

Country Development Strategy Statement

FY 1985



Nepal

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Agency for International Development
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BEST AVAILABLE

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Nepal - CDSS

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Review of Priority Areas

POLICY DIALOGUE

The AID policy dialogue in Nepal must be examined in the context of a 30-year United States economic assistance association with this developing country. Policy has always been part of that relationship and has reflected a common awareness on the part of the Government of Nepal (GON) and AID of development as the measurement for progress in Nepal. Any reference to the conditions existing in the country at the start of the AID program--the virtual absence of communication and transportation infrastructure, health services, agricultural research and extension, even education--and comparison with the present day reflects change and development in a total and dramatic sense. Each of the steps along the way--construction of power and transport systems, creation of an educational system, initiation of agricultural research and extension, spreading of health services, beginnings of a family planning program--has been in some respects a joint GON-AID effort.

Policy has been inseparable from this process, whether concerned with macro issues or the sectors which give them substance. AID advice and assistance in previous years is evident in the present day throughout almost the entire structure of government and services in Nepal. There is virtually no basic policy, no major department or service and no commitment to development shared by the Government of Nepal at present which does not contain from some period the imprint of AID thought on how the problem should be addressed.

Throughout this unique association the Government of Nepal has been willing to embrace new policies when they have offered promise of being constructive. This has meant a consistent willingness on the part of the Government to change, so long as the change seems to offer a better approach. In a setting, for example, where less than half the economy is monetized and where per capita industrial investment is less than \$2.50, Government investment was essential if basic services were to be provided at all. As the economy and society have been strengthened, however, the Government has promoted new investment policies and has declared its intention to withdraw from fields where private effort is now able to respond. Equally, while the Government has continued to experiment with ways of increasing revenue generation, it has followed a relatively conservative fiscal and monetary policy. This is not in any sense to pretend this is a perfect world or ideal policy framework at all times or in all parts, but it does mean that the GON is receptive.

The discussions in which we are currently engaged essentially reflect the present emphases of our development program in Nepal, despite the relatively small U.S. contribution to Nepal's development efforts. These discussions include formulation of a national population strategy, support for decentralization of GON development, and initiatives in renewable energy and natural resource conservation.

With respect to population strategy, AID Nepal has encouraged development of a strong supra-ministerial body with the capability

and mandate to formulate relevant policies to reduce the current high population growth rate of 2.6 percent. Technical assistance and training at the sector level, and interventions at the highest levels of Government have helped raise awareness of the seriousness of the problem and motivated efforts to address it.

Regarding decentralization, the GON recently promulgated a Decentralization Act which is intended to shift more authority and responsibility to local governments. This development complements the efforts of several donors, including the U.S., who are strengthening local government through integrated development efforts. Decentralization success may be of particular importance to local government units in the hill areas, the current focus of the AID Nepal program, where relative inaccessibility has left hill units without adequate authority to develop or use resources. The main focus of U.S. attention in this area is to equip local organizations to increase food production and income, and to improve local ability to carry out development programs.

The third major issue relates to renewable energy and natural resource conservation. Population pressures have had enormous impact both in the hill areas and in the lowlands (Terai). In the hills the ability of the land to support growing population has probably already been surpassed; while in the Terai the effects of migration (from the hills as well as from India) are increasingly obvious. The Government has now begun measures to address these issues; previous Nepalese planning made little mention of these problems.

The issues cited above represent only a few areas in which there is both need and potential for policy change. Others include development of hydro potential, agriculture, local resource generation, improved Government management, greater use of existing infrastructure, divestiture of inefficient parastatals and stimulation of the private sector. AID Nepal encourages the GON in these areas, and as we acquire greater information we may identify more direct links to the projects we support. At the moment, utilizing PD and S funds, we are examining agricultural marketing and pricing policies in Nepal. This study will supplement the Asian Development Bank's Agriculture Sector Strategy Study and provide additional data for policy discussion with the GON. During FY 1983 we are also planning to use PD and S funds for an analysis of the Nepalese private sector and a study of the food production, stocks and distribution systems. Possible policy initiatives may well result from these studies.

A number of constraints cause policies of any kind to evolve slowly in Nepal. As in many developing countries, final decision-making on matters of real substance takes place at the top. When the Government was small, this caused little delay and given the thin management ranks, was undoubtedly adequate. As Government responsibilities have expanded, however, changes have not kept pace, although managerial personnel have increased in number and in quality. Devolution of decision-making authority in a real or political sense is a slow process in a highly traditional society. It is happening but the pace remains slow.

Experience has shown that AID Nepal can play an effective role in the development discussions of Nepal only if it continues to initiate serious discussions with the GON of policy issues the GON itself perceives to be timely and important. Over the years the United States has done just this and has thereby gained credibility; the U.S. presence and our contribution remain important to the Nepalese. We expect to continue to have an influential voice, particularly on the issues of population policy, decentralization, energy and resource conservation, which are addressed by current AID efforts in Nepal.

PRIVATE SECTOR

The AID Nepal program is presently focused on the dominant element of the country's economy and of the economy's private sector -- small and medium scale farmers. This concentration of private sector endeavors in small scale agriculture reflects the following considerations:

- 93 percent of the population depends upon agriculture for a living, lacking foreseeable employment alternatives;
- Nepali agricultural production is at best at a subsistence level. Although 57 percent of 1981 exports (equivalent of no more than three percent of GDP) were raw and semi-processed agriculture products, they merely financed consumption of an equivalent value of food and agriculture imports; and,
- an estimated 95 percent of GDP is absorbed by domestic consumption, and the residual (the equivalent of \$95 million in 1981) must finance public and private depreciation as well as new investment.

Available domestic resources are, therefore, extremely limited for investment, by either the public or the private sector, or for altering the agricultural orientation of the private sector. In addition to the lack of financial resources, other factors limit development of Nepal's private sector:

- shortage of entrepreneurial and skilled labor supply;

- relatively efficient competition from India that can and does supply most of Nepal's manufactured needs through an extensive and uncontrolled open border; and,
- limited size of the domestic market, due to inadequate infrastructure that restricts the distribution of goods, and general non-monetization of the rural economy hampering expansion of demand.

The remainder of Nepal's limited private sector activity (apart from agriculture) is divided between trade and tourism, and only marginally in industry. The industrial sector consists of manufacturing (agriculture processing and production of basic import substitutes) and cottage industries, with an estimated four percent share of 1981 GDP. Parastatals, however, dominate the industrial sector. In 1981 twelve public sector enterprises (from a total of nearly 60) produced one-half of total industrial GDP. In contrast, the private portion of the industrial sector resembles that of the agriculture sector -- 3500 registered small scale firms, plus the cottage industries.

The lack of an actively expanding non-agriculture domestic private sector does not negate the demand for such in Nepal. To date, however, that demand is being satisfied by recorded and unrecorded imports, primarily from India. Nevertheless, the requirement for efficient private sector agro-industry (grain, seeds, and sugar processing, etc.) and the production of consumer goods will continue to expand with population growth and monetization of the

rural economy. Also, opportunity for greater private sector involvement in Nepal's economy has been fostered by the GON during the past year through the passage of new legislation.

New GON domestic and international trade policy seeks improved efficiency, with the explicit goals of stimulating effective demand and overcoming distribution obstacles, thereby improving the attractiveness of the trade sector to private investors. The GON has also adopted a new industrial policy which recognizes industrialization as an integral part of national plans to promote economic development. It seeks to create a setting in which industrial investment, specifically through the private sector, is encouraged. This policy provides clear definition and logical classification of industries, simplification of licensing procedures, introduction of financial incentives, special provisions to attract foreign investment and provision of financial, management and technology assistance through GON agencies. The new policy simplifies the establishment of industries and provides coordinating links between various relevant GON agencies. These new incentives also provide tax concessions, reduced trade duties and provide for easier commercial bank credits.

We have no current involvement in direct support of private sector institutions. Most current AID supported projects and programs attempt of necessity to make use of the predominant traditional social,

cultural and public institutions. Nevertheless, we are addressing the need to stress the developing private sector and propose to take this up initially through a current PD and S study. This should identify points at which the AID program might work with the private sector as it supports GON main development priorities.

Though relatively small, Nepal's non-agricultural private sector does benefit directly from the AID program. Data indicate that approximately one-third of the 1980-1987 AID Nepal program expenditures will purchase goods and services from the indigenous private sector.

During the past year the GON transferred resources out of and eliminated eight inefficient public sector rice exporting companies, leaving this area to the private sector. AID has proposed to the GON that the same process be followed regarding the U.S. assisted twenty-year old ropeway, that this could stimulate the private transportation sector. The issue is still under consideration. The system for most rapid private sector growth (agriculture and non-agriculture) impact, however, will consist of sub-lending through the development finance institutions in Nepal -- The Nepal Industrial Development Corporation, The Agricultural Development Bank of Nepal (ADB/N), and the commercial banks. We are already engaged in this through the ADB/N and expect to continue this program (through the Rapti Project and the Resource Conservation and Utilization Project).

TECHNOLOGY TRANSFER AND RESEARCH

Technology transfer and research are prominent themes in AID's program in Nepal. Both are and have been for many years a part of our continuing policy discussion with the Government (and with other donors) and both are reflected in our project portfolio. Fortunately, the GON shares the view that these themes have important roles in development. There are few obstacles to our cooperation in this respect, and this is not surprising - AID, past and present, has been at the forefront among donors in this regard.

The lack of obstacles to cooperation, however, does not mean that a similar situation prevails with respect to the design and implementation of projects addressing these concerns. Difficulties which obstruct effective work on technology transfer and research surface regularly.

Some of these arise from Nepal's history and its limited recent experience with the outside world. Some derive from the problems of illiteracy, poverty, backwardness and a low resource base. Others stem from Nepal's location on the flanks of a rugged and fragile mountain system. And still others are associated with the growing pains of new institutions which suffer greatly from shortages in financial support, trained staff and other prerequisites. These constraints, and in Nepal there are many in each of these general categories, combine to make the complicated processes of technology transfer and research difficult, slow moving and sometimes expensive.

The substance of the agricultural research agenda in Nepal is complicated by the diversity of crop

growing conditions caused by altitude and climate variations, particularly in the hills. Also, rural economic and social conditions, which have created a survival-oriented view, make it very difficult for farm families to accept risk in trying new technologies.

These problems notwithstanding, Nepal has made progress in identifying its development needs and establishing institutions for change. The GON has been the pioneer in this, with encouragement and assistance from AID and other donors, and in recent years from a growing number of private sector firms and PVOs. As a result, the number of organizations dealing with research and research services has expanded dramatically. More and more, examples of technology transfer are seen, even in remote parts of the country.

Nepal's research and extension institutions are gradually maturing. Staffs are better trained and equipped to do the jobs expected of them, though personnel shortages and fiscal support frequently limit the scope of their activities. Many of these institutions are now applying fairly high levels of technology. For example, the Ministries of Health and Agriculture are using computers to process and analyse data and monitor field conditions. At the same time, these organizations display ability to evaluate technology available from outside the country as well as skill in selection and adaptation. They are also improving their understanding of the constraints in rural Nepal and are successfully molding new technologies appropriate to these circumstances.

These developments augur well, for they indicate potential for significant increases in the economic and social returns from investments made in research and technology transfer.

As indicated above, AID has worked closely with the GON. We have also worked consistently with the National University and with other organizations involved in training and research. These areas offer continuing opportunities and needs which we address in our current program. Today, AID is assisting Nepal's research and technology in a number of ways:

Agriculture: The Integrated Cereals Project concentrates on cropping systems research and dissemination of new technologies through verification trials and production campaigns. The Seed Production and Input Storage Project improves the supply of inputs by establishing mini-seed processing units in remote areas. The Institute of Agriculture and Animal Science Project supports a substantial research program. The Agriculture Development Council (ADC) Project (OPG) concentrates on social science research and the development of a management information system for the Ministry of Agriculture.

Resource Conservation: The Resource Conservation and Utilization Project monitors research in two large catchment areas and is heavily involved in technology transfer at both the central and field levels. Its work with the Institute of Renewable Natural Resources (IRNR) also establishes a base for training and research.

The Agricultural Resource Inventory Project helps to establish a remote sensing center in Nepal, using satellite imagery and aerial photography and concentrates on interpretation, data processing and the training of staff of data user agencies.

NOTE: Integrated Cereals (cropping systems), Seed Production and Input Storage and Agricultural Resource Inventory (remote sensing) each terminates in 1984. We look upon the agriculture projects as the backbone and substance of much of our work in the hills in addition to the most important effect they have on Terai and valley agricultural production. The AID Mission believes that we ought to continue this support, but this remains to be worked out with AID/Washington.

Rural Development: The Rapti Zone Project has an Appropriate Technology Unit which applies research and transfer of technology to rural families.

Health and Family Planning: The Integrated Rural Health and Family Planning Project works in both research and technology transfer. Examples of appropriate technology transfer activities are its work with oral rehydration therapy, immunization, data processing and contraception.

Population Policy: The Population Policy Project supports a wide range of research and data processing needs through the National Population Commission.

While AID expects to continue this assistance well into the future, as research institutions mature and become stronger the emphasis of AID support will shift to technology transfer institutions. This should result in increased AID interaction with the non-agriculture private sector. We also expect to expand our already substantial cooperation with the Peace Corps (currently 32 PVCs work in six AID-supported projects) and continue to work with and through PVOs.

INSTITUTIONAL DEVELOPMENT

Nepal entered the 1950s with virtually no modern public or private sector institutional structure. Nepal's fleeting exposure to colonial interests and 100 years of autocratic government left it with little beyond rich cultural, religious and social institutions to cope with a rapidly impinging modern world. Progress over the past thirty years in establishing functional governmental, transportation and communications, education and health care institutions has been matched only by the continual need to expand and improve these.

AID has played a role, since the beginning of this period, in establishment and development of most of these and many other Nepalese institutions. AID's ability and skills in such development have increased in keeping with the growing number, scope and strength of these institutions.

Current Emphases and Objectives

Areas of current institutional development in which AID is involved include:

- Education and Training

Nepal's primary and secondary school systems have received extensive financial support through training, advisors and commodities, and construction and renovation of schools

throughout the country. Current efforts are directed at training rural teachers in the expanding primary education system, and in establishing domestic training capabilities in critical personnel areas. These latter include the university level as well as working directly with GON departments. Current programs include Radio Education Teacher Training, the Institute for Agriculture and Animal Science, the Institute of Renewable Natural Resources and the Ministry of Forests Training Wing.

- Agricultural Research and Extension

Working within an institutional and manpower base to which AID assistance has contributed heavily over the past thirty years, present objectives include refinement of basic cereals crop research and new approaches for extending these developments. Recent evaluations, including the Foodgrain Technology Project impact assessment, have reiterated the importance of such linkages. Much of these current efforts draw upon and strengthen linkages between AID supported domestic organizations and international institutions.

- Health and Family Planning

Current efforts improve overall management capabilities and at the local level integrate basic health care and family planning delivery systems. The Integrated Rural Health and Family Planning Services Project is our main vehicle.

- Population Policy

AID supports the GON in development of a highly specialized unit to carry out research, disseminate findings and influence policy on population issues.

- Resource Management System

AID trains personnel in-country, provides specialized overseas training to middle level personnel, strengthens concerned GON agencies and develops approaches for improved resource management. These efforts flow through the Resource Conservation and Utilization (RCU) Project.

- Local Development and Decentralization

AID has initiated assistance to improve local government and administration and these efforts are combined with support to a range of productive and social sectors. These efforts are supported by AID's Rapti Zone and RCU Projects.

Effects of These Efforts on Other Institutions

AID's institutional development work in Nepal affects both the private sector and traditional institutions. AID support has been instrumental in helping to establish some of the economy's key parastatal institutions while still encouraging and supporting the development of private sector businesses and industries.

Potential

At the present state of Nepal's development and mixed economy the types of basic institutions with which AID is now working

carry primary responsibility for infrastructure development, basic services and most aspects of economic development. This is likely to remain the case for the foreseeable future.

These institutions are central to most AID supported development programs in Nepal.

Given the need for some degree of institutional development in almost all AID assisted projects in Nepal, the question really is how best to carry out such development. On that point, we are satisfied that the range among our current projects addresses this adequately, with a responsiveness to Nepal's particular institutional status and capabilities.

AID Plans in Nepal During the CDSS Period

Two trends direct our continuing contribution to development of institutions in Nepal during this CDSS period. These are the stimulation and support of private enterprise at the local level on a small scale (as in our Contraceptive Retail Sales Project and through the Appropriate Technology Unit of the Rapti Zone Project), and the implementation of governmental decentralization. Neither trend will mechanically determine the appropriate sectors of AID assistance during the coming years, but they will significantly affect the nature and level of institutional development carried out.

Current institutional support in agriculture is strongly oriented toward linkages among the central research programs, local extension efforts and farmer production initiatives. This is being done, for example, through the development of institutions

to support local production and private sector marketing of improved seeds. The increasing availability of extension and research personnel should give much greater impetus to local (district) level production, an essential condition to growth in Nepal.

Programs supported and encouraged by AID and other donors in the health and family planning fields will result in trained health and family planning care personnel to support both Government and private sector efforts. Rural areas willing and able to support locally controlled and financed health care services will increasingly be able to develop these through cooperation with Government institutions.

PARTICIPANT TRAINING

AID, other donors and the GON are well aware of the need to reinforce absorptive capacity for development assistance in Nepal. A principal impediment to achieving higher rates of investment is the limited number of people in both the private and public sectors with requisite management and technical skills.

The National Planning Commission, in the Sixth Five Year Plan, has attempted to quantify the technical manpower needs of the country, assigning skilled manpower targets which will require increased donor funding for participant training. It is clear from the GON data that hundreds of vacancies exist for engineers, agricultural and forestry staff and medical personnel. Experienced public sector (as well as private sector) managers are also in scarce supply.

Neither the Planning Commission itself nor the Ministry of Finance (through which all development aid flows) has economic staff to analyze policy alternatives, evaluate proposals for investment and influence expenditure decisions adequately. Central programming units in the line ministries often lack trained personnel to develop sound plans for program implementation.

Decentralization of development programming is supported at the highest levels of the GON as well as by major donors. This means delegating authority to district offices, local staff of line ministries and local elected representatives for deciding investment priorities and for implementing development schemes.

Shortages of trained manpower, however, at the field level are readily apparent. At present there are 58,000 field positions in the service of the central Government, and in a zonal/regional/district headquarters such as Pokhara, for example, there are more than 60 separate Government offices. Each of these faces acute shortages of trained managers, accountants and technicians. At the same time, decentralization will transmit responsibility and channel funds to the 75 district assemblies. These assemblies will then be broken down into social, education, forest, agriculture, health and development committees, each headed by a member of the National Legislature from that district. However, very few of these committees will contain members with post secondary education.

The Soviet Union provides Nepal with approximately 150 scholarships a year, with an emphasis upon engineering. The World Bank and the Government of India also support engineering training. However, in the light of Nepal's hydropower potential, current training efforts fall short. AID Nepal is currently developing an FY 1985 PID for a participant project to support Government institution building programs generally, with a focus on public administration, financial management, general management (public and private) and engineering, as well as being open to other fields. Public and financial administration in Nepal, as well as private sector management capabilities, are keys to increasing Nepal's absorptive capacity for development. Training in these sectors is all the more critical now that the GON has embarked upon a course of decentralized administration.

Additionally, the Agriculture and Health Ministries depend upon skilled manpower to plan programs centrally as well as to carry out field extension. Both are in urgent need of trained female extension agents who can easily relate to village women. The latter carry the main burden of agricultural production and are the key to improved child health and nutrition as well as to lower rates of reproduction.

Objectives of AID Training Program

AID Nepal training programs focus at present on agriculture, health, family planning, resource conservation and population policy, in order to improve GON capability in these key sectors. More than half of the training has been carried out in India under PL-480 Rupee funding. Participants are also sent to the U.S. or third countries for advanced degree training. The opportunity for use of the skills acquired from AID funded participant training is high. Returning trainees are required to serve for at least two years in the Government Ministry or Agency which sponsored their training. To-date over 99 percent of the more than 3000 participants trained abroad (35 percent in the U.S., 42 percent in India/Pakistan and 23 percent in other countries) by AID Nepal during the past thirty years have returned to work in Nepal. For FY 1983 and FY 1984, we plan to continue training support to projects in agriculture, health, family planning, resource conservation and population policy.

IMPLICATIONS

The functional account resources required to achieve the AID Nepal strategy are as follow:

	<u>Planning Levels</u>				
	(\$ Millions)				
	<u>FY 1984</u>	<u>FY 1985</u>	<u>FY 1986</u>	<u>FY 1987</u>	<u>FY 1988</u>
Agriculture, Rural Development and Nutrition	8.4	12.2	14.4	15.5	18.0
Population	2.3	2.9	3.1	3.3	3.5
Health	1.8	2.9	2.5	3.2	3.5
Education and Human Resource	1.0	-	-	-	-
Total	13.5	18.0	20.0	22.0	25.0

The FY 1985 planning level underscores the limited resources available to support our program in Nepal. These planning levels reflect the program focus -- agriculture/rural development/nutrition is the principal account followed by the fields of population and health, with education in support. Although these levels show modest increases, in a larger context they imply that our rate of project expenditures may decrease.

AID-GON efforts have accelerated project expenditures over the past two years -- \$5 million in FY 1980, \$10 million in FY 1981, \$18.5 million in FY 1982 -- and the annual spending level is projected to remain near \$20 million in to FY 1985. This will bring our pipeline down to \$20 million at the end of FY 1984, equal to the annual expenditure rate. At that pipeline level, the \$20 million expenditure rate could not be maintained.

If we are to be able to implement at the levels we have urged upon the GON it is important that these planning levels be secured. They will provide us both with flexibility and the opportunity to continue those programs which offer greatest potential for return in succeeding years and which reinforce our basic strategy.

The Rapti and Resource Conservation Projects are not self-sufficient. Radio education and PVO efforts contribute to the accomplishment of their objectives. More important, however, Rapti and RCU depend on crop yield increases, agricultural technologies and extension support from the entire agricultural structure. Agricultural policy, planning, research and education are key to our long-term strategy.