggests growing challenges for the banking sector in managing defaults, possibly related to post-pandemic

economic stresses and inflationary pressures. In Q4 of 2024/25, the NPL ratio reached moderate high of 4.62%, signaling some correction from immediate previous quarter high of 5.30%. **Q1 of 2025/26 NPL surged to 5.23%**.

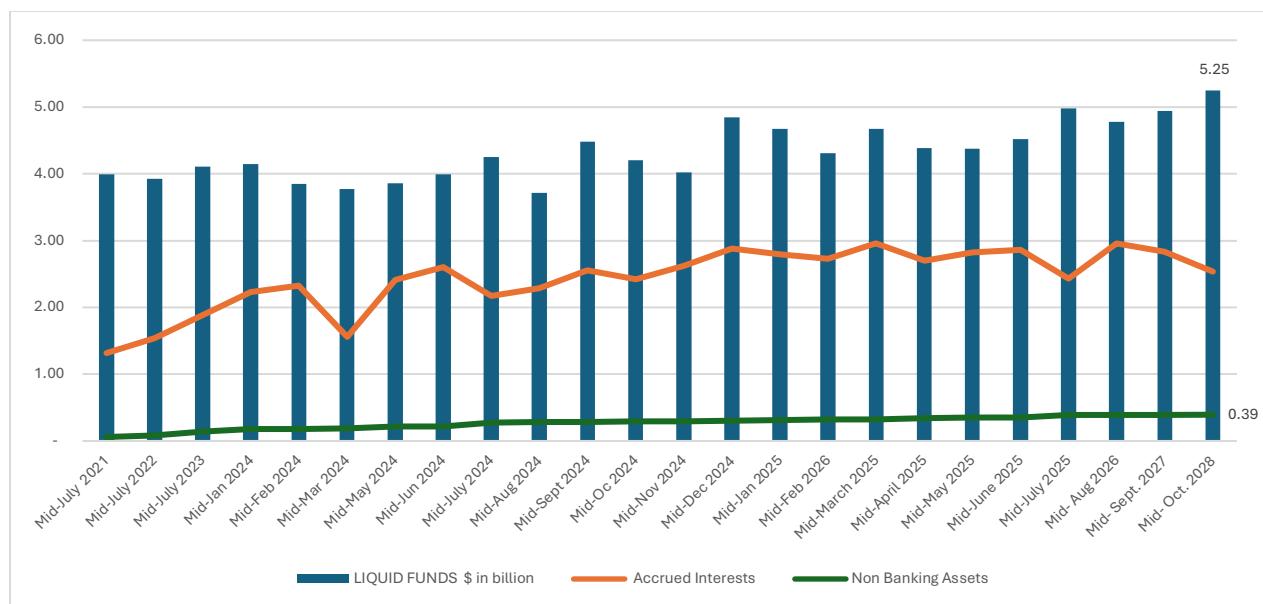
The data suggests a correlation between economic performance and banking sector stability. Periods of high GDP growth generally align with lower NPL ratios, reflecting a healthier economic and banking environment, while times of economic contraction tend to correspond with higher NPL ratios, indicating stress within the banking sector.



From mid-July 2021 to mid-August 2025, a steady rise in accrued interest, from USD 1.32 billion to USD 2.96 billion (2.43 billion June 2025), suggests a growing volume of interest income yet to be received, driven by delayed loan repayments. This trend indicates an over-optimism in credit operations and also reflects potential stress in loan recovery.

In contrast, liquid funds have shown fluctuations without a consistent upward trend, hovering around USD 4.98 billion (4.78 billion August 2025), which implies that institutions have significantly increased their liquid reserves due to lower credit deployment. This may point to excess liquidity buffers or a deliberate shift in asset allocation to low risky assets has supported increasing cash-equivalents.

Meanwhile, non-banking assets, rising gradually from USD 0.06 billion to USD 0.39 billion (0.39 billion in July 2025), reflect increased holdings in foreclosed properties or other non-core assets, typically acquired through loan defaults. The concurrent rise in accrued interest and non-banking assets, alongside relatively stagnant liquid assets, suggests that financial institutions are facing higher credit risk and delayed recoveries, which could be putting pressure on their balance sheet resilience and liquidity position.



## 3) BFIs Outlook 2024/25, 2025/26, 2026/27 and 2027/28

Assets and Liability (Exchange Factor \$ 1 = NPR 130)								
Capital, Deposits and Risk Assets. USD in million								
Particulars	Jul-25	Change	July 2026e	Change	July 2027e	Change	July 2028e	Change
CAPITAL FUND	5,965	6.41%	7,093	18.91%	7,332	3.38%	7,578	3.35%
PAID UP CAPITAL	3,412	1.65%	3,452	1.16%	3,485	0.97%	3,520	0.99%
BORROWINGS	1,808	-2.41%	1,606	-11.21%	1,287	-19.87%	979	-23.92%
Borrowing from NRB	3	10.31%	2	-25.08%	4	50%	4	14%
DEPOSITS	56,181	12.44%	63,563	13.14%	70,912	11.56%	78,289	10.40%
Current	4,061	38.26%	3,380	-16.76%	3,516	4.01%	3,291	-6.40%
Saving	20,565	36.79%	28,101	36.65%	34,520	22.84%	8,138	-76.42%
Fixed	26,977	-3.73%	26,169	-2.99%	25,649	-1.99%	41,466	61.67%
Call	4,209	15.80%	5,535	31.50%	6,846	23.69%	8,138	18.87%
Others	369	9.10%	378	2.30%	381	0.70%	385	1.09%
LIQUID FUNDS	4,979	17.00%	5,693	14.33%	6,333	11.25%	6,874	8.55%
GOVT. SECURITIES/OTHER	13,409	18.49%	16,893	25.98%	19,874	17.65%	23,540	18.44%
Investment in share and other	2,811	32.54%	3,188	13.42%	3,927	23.18%	5,070	29.12%
LOANS & ADVANCES	43,010	8.18%	46,294	7.64%	50,122	8.27%	54,125	7.99%
Total Capital/RWA	12.45%	-3.86%	13.44%	7.90%	12.57%	-6.45%	11.77%	-6.39%
CD	75.27%	-3.54%	71.87%	-4.52%	70.01%	-2.59%	68.68%	-1.90%
NPL /Total Loan	4.62%	18.44%	3.96%	-14.20%	3.84%	-3.03%	4.16%	8.19%
Return on Capital Employed	10.23%	1.45%	16.15%	57.91%	16.60%	2.79%	16.44%	-0.97%

Profit and loss. USD in million								
	Jul-25	Change	July 2026e	Change	July 2027e	Change	July 2028e	Change
Int on Loans and Adv.	3,698	-18.28%	3,038	-17.85%	2,808	-7.59%	2,435	-13.28%
Total Int. Income	4,363	-15.86%	3,769	-13.62%	3,251	-13.74%	2,793	-14.11%
<u>Avg. Yield From Loan</u>	8.08%	-18.66%	6.30%	-22.06%	5.60%	-11.09%	4.50%	-19.70%
Int Expenses	2,694	-23.19%	1,702	-36.82%	1,473	-13.48%	1,202	-18.40%
Avg. Cost of Fund	4.46%	-22.52%	2.49%	-44.15%	2.08%	-16.61%	1.54%	-26.09%
<b>NII</b>	<b>1,669</b>	<b>-0.55%</b>	<b>2,067</b>	<b>23.84%</b>	<b>1,778</b>	<b>-13.95%</b>	<b>1,591</b>	<b>-10.55%</b>
Interest Spread	3.62%	-13.34%	3.50%	-3.41%	3.52%	0.72%	2.96%	-15.93%
Commission & fees	263	11.83%	238	-9.79%	205	-13.82%	171	-16.40%
Ex. Fluctuation Gain	74	51.16%	71	-3.84%	70	-1.13%	70	-0.01%
Other Operating & Non-operating Income	109	56.02%	300	175.07%	506	68.84%	709	40.02%
Gross Income	2,115	4.08%	2,675	26.48%	2,560	-4.32%	2,541	-0.73%
Employees Exp	524	7.00%	539	2.95%	559	3.64%	587	4.99%

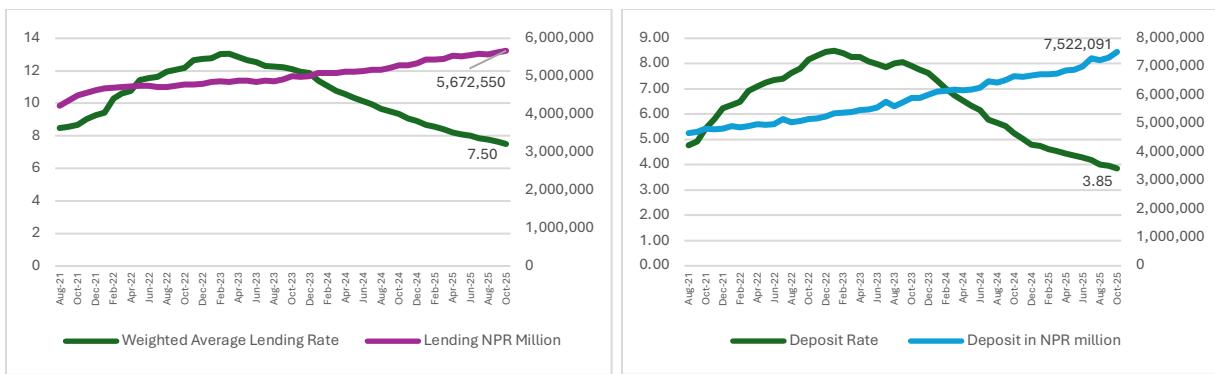
Employee cost in % of Total Int. Income	12.01%	27.17%	14.31%	19.18%	17.20%	20.14%	21.02%	22.24%
Office Operating Exp	334	1.06%	301	-10.06%	289	-3.92%	284	-1.68%
LLP & write-off	759	13.85%	416	-45.22%	217	-47.85%	170	-21.44%
Additional LLP to Risk Assets	1.87%	12.98%	0.90%	-51.94%	0.43%	-51.84%	0.31%	-27.25%
Provision Written Back	450	35.19%	360	-20.00%	396	10.00%	435	10.00%
<b>PBT</b>	<b>947</b>	<b>7.95%</b>	<b>1,779</b>	<b>87.78%</b>	<b>1,890</b>	<b>6.27%</b>	<b>1,935</b>	<b>2.35%</b>
Return on total assets	1.36%	-1.86%	2.33%	70.71%	2.25%	-3.39%	2.09%	-6.96%

Particulars	\$ in million			
	Expected July 25	Expected July 26	Expected July 27	Expected July 28
Total Operating Income	4,809	4,378	4,032	3,743
Total Operating Expenses	<b>3,553</b>	<b>2,543</b>	<b>2,321</b>	<b>2,073</b>
Provision Written Back	450	360	396	435
Provision for Risk	(692)	(401)	(202)	(150)
Loan Written Off	(67)	(15)	(15)	(20)
Net Profit before Bonus & Tax	<b>947</b>	<b>1,779</b>	<b>1,890</b>	<b>1,935</b>
Bonus	89	167	178	182
Tax	257	483	514	526
Net profit	<b>601</b>	<b>1,128</b>	<b>1,199</b>	<b>1,227</b>

The profit and loss forecast for July 26 to July 28 indicates a period of rising income and strengthening profitability, supported by declining risk provisions. Total operating income is projected to decline from \$4,809 million on July 25 to \$3,743 million by July 28, while operating expenses are expected to remain manageable, dipping to \$2073 million on July 28. Provisions for risk are forecasted to ease significantly, from \$692 million on July 25 to just 150 million on July 28, providing a major boost to earnings.

Loan write-offs are expected to remain minimal, ranging between \$67 million and \$20 million. As a result, net profit before bonus and tax is projected to rise from \$947 million to a peak of \$1,890 million on July 27, slightly high at \$1,935 million on July 28. After adjusting for bonuses and tax obligations, net profit is forecasted to increase from \$601 million to a high of \$1,227 million on July 28, with significant surge expected on July 26. Overall, the outlook suggests strong profit growth, with peak performance expected on July 28, driven by higher income and lower provisions, though rising costs and taxes may soften gains toward the end of the period.





### Weighted Average Lending Rate vs Lending Growth

The weighted average lending rate rises steadily from approximately 8.5% in August 2021 to a peak of 13.03% in January 2023. Following this peak, the rate declines consistently, reaching 7.76% by August 2025. Meanwhile, lending exhibits relatively stable growth at around NPR 5,591 billion in July 2025 but witnessed moderate increase to NPR 5,641 billion by November 2025.

Lending growth initially appears less responsive to rising interest rates, remaining stable or increasing moderately despite higher rates (2021 to early 2023). After rates begin to fall in 2023, lending growth continues rising, suggesting that lower interest rates positively support lending growth. There is some inverse relationship between lending rates and lending growth, but the impact is not immediate. It suggests that businesses and consumers are more responsive to sustained rate changes over time rather than short-term fluctuations.

### Deposit Rate vs Deposit Growth

The deposit rate rises sharply from Aug 2021 (~5%) to 8.51% by early 2023. Post Jan 2023, the rate starts declining to 4.02% by August 2025. Deposits in NPR million increase steadily, with significant growth after early 2023, reaching a peak of NPR 7,513 billion (slight increase from mid July 7,477 billion) by November 2025. Deposit growth appears positively correlated with higher deposit rates initially. Even as rates decline in 2023-2024, deposits continue to grow, suggesting other factors like improved economic confidence or liquidity may play a role. Higher deposit rates initially stimulate deposit growth. However, growth continues even as rates fall, indicating that deposits may not solely depend on rates but are influenced by broader economic conditions and liquidity.

#### Interest rates and lending growth:

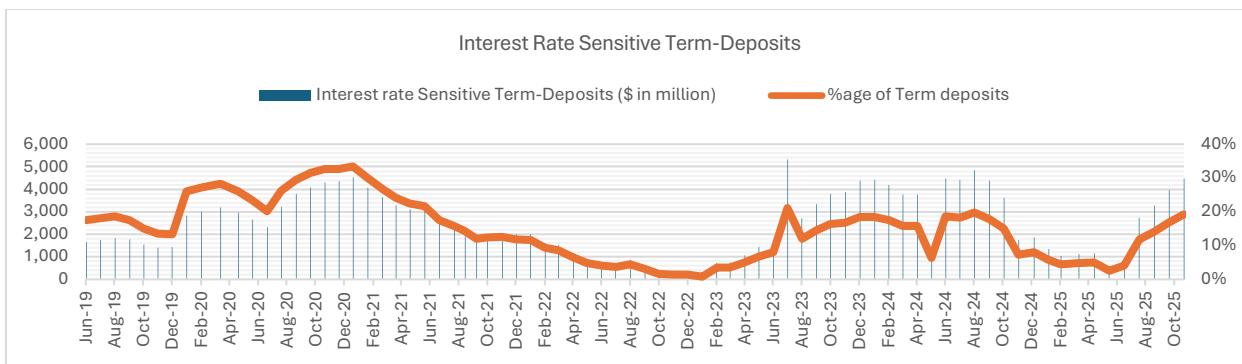
Lending growth is more resilient to short-term changes in interest rates but shows an inverse relationship over time. Lower rates encourage lending growth.

#### Interest rates and deposit growth:

Deposit growth responds positively to higher rates but continues rising despite rate reductions, indicating a more complex relationship influenced by confidence and liquidity.

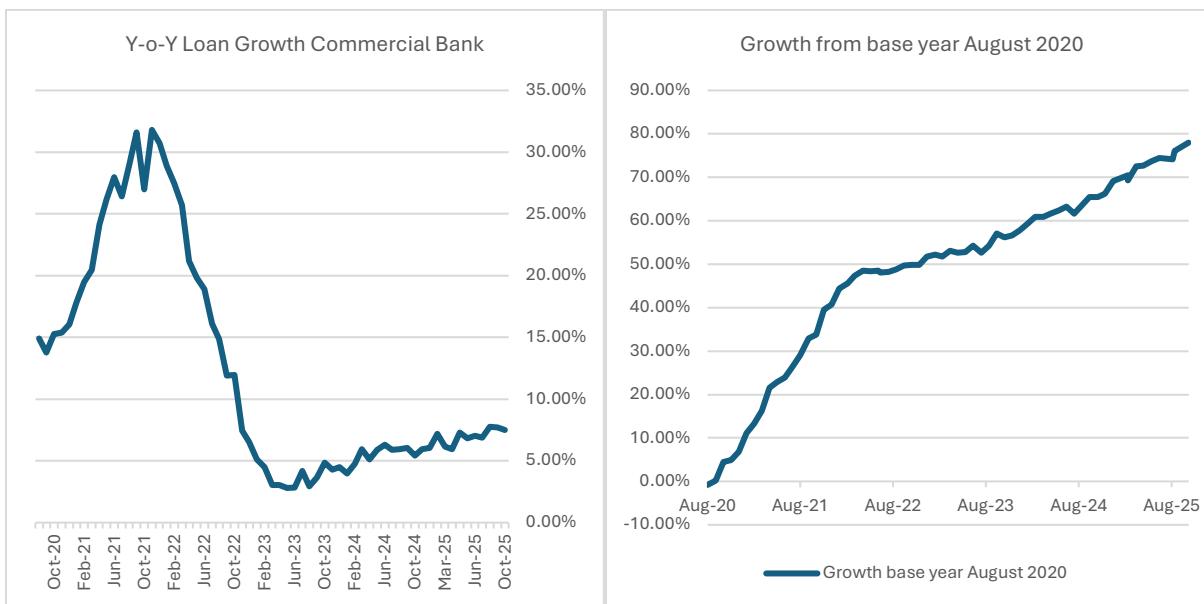
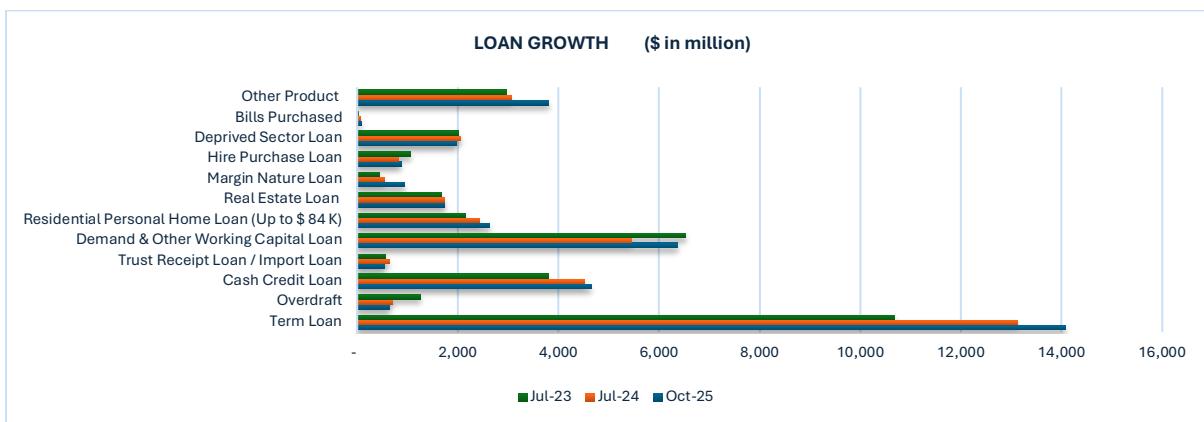
In summary, while interest rates influence growth in deposits and lending, the relationship is not perfectly direct. External economic factors, confidence, and liquidity conditions also play a major role in determining overall growth.

Amount in million		Net Maturity Amount in \$ million			
Period	Deposit mix	Within next month	Within a Year	Total	
<b>3-6 months</b>	19%	318.30	3,945.85	4,264.15	
<b>6-12 months</b>	35%	2,121.12	6,314.80	8,435.92	
<b>1-2 yrs.'</b>	20%	166.68		4,405.43	
<b>2 yrs. and above</b>	26%	1,866.97		4,172.15	
<b>Total</b>	100%	19.19%	44.02%	<b>100%</b>	



Although interest rate-sensitive fixed deposits are experiencing a decline, fluctuations in the short-term money market are likely to persist. Nonetheless, we expect interest rates to remain subdued over an extended period. The deposit mix of the Nepalese banking sector over the past several months reveals a clear shift in depositor behavior, largely influenced by declining interest rates on fixed deposits. From August 2023 to July 2025, there has been a noticeable increase in saving deposits, both in absolute terms and as a proportion of total deposits. This trend suggests that depositors are gradually favoring more flexible savings accounts over long-term fixed deposits, likely due to the narrowing interest rate differential.

#### 4) Sector wise Loan Growth of Commercial Banks



## Section 6 Insurance Sector

### 1) Insurance and Financial Sector Performance: FY 2024/25

Nepal's financial sector, comprising both the insurance industry and the banking system, faced a challenging year in FY 2024/25 marked by a surge in claims, property damage, and credit losses arising from the Gen Z protest and widespread flooding. Despite these shocks, the insurance sector demonstrated resilience, recording strong growth in premium collection, coverage, and capital formation, while the banking sector grappled with significant disruptions to borrowers and physical infrastructure.

### 2) Insurance Sector Overview

The insurance industry continued to expand, with Gross Premium Collection reaching NPR 227.18 billion, a 14.75% increase from the previous fiscal year. Life insurance premiums grew by 16.47% and non-life by 8.3%, driven by heightened risk awareness and policy renewals in the aftermath of the crises. Population coverage improved notably, life insurance coverage excluding foreign employment policies rose from 36.53% to 39.99%, while inclusion of such policies lifted overall coverage to 48.33%, reflecting deeper insurance penetration across demographics.

Insurance penetration, measured as the ratio of gross premium to GDP, increased from 3.47% to 3.72%, and insurance density rose by 13.74%, reaching NPR 7,330 per capita. These gains highlight insurance's expanding role in household and corporate risk mitigation.

However, claim settlements surged, reflecting the financial impact of both the protests and floods.

- Life insurance claims rose by 18.61% to NPR 78.98 billion, alongside an 8% increase in the number of claims paid.
- Non-life insurance claims grew sharply by 41.12%, reaching NPR 25.26 billion, largely due to damage to commercial, industrial, and transport assets during the unrest and natural disaster events.

Despite these pressures, insurers strengthened their balance sheets, with total investments up by 10.24% to NPR 829.40 billion, and paid-up capital increasing by 13.15% to NPR 99.44 billion. Employment indicators also improved, with the number of insurance agents up by 21.37% and surveyors by 13.29%, underscoring the sector's adaptive capacity and expansion of its service base.

### 3) Impact on commercial sector

Although a large portion of government properties damaged during the recent protests and floods were uninsured, the commercial sector is expected to lodge insurance claims totaling around NPR 40 billion. The private sector suffered significant losses due to extensive physical damage, operational disruptions, and potential loan impairments. Preliminary estimates suggest that over 700 borrowers have been affected, with a combined sanctioned credit limit exceeding NPR 175 billion, outstanding exposure of more than NPR 115 billion, and an estimated total loss above NPR 40 billion.

Banking and financial institutions (BFIs) also reported widespread damage to infrastructure, including over 50 branches, 90 ATMs, and 70 extended counters either vandalized or destroyed. These disruptions have severely hampered service delivery and credit recovery, eroded business confidence, and strained liquidity in affected areas. While most BFIs have insurance coverage, the scale of destruction has led to a sharp rise in insurance claims, delayed loan repayments, and increased provisioning requirements across the financial system.

### 4) Overall Assessment

Indicator	Sub Indicators	F.Y. 2080/81	F.Y. 2081/82	Changes %
<b>Gross Premium Collection (in NPR Billion)</b>	Life Insurance	156.50	182.27	16.47%
	Non-Life Insurance	41.47	44.91	8.30%
	Total	Rs 197.97	Rs 227.18	14.75%
<b>Population % Covered By Life Insurance</b>	Excluding FE Policies	36.53	39.99	9.47%
	Including FE Policies	43.27	48.33	11.69%
<b>Insurance Penetration (Percentage of Gross Premium to GDP)</b>	Life Insurance	2.74	2.98	8.76%
	Non-Life Insurance	0.73	0.74	1.37%
	Total	Rs 3.47	Rs 3.72	7.20%
<b>Total Investment (in NPR Billion)</b>	Life Insurance	683.84	759.66	11.09%
	Non-Life Insurance	68.53	69.74	1.77%
	Total	Rs 752.37	Rs 829.40	10.24%
<b>Life Insurance Claim (Amt. in NPR Billion)</b>	Nos. of Gross Claim Paid	280,151.00	302,659.00	8.03%
	Amt. of Gross Claim Paid	66.59	78.98	18.61%
<b>Non-Life Insurance Claim (Amt. in NPR Billion)</b>	Nos. of Gross Claim Paid	151,884.00	150,639.00	-0.82%
	Amt. of Gross Claim Paid	17.90	25.26	41.12%
<b>Direct Employment (in Nos.)</b>	Direct Employment	11,951.00	12,336.00	3.22%
<b>Insurance Agents (in Nos.)</b>	Insurance Agents	329,572.00	400,000.00	21.37%
<b>Surveyors (in Nos.)</b>	Surveyors	1,249.00	1,415.00	13.29%
<b>Paid Up Capital (in NPR Billion)</b>	Life Insurance	60.08	70.09	16.66%
	Non-Life Insurance	5,147.24	5,934.01	15.29%
	Total	Rs 5,207.32	6/4/10	15.30%

The latest data on Nepal's insurance sector shows a year of broad-based expansion, marked by rising premiums, wider population coverage, and strong investment growth—especially in life insurance. Gross premium collection increased by 14.75%, driven primarily by life insurance, which grew by 16.47%, while non-life insurance expanded by a moderate 8.30%. Coverage indicators also improved, with the share of population insured under life policies rising to 39.99% (excluding foreign employment policies) and 48.33% including them, an impressive annual increase of 9.47% and 11.69% respectively.

Insurance penetration in the economy strengthened as total premiums reached 3.72% of GDP, reflecting a 7.20% rise, supported mainly by the life segment. Investment by insurers grew significantly to NPR 829.40 billion, with life insurers contributing most of the 10.24% overall increase. Claims data highlights mixed trends: life insurance claims grew both in volume (8.03%) and value (18.61%), while non-life saw a slight decline in number of claims but a sharp 41.12% rise in claim amounts, indicating higher severity of the Gen Z protest. Despite the sector's overall expansion, insurance density remains stagnant at zero, suggesting that premium levels per capita are not being effectively captured or reported. Overall, the sector shows positive momentum with deeper market penetration, increased policy uptake, and expanding investment capacity, though challenges remain in broadening per-capita engagement and managing rising claim burdens in non-life insurance.

## Section 7 Capital Market

### 1) Impact of IPO Delays by SEBON on Market Trust and Governance Concerns

- a) The Securities Board of Nepal (SEBON) currently faces significant scrutiny due to extended delays in the approval of Initial Public Offering (IPO) applications, as evidenced by the IPO pipeline data as of 2082.01.28. These delays, observed across multiple sectors and types of companies, have increasingly created mistrust in the capital market, raising serious concerns about regulatory mismanagement and potential rent-seeking behavior.
- b) An analysis of the pipeline data reveals that the delays are not isolated to one segment of the market. IPOs across all categories—including hydropower, manufacturing, hospitality, investment companies, and insurance—have been pending for extended periods. The number of shares offered ranges from under 100,000 to over 30 million, with corresponding issue amounts ranging from NPR 10 million to over NPR 6 billion. Despite the variation in size and sector, delays are prevalent across the board, suggesting systemic inefficiencies within SEBON's approval mechanism.
- c) Furthermore, many IPO applications date back over 12 to 18 months, some with little to no movement despite the submission of responses and required documentation by the issuing companies. This stagnation has created the perception of a regulatory bottleneck that is not just administrative but potentially influenced by non-transparent practices. The inconsistency in processing timelines has led stakeholders to question whether certain companies receive undue favor, reinforcing fears of rent-seeking behavior among regulators.
- d) The dominance of ordinary equity shares issues in the pipeline—commonly sought after by retail and institutional investors alike—means that delays in their approval have an outsized impact on market sentiment. Investors are left uncertain about capital allocation, and companies are unable to capitalize on favorable market conditions. Such inefficiencies discourage broader participation in the market and undermine the goal of financial inclusion.
- e) SEBON's inaction and lack of timely communication have not only delayed capital formation but also damaged its institutional credibility. The perception that approvals may depend on informal networks or discretionary influence rather than objective criteria further deteriorates trust. This environment of uncertainty and suspicion is detrimental to Nepal's evolving capital markets.
- f) Recommendations

SEBON's prolonged indecision in processing IPO applications has become a significant obstacle to market growth. It has fostered widespread doubt about regulatory governance, amplified concerns about rent-seeking behavior, and discouraged participation from both issuers and investors.

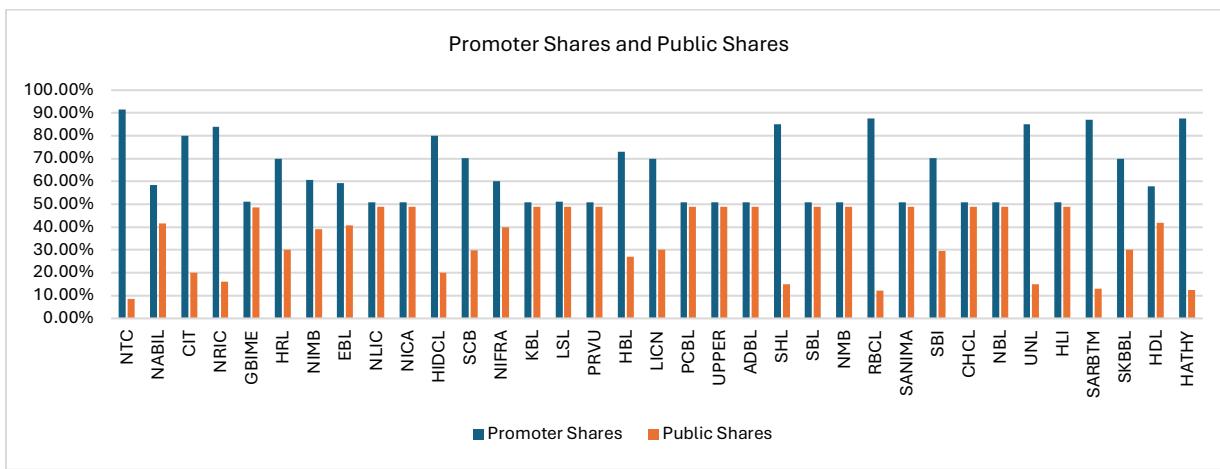
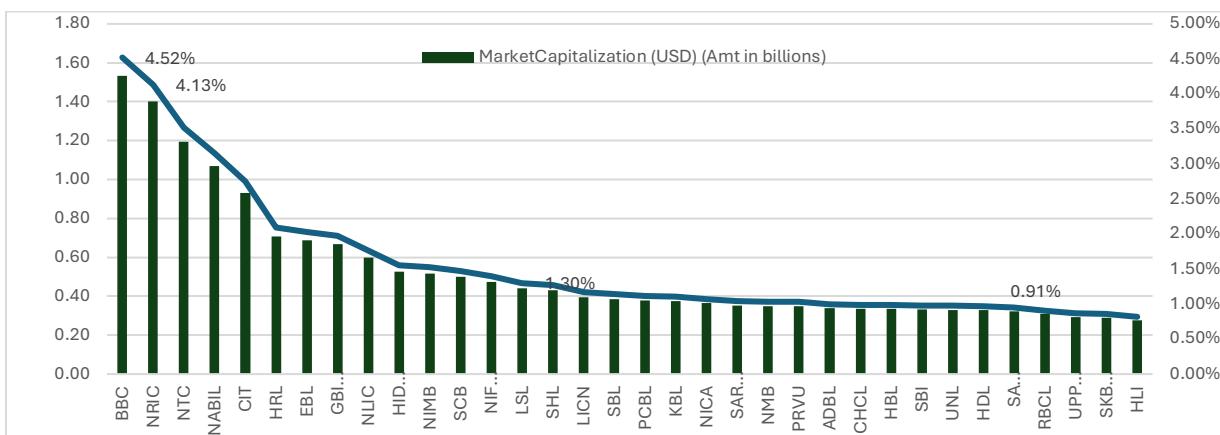
- a) To restore trust and improve market efficiency, SEBON must:
- b) Implement a transparent, time-bound IPO approval process.
- c) Increase accountability within the regulatory framework.
- d) Introduce digital tools to streamline tracking and evaluation.

Without urgent reforms, the credibility and effectiveness of SEBON as a regulator will continue to decline, putting the integrity of Nepal's capital market at risk.





The 34 companies listed on NEPSE make up 53.44 % of the total market capitalization, with most of their shares not available for free trade.



#### Section 8 Fiscal Situation

##### 1) Government of Nepal Receipts & Payments Status

(Exchange Factor \$ 1 = NPR 130 )

Government Receipts & Payments Status	Annual Budget	11/23/2025	% age
1. Revenue (USD in million)	11,384.62	2,097.99	18.43%
a) Tax Revenue	10,196.80	1,966.88	19.29%
b) Non Tax Revenue	1,187.82	131.11	11.04%
2. Grants	411.13	16.17	3.93%
3. Other Receipts	-	17.50	
Total Receipt	11,795.75	2,131.66	18.07%
2. Total Expenditure from Treasury	15,108.54	3,199.43	21.18%
a. Recurrent	9,084.46	2,137.62	23.53%
b. Capital	3,137.60	157.32	5.01%
c. Financing	2,886.48	904.49	31.34%
Deficit	(3,312.79)	(1,067.77)	
% of GDP	7.06%	2.28%	

##### 2) Government Treasury position

3) (Exchange Factor \$ 1 = NPR 119 ). (USD in million)

	Mid-Month	August	September	October	November	December	January	February	March	April	May	June	July
F/Y 2023/24	Expenditure	287	942	2,289	3,773	4,709	5,685	5,685	6,498	7,328	8,543	9,709	11,361
	Revenue	663	1,186	1,841	3,054	4,172	4,768	4,768	5,370	6,286	6,991	7,724	8,898
	Treasury Position	1,756	1,614	1,441	1,579	1,989	1,809	1,809	1,722	2,636	2,351	2,114	834
F/Y 2024/25	Expenditure	338	1,156	2,766	3,689	4,673	5,610	6,343	7,053	8,391	9,730	10,781	12,799
	Revenue	815	1,398	2,086	2,798	3,410	4,703	5,544	6,209	7,189	7,752	8,776	10,250
	Treasury Position	1,662	2,265	1,476	1,800	1,847	2,502	2,942	3,297	3,124	3,033	2,857	1,099
F/Y 2024/25	Expenditure	389	1,514	3,064									
	Revenue	716	1,344	2,128									
	Treasury Position	1,905	2,148	1,470									

##### 4) Gross Value Added by Industrial Division

Industrial Classification. Rs. millions	2022/23	2023/24	2024/25		2024/25
Agriculture, forestry and fishing	11,43,101	12,48,694	13,53,729	UP	25.16
Mining and quarrying	24,009	24,020	24,776	UP	0.46
Manufacturing	2,43,679	2,49,252	2,67,803	UP	4.98
Electricity and gas	76,908	84,187	93,237	UP	1.73
Water supply; sewerage and waste management	21,735	22,052	22,788	UP	0.42
Construction	2,76,190	2,72,725	2,81,639	UP	5.24
Wholesale and retail trade; repair of motor vehicles and motorcycles	6,69,055	7,07,522	7,82,958	UP	14.55
Transportation and storage	3,18,739	3,42,873	3,87,578	UP	7.20
Accommodation and food service activities	92,682	1,21,423	1,32,546	UP	2.46

Industrial Classification. Rs. millions	2022/23	2023/24	2024/25	Rs. millions	2024/25
Information and communication	92,741	97,832	1,04,251	UP	1.94
Financial and insurance activities	3,33,778	3,31,032	3,57,655	UP	6.65
Real estate activities	4,02,323	4,24,376	4,46,100	UP	8.29
Professional, scientific and technical activities	45,408	49,982	52,084	UP	0.97
Administrative and support service activities	33,060	36,038	38,768	UP	0.72
Public administration and defence; compulsory social security	4,67,358	4,81,098	4,69,164	DOWN	8.72
Education	3,95,230	4,31,635	4,23,513	DOWN	7.87
Human health and social work activities	90,993	94,877	1,02,638	UP	1.91
Other Services	30,401	33,787	38,363	UP	0.71

##### 5) High-Growth Sectors: Small but Rapidly Expanding

###### High-Growth Sectors: Small but Rapidly Expanding

Several smaller sectors posted impressive growth rates, indicating dynamic shifts in emerging industries:

- Electricity and gas saw the highest growth rate at 13.82%, though it contributes only 1.73% (NPR 93.24 billion) to GDP.
- Transportation and storage grew by 9.45%, contributing a significant 7.20% (NPR 387.58 billion) — both a fast-growing and sizeable sector.
- Financial and insurance activities expanded by 6.29%, with a 6.65% share (NPR 357.66 billion), suggesting healthy sectoral modernization and financial deepening.
- Accommodation and food services grew by 5.00%, though still relatively small at 2.46% (NPR 132.55 billion).
- Information and communication rose by 4.81%, contributing 1.94% (NPR 104.25 billion).
- Human health and social work grew by 4.77%, reflecting post-pandemic recovery in health investment.

These sectors, although not the largest in value, point to a shift toward services, logistics, and utilities, showing a diversification of growth sources beyond traditional agriculture and trade.

##### 6) Mid-Sized Productive Sectors: Stable, Foundational Growth

###### Mid-Sized Productive Sectors: Stable, Foundational Growth

A cluster of **productive sectors** with both moderate size and growth rate form the **core of Nepal's structural economic transition**:

**Manufacturing** (NPR 267.80 billion, 4.98% of GDP) grew by **3.78%**, reflecting modest industrial growth.

**Construction** (NPR 281.64 billion, 5.24%) grew by **2.21%**.

**Wholesale and retail trade** (NPR 782.96 billion, 14.55%) saw **3.30% growth**, maintaining its dominant role in value addition.

These sectors are **key drivers of employment and investment**, and their **steady expansion** supports infrastructure, trade, and industrialization goals.

7) *Traditional Large Sectors: Slow or Declining Performance***Traditional Large Sectors: Slow or Declining Performance**

The **largest sectors by value** showed either **slow growth or contraction**, highlighting challenges in transforming the economic base:

- **Agriculture, forestry, and fishing** remains the largest sector at **NPR 1,353.73 billion (25.16%)**, but grew by only **3.28%** — a low rate relative to its economic weight.
- **Real estate activities** contributed **NPR 446.10 billion (8.29%)** but grew by just **2.72%**.
- **Public administration and defence** (NPR 469.16 billion, 8.72%) and **education** (NPR 423.51 billion, 7.87%) both saw minimal growth of **2.24%** and **1.98%**, respectively — likely reflecting tighter public budgets or reduced fiscal momentum.

Despite their large contribution to GDP, these sectors are **no longer the main engines of growth**, signaling potential saturation or policy constraints.

8) *Government Revenue*

**Amount in USD million (Exchange Factor 1 UAS = 130 NPR)**

HEADS	Apr-25	May-25	Jun-25	Jul-25	Aug-25	Sep-25	Oct-25	Nov-25	compared to Last year
Customs	163,692	184,458	207,508		16,652				
<b>Import Duties</b>	130,774	147,434	165,653						
<b>Green Tax</b>	-	-	-		-				
<b>Export Duty</b>	491	601	719						
<b>Infrastructure Tax</b>	15,336	17,172	19,169						
<b>Other incomes of Custom</b>	481	532	653						
<b>Agriculture Reform Duties</b>	5,610	6,176	6,692						
<b>Road Maintenance and Improvement Duty</b>	7,366	8,357	9,416						
<b>Road Construction and Maintenance Duty</b>	3,634	4,185	5,205						
<b>Value Added Tax</b>	239,874	269,601	302,518		27,611				
<b>Production, Sales and Service</b>	100,882	113,299	127,187						
<b>Imports</b>	138,992	156,302	175,331						
<b>Excise Duties</b>	123,981	142,413	161,921		13,891				
<b>Internal Production</b>	91,496	105,583	119,508						
<b>Excise on Imports</b>	32,485	36,830	42,414						

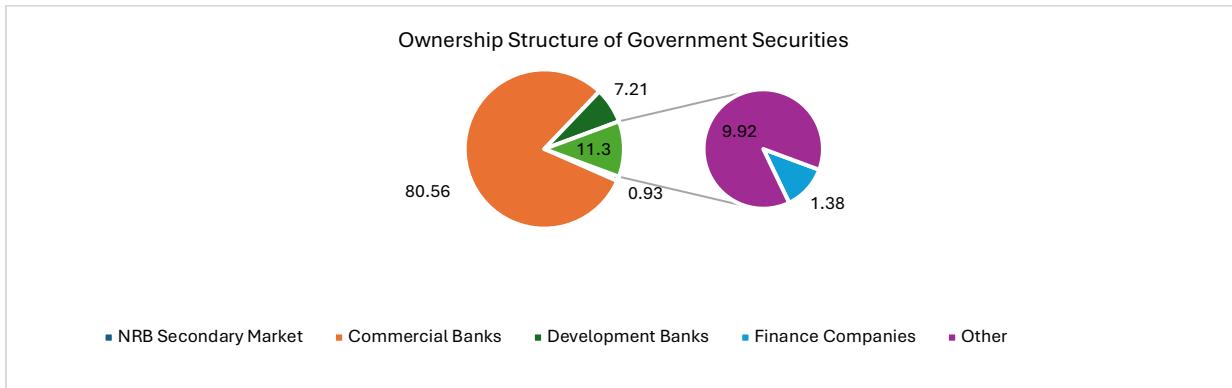
Educational Service Tax	2,981	3,381	3,679		417				
Income Tax	<b>213,607</b>	<b>229,089</b>	<b>242,375</b>		<b>22,416</b>				
<b>Income Tax</b>	189,981	200,791	213,349		16,710				
<b>Interest Tax</b>	23,626	28,299	29,027		5,706				
Total Tax Revenue	<b>744,135</b>	<b>828,942</b>	<b>918,002</b>	1,049,875	80,986	1,575,334	249,051	326,550	12.64%
<b>Non Tax Revenue</b>	87,235	93,490	98,084	128,945	3,803		2,007	3,489	-89.54%
Total Revenue	<b>831,371</b>	<b>922,432</b>	<b>1,016,085</b>	<b>1,178,820</b>	<b>84,789</b>	<b>1,588,070</b>	<b>251,059</b>	<b>330,039</b>	2.10%
<b>Other Receipts</b>	9,763	11,209	11,584	40,898	309	11,783	2,129	2,964	-48.67%
Total Receipts	<b>841,133</b>	<b>933,641</b>	<b>1,027,670</b>	<b>1,219,719</b>	<b>85,098</b>	<b>1,599,853</b>	<b>253,188</b>	<b>333,003</b>	1.21%

9) Key Indicators

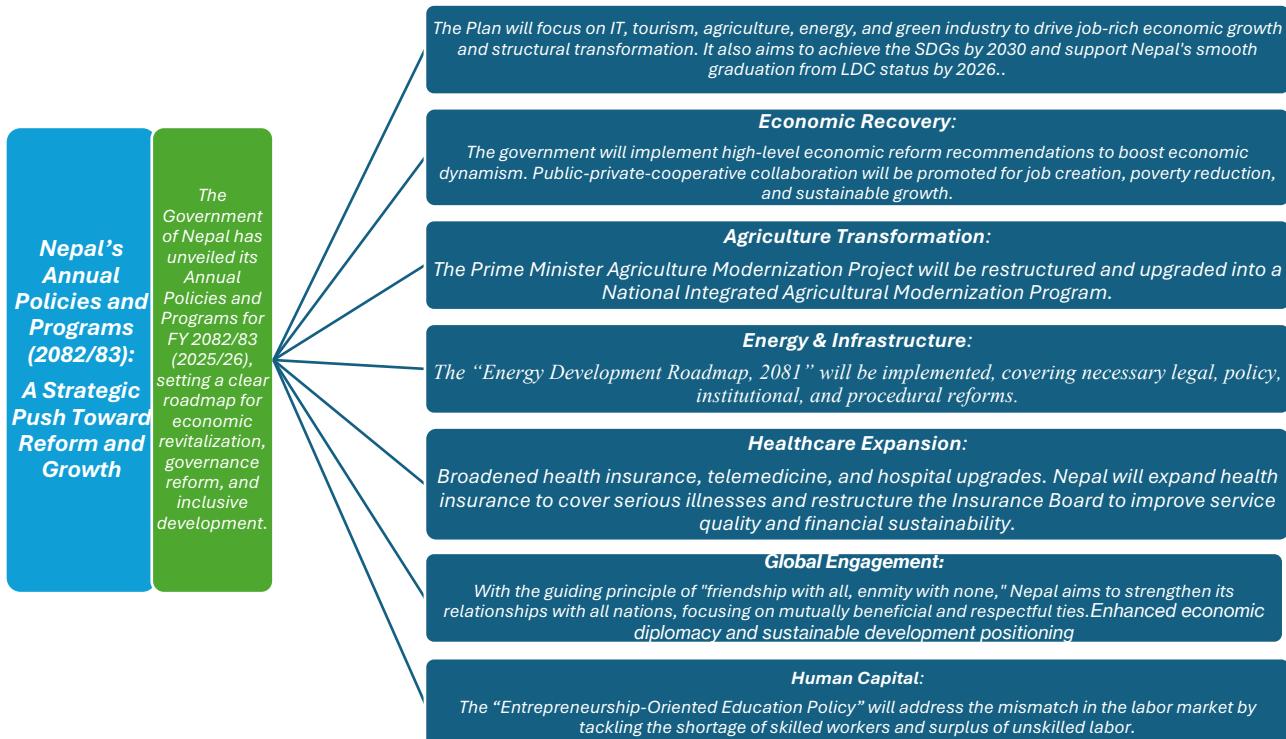
Indicator	2023/24 (to October 2024)	2024/25 (to October 2025)
CPI-based Inflation (y-o-y)	4.82%	1.47%
Trade	Imports ↓4.2%; Exports ↓6.1%;	Imports ↑19.8%; Exports ↑89.6 %;
Remittances	↑15.1% (NPR), ↑13.29% (USD)	↑35.4% (NPR), ↓29.2% (USD)
Balance of Payments	Surplus Rs. 184.99 billion	Surplus Rs. 237.59 billion
Gross Foreign Exchange Reserves	USD ↑16.60 billion	↑USD 21.21 billion
Government Expenditure	Rs. 329.20 billion	Rs. 364.59 billion
Government Revenue	Rs. 284.26 billion	Rs. 249.05 billion
Broad Money (M2)	y-o-y expansion: 13.3%	y-o-y expansion: 12.2%
BFI Deposits	↑2.6 y-o-y: ↑12.8%	↑3%; y-o-y: 13%
Private Sector Credit	↑2.6 y-o-y: ↑6%	↑1.5%; y-o-y: 7.3%

	Heading	2021/22	2022/23	2023/24	2024/25
A	Real Sector (growth and ratio in percent)				
	Real GDP at basic price	5.3	2.3	3.4	4.0
	Real GDP at purchasers' price	5.6	2.0	3.7	4.6
	Nominal GDP at purchasers' price	14.3	7.8	6.4	7.0
	Gross National Income (GNI)	14.4	8.5	6.9	6.7
	Gross National Disposable Income (GNDI)	12.4	11.0	8.5	7.4
	Gross Capital Formation / GDP	37.6	31.1	30.4	28.1
	Gross Fixed Capital Formation / GDP	29.0	24.6	24.3	24.1
	Gross Domestic Savings / GDP	6.6	7.2	6.2	6.6
	Gross National Savings / GDP	29.6	33.9	35.4	36.2
	Gross Domestic Product (Current Price) (Rs in billion)	4976.6	5367.0	5709.1	6107.2
	Heading			Mid-August	
		2023/24	2024/25	2024/25	2025/26
B	Public Finance (growth and ratio in percent)				
	Revenue Growth (%)	7.1	10.5	20.1	-10.8
	Expenditure Growth (%)	-2.0	9.3	14.8	15.2

	Domestic Debt (Rs. in billion)	1180.9	1268.2	1200.0	1276.0
	External Debt (Rs. in billion)	1257.9	1401.4	1257.9#	1401.4#
	Revenue / GDP	19.0	19.6		
	Recurrent Expenditure / GDP	16.3	16.1		
	Capital Expenditure / GDP	3.4	3.6		
	Domestic Debt / GDP	20.7	20.8		
	External Debt / GDP	22.0	22.9		

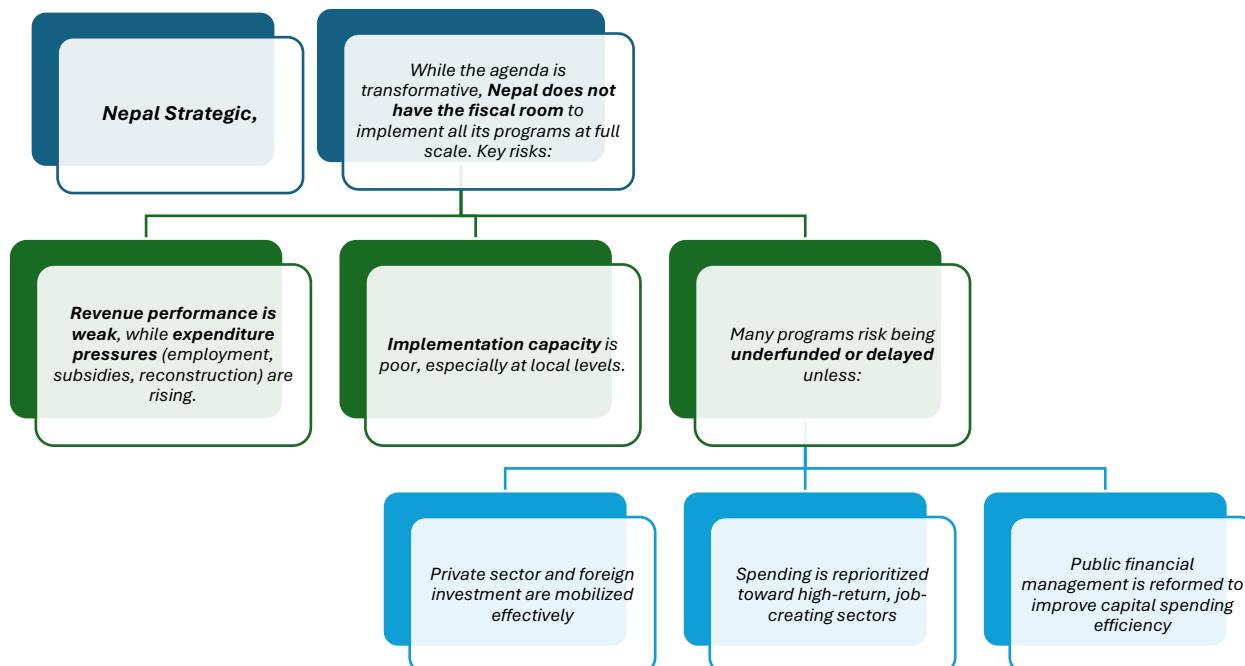


#### 10) Nepal's Policies and Programs for Fiscal Year 2025/26



## 11) Economic and institutional reform - budget 2025/26

					
<b>Economic Revitalization &amp; Fiscal Reform</b>	<b>Assets Management Company &amp; Financial Sector Restructuring</b>  The government will implement high-level economic reform recommendations to boost economic dynamism. Public-private-cooperative collaboration will be promoted for job creation, poverty reduction, and sustainable growth.  Emphasis on reducing trade deficits through productivity-driven import substitution.	<b>Digital Banking &amp; Fintech Ecosystem</b>  A national <b>Assets Management Company</b> will be established to manage non-performing assets and improve financial sector health.  Reforms to address distressed banks and ensure sectoral stability are prioritized.	<b>Agricultural Modernization</b>  A <b>Digital Bank</b> will be promoted to expand financial inclusion and increase digital payment access across Nepal. Policy direction favors fintech integration, cybersecurity, and regulatory innovation.	<b>Infrastructure, Energy, and Trade</b>  The Prime Minister Agriculture Modernization Project will be restructured and upgraded into a <b>National Integrated Agricultural Modernization Program</b> .	<b>Health, Human Capital &amp; Governance</b>  Universal access to clean and renewable energy will be ensured. The " <b>Energy Development Roadmap, 2081</b> " will be implemented, covering necessary legal, policy, institutional, and procedural reforms.  Strengthen the training programs for healthcare professionals.  Education reform aligned with labor market needs, including national skill standards.  Governance reforms include local-level judicial strengthening and harmonized federal laws.



## 12) Nepal Requires an Immediate Economic Rescue Plan to Revive Its Economy

Following the Gen Z protest, Nepal faces one of its most serious economic and institutional crises in decades. The unrest exposed deep vulnerabilities in fiscal management, financial stability, and governance, triggering asset losses, credit disruptions, and weakened market confidence. Nepal urgently needs an integrated Economic Rescue Plan to restore fiscal balance, stabilize the financial sector, and anchor inflation amid deepening political and economic uncertainty. The plan should serve both as a stabilization mechanism, to contain immediate shocks, and a recovery catalyst, rebuilding confidence and supporting reconstruction after political unrest and natural disasters.

A coordinated response, underpinned by political consensus, institutional discipline, and transparent implementation, can turn this crisis into an opportunity for structural renewal.

### Key Pillars of the Rescue Plan

1. Restoring Fiscal Balance
  1. Fiscal balance is now a national priority after widespread damage to public infrastructure and private assets.
  2. Government revenues have contracted sharply, while reconstruction and compensation costs are rising.
  3. A credible fiscal strategy must emphasize:
    - a. Expenditure rationalization and project prioritization.
    - b. Enhanced revenue mobilization through administrative and compliance reforms.
    - c. Strict debt and deficit control to prevent budgetary deterioration.
  4. Sound fiscal discipline will be crucial to restore investor and donor confidence and safeguard Nepal's sovereign credibility.
2. Ensuring Financial Stability
  1. The economic slowdown and unrest have increased Non-Performing Assets (NPAs), Non-Banking Assets (NBAs), and credit defaults, especially in tourism, retail, and manufacturing.
  2. Sudden policy changes, such as the rapid implementation of working capital guidelines, disrupted credit flows and liquidity conditions.
  3. Confidence among lenders and borrowers has weakened, constraining domestic demand.
  4. The government and NRB should:
    - a. Strengthen supervisory oversight and asset quality management.
    - b. Establish a transparent restructuring framework for distressed sectors.
    - c. Provide targeted liquidity support to viable enterprises.
    - d. Implement confidence-building measures to revive credit flows and restore trust in the banking system.
3. Anchoring Inflation
  1. Inflationary pressures have eased but remain vulnerable to political disruptions and market volatility.
  2. Volatile prices of fuel and essentials have eroded purchasing power despite stable reserves and supply chains.
  3. Maintaining price stability requires:
    - a. Disciplined fiscal and monetary coordination.
    - b. Prudent money supply management.
    - c. Strategic import facilitation to stabilize markets and protect households
4. Core Components of the Emergency Economic Plan
  1. Fiscal Measures: Launch an emergency package to rebuild infrastructure, support affected businesses, and curtail non-essential spending.
  2. Financial Sector Reforms: Strengthen prudential norms, provide targeted liquidity injections, and promote inclusive finance for reconstruction.
  3. Monetary Policy Actions: Maintain an accommodative stance to ensure liquidity for productive sectors and job creation.
  4. Governance and Coordination: Establish a High-Level Economic Rescue Task Force to synchronize policy actions among ministries, NRB, development partners, and local governments.
5. Immediate Action Steps
  1. Conduct a rapid, transparent assessment of economic damages and fiscal gaps.
  2. Implement targeted relief and reconstruction programs.
  3. Expedite insurance settlements and credit access for affected enterprises.
  4. Engage development partners for concessional financing and project support.
  5. Strengthen accountability and monitoring frameworks to prevent leakages and rebuild public trust.
6. Anticipated Outcomes
 

A well-executed Economic Rescue Plan will:

  1. Stabilize macroeconomic conditions and restore fiscal discipline.
  2. Revive private-sector confidence and stimulate employment through reconstruction.
  3. Strengthen financial governance and inflation control.
  4. Reinforce structural resilience, laying the groundwork for sustainable and inclusive recovery.

## 7. Conclusion

In the wake of the Gen Z protest, Nepal's economy demands decisive leadership and coordinated reform. An Emergency Economic Rescue Plan, anchored in fiscal prudence, financial stabilization, and transparent governance, can rebuild confidence, attract investment, and reignite growth.

Its success depends on political consensus, institutional coordination, and swift, credible implementation. If executed effectively, this plan can transform today's turmoil into the foundation of a more resilient, equitable, and forward-looking Nepali economy.

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