

NEPAL'S RATING – BUDGET 2026/27

FY 2025/26 Implementation Review ▶ FY 2026/27 Execution Outlook

2025/26 Budget

Rs 1,964B

Capital Used: 52% (EST.)

2026/27 Budget

Rs 2,124B

Largest Ever +25.2%

Revenue Miss '26

–Rs 163B

Only 86.3% (EST.)

GDP Gap '26

3.85%

vs 6% target

- ▶ Budget Implementation Gap 2025/26
- ▶ Sector-wise Execution Capability 2026/27
- ▶ Capital Expenditure Crisis Analysis
- ▶ Revenue & Fiscal Risk Dashboard
- ▶ Development Partner Support Assessment
- ▶ Private Sector Confidence Indicators
- ▶ Political Economy & Governance Risks

FY 2025/26 BUDGET — IMPLEMENTATION SCORECARD

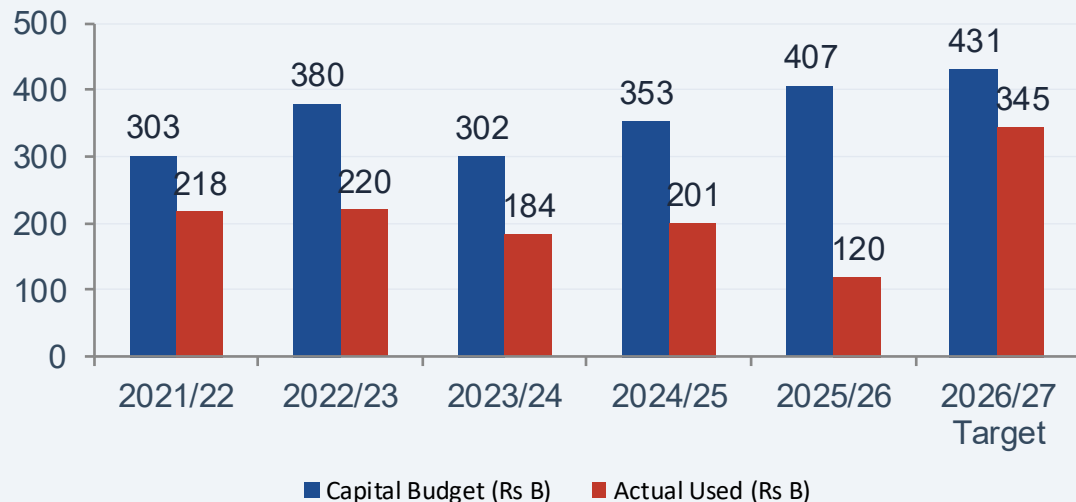
VERDICT: SEVERELY UNDER-EXECUTED | Capital at 52% (Expt.)— Low | Expt. Revenue missed by Rs 280B | GDP achieved: 3.85% vs 6% target

Indicator	Target 2025/26	Revised Outcome	Achievement %
Total Budget Size	Rs 1,964B	Rs 1,670B (est.)	86.37% (est.)— CRITICAL
Revenue Collection	Rs 1,315B	Rs 1,152B (est.)	86.3% (est.) — MISS
Capital Expenditure Used	Rs 407B	Rs 212B (est.)	52% (est.)— CRITICAL
GDP Growth	6.0%	3.85% (est.)	64.2% of target — CRITICAL
Inflation	5.5%	2.13% avg	Better than target
Foreign Grant Utilisation	Rs 53.4B	Rs 30.9B (est.)	~58% — CRITICAL
Foreign Loan Drawdown	Rs 233.4B	Rs 142B (est.)	~61% — CRITICAL
Recurrent Expenditure	Rs 1,181B (60.1%)	~Rs 1.115B (est.)	~94.4% (est.)

Root Causes of Under-execution: Political transition mid-year caused procurement freeze • Treasury deficit constrained releases • Procurement process delays • Low project readiness • Weak contract management at local levels • FATF grey-list impact on foreign grants

CAPITAL EXPENDITURE — 5-YEAR EXECUTION CRISIS

Capital Budget vs Actual Utilisation (Rs Billion)



2025/26 Utilization (Expected) **52%**

Low due to non-economic constraints

5-Year Average **57%**

Consistently sub-par

Historical Best **72%**

FY 2021/22 (post-COVID rebound)

2026/27 Target **≥80%**

Required for 7% GDP growth

GDP Cost '26 **-2pp**

Every 1% utilisation = 0.05–0.07pp GDP

STRUCTURAL REFORM NEEDED FOR 2026/27:

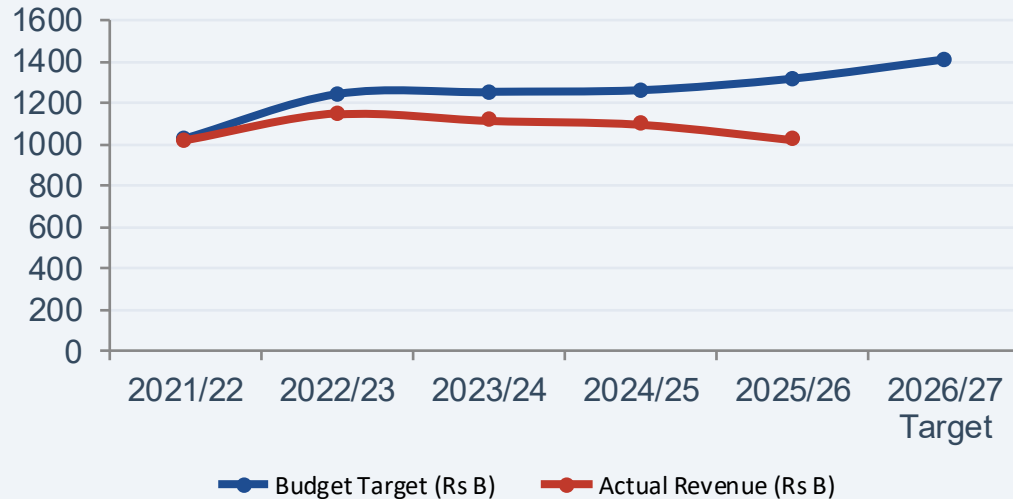
Mandatory e-procurement | Project Prep Facility (PPF) before budget | Performance contracts for chiefs | Sunset law for stalled projects | PPP pipeline activation | Real-time capital tracking dashboard

SECTOR-WISE IMPLEMENTATION CAPABILITY — FY 2026/27

Sector	FY25/26 \$M	FY26/27 \$M	Change	Exec Capability	Risk	Key Implementation Constraint
Economic Affairs (Infrastructure)	2968	3401	+14.6%	MEDIUM	HIGH	PPP pipeline activated; procurement delays endemic; completion of bridges/roads historically slow
Education	459	449	-2.3%	MEDIUM-HIGH	MEDIUM	Recurrent-heavy; teacher salaries reliable; capital (school buildings, labs) historically poor
Health	532	566	+6.5%	MEDIUM	MEDIUM	Drug procurement delays; hospital construction lags; social health insurance expansion manageable
Social Protection	1642	1726	+5.1%	HIGH	LOW	SSF payments and pensions are direct transfers — easiest execution; minimal procurement risk
General Public Svc	7338	7990	+8.9%	HIGH	LOW	Salaries & debt service — mechanical disbursement; reflects fiscal burden, not productive spend
Energy (IT/Hydro)	—	—	New push	LOW	CRITICAL	NEA restructuring + AI computing centre are bold but face legal/regulatory/talent constraints
Agriculture	—	—	Subsidy focus	MEDIUM	HIGH	40% capex subsidy + insurance coverage: implementation via cooperatives; last-mile delivery weak
Environment	98	76	-22.5%	LOW	HIGH	Cut against global commitments; REDD+ and climate finance absorption has been poor historically

REVENUE REALISM & FISCAL SUSTAINABILITY RISK

Revenue Target vs Actuals (Rs Billion)



Revenue Growth Required

+23.7%

Difficult to achieved

Actual Revenue Growth '26

+3.2%

Far below what '26/27 targets need

Fiscal Deficit '27

5.2% GDP

IMF recommends $\leq 3.5\%$

Domestic Borrowing '27

Rs 410B

Crowds out private investment

Public Debt Trajectory

47–50% GDP

Approaching 48% threshold

Treasury Deficit May 2026

Rs 199B

Ongoing fiscal strain

STRUCTURAL FISCAL TRAP: SPENDING OBLIGATIONS EXCEED REVENUES

- ▶ Mandatory obligations (salaries, debt service, pensions, social security) = Rs 1.33T vs Expected revenue = Rs 1.15T
- ▶ Revenue/GDP ratio at ~17% — IMF ECF requires >17.5% for programme compliance. Tax net remains narrow.
- ▶ VAT digital incentive and customs rationalisation are positive structural moves but yield impact is 2–3 years away.
- ▶ Revenue overestimation is systemic — targets missed every year since 2022/23. Credibility gap widening.

DEVELOPMENT PARTNER SUPPORT — ASSESSMENT & RISKS

IMF (ECF Programme) SDR 395M programme ECF review progress — revenue compliance, fiscal deficit reduction, NRB independence reforms required. Any backsliding risks suspension and triggers contagion for other donors.	CONDITIONAL	World Bank \$1.5B+ portfolio Strong project pipeline — energy, education, social protection. BUT absorption capacity is weak. Apr 2026 report cites procurement delays as top bottleneck.	MODERATE	ADB (Asian Dev. Bank) \$800M+ annual ADO Apr 2026 projects 4.9% Nepal growth — below GoN target. ADB support contingent on government reform delivery, esp. PPP framework and financial sector.	MODERATE
India (Bilateral) Largest bilateral Cross-border power trading policy (NEA unbundling) directly impacts India bilateral energy deals. Relationship stable but implementation of power trade framework is complex.	LOW-MEDIUM	Global Trends to Nepal's Economy Trade balance, Current account In FY 2025/26, Nepal's external sector remained resilient, supported by a narrowing trade deficit, a current account surplus, strong foreign exchange reserves, and moderate import growth. However, the 2026/27 outlook points to rising pressure on the trade balance, current account, and reserves, while import growth is expected to place moderate pressure on external stability.	MEDIUM	FATF Grey-list Impact Grant absorption hit Nepal on FATF grey-list — foreign grants fell to 13.52% of target in H1 2025/26 (only \$54.75M of \$404.9M). Exit from grey-list is prerequisite for 2026/27 grant projections.	CRITICAL

⚠️ KEY RISK: FATF Grey-list exit is the single biggest leverage point for development finance. 2026/27 budget assumes \$467M foreign grants — but H1 2025/26 achieved only \$54.75M (13.5%). AML/CFT compliance is a budget execution prerequisite.

PRIVATE SECTOR CONFIDENCE — DRIVERS & CONSTRAINTS

✔ CONFIDENCE BOOSTERS (2026/27 Budget Signals)

- ▶ Income tax threshold doubled to Rs 10L — direct purchasing power boost
- ▶ Max personal income tax rate cut by 10pp — investor retention signal
- ▶ Capital gains tax finalised — certainty for equity market investors
- ▶ Foreign Investment Act amended — NRB prior approval removed for repatriation
- ▶ Limited Liability Partnership law — enables VC/angel investment structures
- ▶ Investment Express: automated 1-stop clearance — reduces friction
- ▶ Excise duty abolished on 360 goods — reduces cost of doing business
- ▶ Company law: conflict-of-interest clarity + easier dissolution
- ▶ Commercial arbitration tribunal — resolves business disputes faster
- ▶ Sovereign Wealth Fund — signals long-term asset management intent

⊘ CONFIDENCE DESTROYERS (Systemic Concerns)

- ▶ Regulatory inconsistency — frequent policy reversals erode business certainty
- ▶ Weak contract enforcement — dispute resolution still slow despite tribunal
- ▶ Capital utilization below average% — signals government is unreliable buyer
- ▶ Treasury deficit Rs 199B — payment arrears to contractors commonplace
- ▶ Revenue overestimation history — tax administration capacity concerns
- ▶ SOE competition: Nepal Airlines, Bishal Bazaar, Gorkhali Rubber — PPP risk
- ▶ Labour market rigidity — industrial relations law unchanged
- ▶ Infrastructure bottlenecks — power/road constraints hurt productivity
- ▶ Exchange rate uncertainty — forex risk hedging new and untested
- ▶ FATF grey-list — banking correspondent risk persists for trade finance

NET ASSESSMENT: Cautiously Optimistic — Conditional on Delivery

The reform package is structurally coherent — the right laws, the right tax moves, the right institutional changes. However, the private sector has heard similar promises before. The decisive variable is whether the Investment Express, arbitration tribunal, and FITTA amendments are operationalised within 6 months. If they are, business confidence will materially improve. If implementation lags, as has been the historical norm, the announced measures will add to 'reform fatigue' rather than confidence.

POLITICAL ECONOMY, GOVERNANCE & SYSTEMIC RISKS

Political Economy

RISK: MODERATE

Political Stability vs Budget Integrity

The RSP-led government is expected to provide greater political stability following the 2024 elections. Progress in FDI and infrastructure development has been supported by strong political commitment. While challenges such as political influence in project selection, contractor accountability, and the efficient allocation of public resources may persist, gradual improvements are anticipated over time. Sustaining momentum under the “Mission Mode” approach will, however, require robust institutional accountability, effective oversight, and continued commitment at the highest levels of government.

Procurement System

RISK: HIGH

PPMO Reform — Critical Path

Nepal's Public Procurement Monitoring Office has been flagged by World Bank/ADB for delays averaging 18–24 months from budget approval to contract signing. The proposed e-procurement mandate and Project Prep Facility are in the budget, but passage of enabling regulations is needed within Q1 of FY27.

Debt Management

RISK: HIGH

Public Debt Sustainability

Debt ~47–50% of GDP approaches Nepal's 48% DSA threshold. Foreign loan drawdown at only 10.16% in H1 2025/26. New offshore bond and clean energy bond issuance untested. Sovereign credit rating improvement (a stated goal) requires 2+ years of fiscal discipline — contradicted by the 5.2% deficit.

Fiscal Governance

RISK: HIGH

Budget Credibility Gap

Revenue missed every year since 2022/23. Capital targets missed structurally. The Office of the Auditor General has flagged systemic irregularities at local governments (~Rs 80B unaccounted). PEFA assessment needed — current public financial management is not at implementation-ready standard for Rs 2.124T.

Federal Architecture

RISK: MODERATE

Intergovernmental Fiscal Transfer

Rs 3,214M transferred to provinces/local govts in 2026/27 — a marginal +1.54% increase. Local governments have very low capital utilisation (~20–25%) and weak procurement capacity. Growth Quads and Regional Hub strategy require province-level institutional strengthening that is 2–3 years away from readiness.

External Shocks

RISK: MODERATE-HIGH

Global Macro & Climate Risks












India slowdown risk affects remittances (~25% of GDP) and exports. Geopolitical supply chain disruptions (US-China tension) affect Chinese project pipeline. Monsoon failure / seismic event can derail agriculture and infrastructure spending. Nepal's climate-vulnerable position requires stronger env. allocation — yet Environment cut by 22.5%.

Is Budget 2026/27 Ambitious? — Analytical Scorecard

VERDICT: AMBITIOUS — Credible in Intent, Challenging in Execution

Dimension	Actual Budget	Benchmark	Rating	Analysis
Budget Size	Rs 2,124B (+25.2%)	NPC ceiling: Rs 1,890B	🔴 OVER-REACH	12.4% above NPC ceiling; Political pressure pushed size beyond FM's own preferred Rs 2.1T
GDP Growth Target	7.0%	Actual 2025/26: 3.85%	🔴 VERY AMBITIOUS	Requires near-doubling of growth. Last achieved 7%+ was pre-COVID. Structural constraints remain Budget assume Agricultural, Industry, and Service will grow at 3.5%, 10% and 7% respectively
Revenue Target	Rs 1,405B (+37.6%)	Revised 2025/26: ~Rs 1,171B	🔴 OVER-AMBITIOUS	Requires Rs 234B additional revenue. Actual 2025/26 missed target by Rs 294B. +19.98% is ambitious
Capital Expenditure	Rs 431B (20.3%)	Recommended: Rs 448B (23%)	🟡 BELOW TARGET	Capital % actually lower than recommended. Without execution reform, Rs 431B will see same fate as 2025/26.
Recurrent Exp. Share	59.8% of budget	Recommended: <45%	🟡 CONCERNING	Mandatory obligations Rs 1.33T vs revenue Rs 1.02T. Structural spending trap worsening.
Fiscal Deficit	5.2% of GDP	IMF target: ≤3.5%	🟡 ABOVE SAFE ZONE	Deficit Rs 657B vs IMF-recommended Rs 396B. Debt sustainability at risk above 48% GDP.
Sectoral Priorities	IT, Infrastructure, Agriculture, Social	Aligned with NETF and RSP manifesto	✅ WELL-DIRECTED	Priorities are correct — IT as strategic industry, infrastructure, agriculture reform are right directions.
Structural Reforms	NRB Act, BAFIA, FITTA, PPP reforms	IMF & WB recommendations	✅ POSITIVE	Legislative reform agenda is comprehensive and well-aligned with multilateral recommendations.
Execution Capacity	52% Expected utilization in 2025/26	Required: ≥80%	🔴 CRITICAL GAP	Cannot achieve 7% growth with historical execution rates. Institutional reforms are the decisive variable.
Debt Management	Borrowing Rs 657B	Debt ~47-50% GDP	🟡 BORDERLINE	Near IMF's 48% GDP threshold. Domestic borrowing at Rs 410B vs Rs 362B in 2025/26 raises debt trajectory.

BUDGET EXECUTION RISK MATRIX — FY 2026/27

Risk Dimension	Probability	Impact	Rating	Mitigation Measure
Revenue Mobilisation	HIGH	CRITICAL		Broaden tax base; enforce VAT; digital payment incentives; expedite property tax at local level
Capital Execution	HIGH	CRITICAL		e-Procurement; PPF; sunset law; performance contracts; real-time tracking dashboard
Foreign Grant Inflows	HIGH	HIGH		FATF exit is essential; dedicated DNFBP compliance unit; accelerate AML legislation
Debt Sustainability	MEDIUM	HIGH		Contain deficit below 5% GDP; improve forex hedging; defer non-priority domestic borrowing
SOE Divestment	HIGH	MEDIUM		Nepal Airlines, Nepal telecom ; avoid political interference in valuation
Private Investment	MEDIUM	HIGH		Fast-track Investment Express; operationalise arbitration tribunal; FITTA amendment passage, diaspora involvement,
NEA Restructuring	HIGH	MEDIUM		Detailed transition roadmap; ring-fence staff; avoid service disruption during unbundling
IT/AI Centre (Syuchatar)	HIGH	MEDIUM		International expertise partnership; realistic timeline (5-year horizon, not 1-year); talent pipeline
Agriculture Subsidy	MEDIUM	MEDIUM		Cooperative delivery channel; digital beneficiary database; output-linked payment triggers, 7% growth critically depends on this sector's performance
Political Risk	LOW	HIGH		Maintain RSP-led stability; insulate policies from political pressure
Climate/Disaster Shock	MEDIUM	HIGH		Disaster contingency reserve; restore environment budget cut; REDD+ fund management

FINAL ANALYTICAL SCORECARD

Nepal Budget FY 2025/26 Implementation vs FY 2026/27 Execution Outlook

Assessment Dimension	FY 2025/26 Grade	FY 2026/27 Outlook	Critical Finding
2025/26 Capital Execution	C- 52% (expected)	⚠️ Target 80%	Systemic failure carried forward. Only structural reform can break the cycle.
Revenue Realism	B+ 86.3%	B- +23.7% Growth.	Structurally over-ambitious both years. Credibility of fiscal projections compromised.
Sectoral Priority (Direction)	B	A-	2026/27 priorities well-targeted: IT, energy, infrastructure, agriculture all correct.
Fiscal Sustainability	BB-	BB+ Reform pkg	Deficit at 5.2% of GDP; debt near threshold; structural spending trap worsening.
Development Partner Support	C- 58% grant util. expected	B+ Conditional	FATF grey-list is the critical dependency. IMF programme compliance non-negotiable.
Private Sector Confidence	C-	B+ Reform pkg	Right reform package announced; execution credibility still needs to be established.
Governance & PFM	D	C- If reforms	Procurement, PPMO, and federal capacity remain structural weak points.
Reform Agenda Quality	C	BBB+	Comprehensive 5-objective, 5-priority framework is coherent with IMF/WB/ADB advice.

OVERALL VERDICT: "BB"

FY 2026/27 budget is well-intentioned but structurally over-ambitious. The reform agenda is the right one. The critical variables are: (1) capital execution breakthrough from 52% → 80%, (2) FATF exit for grant flows, (3) revenue discipline, and (4) political insulation of the reform programme. Without these, Rs 2.124T likely to become a paper document.