

**FOR
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To: Members of the Executive Board

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INTERNATIONAL DEVELOPMENT ASSOCIATION

NEPAL

The 15TH Plan National Vision of “Prosperous Nepal, Happy Nepali” (Fiscal Year 2019/20 – 2023/24)

ASSESSMENT LETTER

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Maldives, Nepal, and Sri Lanka**

March 15, 2023

I. OVERVIEW

1. **Nine five-year and five three-year plans have been implemented in Nepal over six decades of planned development.** The Fourteenth plan (FY17 –19) was the first plan following promulgation of the new 2015 Constitution establishing a federalized system of government. The plan tried to mainstream and internalize the Sustainable Development Goals (SDGs) and aimed to transition Nepal into a middle-income country by becoming self-reliant on agriculture, medicine, and energy. Despite making progress on some of the plan’s targeted social goals, economic development outcomes were mixed, and Nepal failed to transition out of the ranks of least developed countries.

2. **The Fifteenth Plan (FY20 –24) (“the Plan”) was envisaged as the foundational first stage for achieving the country’s long-term 2043 vision of “Prosperous Nepal, Happy Nepali”.** The second and third stages of the vision will build on this foundation and implement two five-year plans to accelerate achievement towards and sustain the envisioned prosperity and happiness indicators, respectively. The vision aims to: (i) achieve SDGs by ending all forms of poverty and graduating into a middle-income country by 2030, and (ii) attain high-income country status by 2043. As a foundational stage, the focus of the Fifteenth Plan is to orient the economy towards higher productivity and employment creation. The plan targets a reduction in monetary and multidimensional poverty by 9.2 and 17.1 percentage points, respectively, and inequality by 2 Gini points.

3. **As the current assessment comes before the end of the 15th Plan implementation period,** it compares outturns through FY/22 and World Bank forecasts of macroeconomic variables through FY24 to gauge progress made across major macroeconomic and distributional targets where data is available. The current assessment acknowledges that the period covered by

the Plan includes the unforeseeable shocks of the COVID-19 pandemic and Russia’s invasion of Ukraine.

II. BACKGROUND AND COUNTRY CONTEXT

4. **Over the past decade, Nepal achieved gross domestic product (GDP) growth averaging 4.9 percent in FY09–FY19, enabling the country to attain lower-middle-income status in 2020.** Despite significant progress in access to services, and non-monetary measures of poverty, the country faces structural weaknesses and risks to achieve its goals of inclusive and sustainable growth.¹ In particular, high rates of vulnerability to falling back into poverty and extreme poverty (45 percent in 2010), and exposure to shocks remain an enduring characteristic of economic welfare in Nepal. Over the last decade, these shocks included the Gorkha earthquake and near-complete disruption of trade because of India’s unofficial blockade in 2015, floods in 2017, and the COVID-19 pandemic in 2020. These economic shocks have also led to a surge in debt levels that need to be addressed, although the risk of debt distress remains low.²

5. **Labor market recovery from COVID-19, which induced jobs and income losses for 2 in every 5 workers, has been uneven and weak.** Women (69 percent relative to 83 percent for men) and those in agriculture and lower-skill occupations (65 and 73 percent) reported recovering more slowly. This recovery is also taking place in the context of a weak domestic labor market that relies overwhelmingly on informal and subsistence jobs and limited social assistance for poor. Six months into the COVID-19 crisis, only 2 percent of households reported receiving any additional public assistance despite the severity of the impacts. The economic contraction induced by the pandemic also had prolonged impacts on the labor market: 30 percent of workers who recovered a job experienced more than one employment transition; and recovered jobs were of lower quality (23 percent) resulting in lower earnings (53 percent) compared to jobs that were lost.

6. **The lack of official data on poverty has now limited poverty monitoring in Nepal for over a decade.** Poverty in Nepal was last measured in 2010. The poverty headcount, calculated at the national poverty line, was 42 percent in 1995, declined to 31 percent in 2003, and 12.5 percent in 2010. These improved living standards led to the revision of the national poverty line, which increased the real value of the poverty threshold by 35 percent, resulting in an estimated 25 percent poverty rate in 2010. At the international extreme poverty line (\$2.15/day at 2017 PPP), the poverty rate was 8.2 percent; and overall inequality was fairly low with a Gini index for consumption of 33 in the same year. The fourth Nepal Living Standards Survey (NLSS IV), which will be completed in June 2023 will be used to update official poverty measures. In the interim, the decade-long gap has defined an extremely outdated base to produce reliable simulation and projection-based poverty estimates and made it difficult to assess the impacts of these shocks on broad-based measures of economic welfare.

¹ Nepal’s official Multidimensional Poverty Index (MPI), a measure of deprivation in non-monetary indicators, also reports a substantial decrease from 30.1 to 17.4 percent over the period 2014-2019. Monetary poverty in Nepal was last measured in 2010, and will be updated with conclusion of the next Nepal Living Standards Survey in June 2023

² World Bank Group, April 2022 “Nepal: Joint World Bank IMF Debt Sustainability Analysis”

7. **In addition, enduring challenges remain in achieving equitable and high-quality human development outcomes, despite progress on basic indicators.** These challenges are, in part, due to continued slow progress on indicators of child malnutrition on the one hand; and in emerging areas such as improving the quality of education and access to tertiary education on the other. The challenges of poor child nutrition are also spatially concentrated, in Karnali and Sudurpashchim; while Madhesh has poor education outcomes on indicators that range from school attendance rates to adult literacy. Such spatial disparities have been a long-standing determinant of inequalities in opportunity (and therefore human capital investments in Nepal).³

8. **Structural features of the Nepali economy weigh heavily on the course of the country's development.** Like many other landlocked countries, Nepal has struggled to gain a foothold in merchandise export markets. On the services side, while tourism generates jobs domestically, it earned only 10 percent of total foreign exchange revenues in FY22. Migrant work and remittance inflows are likely to remain the key driver of growth in the future. However, it has been seven years since remittances peaked as a percentage of GDP (25.5 percent in FY15), and they may not return to this level. Nepal has enormous hydropower potential but must balance development of the sector with existing fiscal space and securing export markets. Ensuring macroeconomic stability and a sustainable debt burden is critical when planning multiple and larger-scale infrastructure investments.

9. **After a decade-long political transition, Nepal adopted a new constitution and transitioned to a federal democratic republic in 2015.** The new governance structure has seven provincial governments and 753 local governments. The federal system provides both challenges and opportunities for translating shared national goals of economic prosperity, social justice, and climate and disaster resilience into a comprehensive development approach. Among other impacts, the transition has elevated public spending, leading to higher public debt and reduced fiscal space to address shocks, and raised expected challenges with respect to institutional capacity and coordination across levels, jurisdictions, and sectors. In terms of opportunities, the federal structure provides an enabling environment to ensure effective governance at the local level with enhanced development and citizen participation fostering social inclusion, pluralism, accountability, and appropriate policy responses to local development challenges. Additionally, federalism has empowered local bodies with extensive fiscal autonomy and resource mobilization and management responsibilities. The Plan builds on these opportunities and includes granular quantitative provincial targets for FY24 in Table A2.6 of the 15th Plan.

10. **Reducing vulnerability, equalizing opportunities, and improving resilience remain the key challenges to consolidating the gains made on poverty reduction in Nepal.**⁴ Moreover, when shocks do occur, households have few safety net or other mechanisms such as insurance (public or private), which they can use to manage the impacts. Existing transfers are fragmented and small, and do not easily scale in response to disasters. Social protection programs have also thus far not been very effective in protecting the poor: the poverty headcount would increase by a marginal 0.5 percentage points (from 25.2 percent to 25.7 percent) in the

³ World Bank, 2016 "Moving Up the Ladder: Poverty Reduction and Social Mobility in Nepal"

⁴ Ruppert Bulmer, E., Shrestha, A., and Marshalian, M. 2020. Nepal Jobs Diagnostic ; World Bank 2021, "Nepal Light Poverty Assessment".

absence of all currently administered social assistance programs.⁵ The underlying reasons for the low impact are that the programs are not generous enough and rely on categorical targeting rather than being explicitly targeted to poor. Therefore, the impact of existing social protection programs on reducing poverty and inequality is more limited than it could be with better design, scalability, and targeting.

III. NEPAL'S 15TH PLAN: NATIONAL VISION OF “PROSPEROUS NEPAL, HAPPY NEPALI”

11. **The results framework of the 15th Plan establishes a baseline in FY19 and sets annual targets through each of the fiscal years covered by the Plan through FY24.**

The following table shows the significant alignment between the ten 15th Plan national goals and the six 2018 World Bank Nepal Systematic Country Diagnostic (SCD) key focus areas:

Ten National Goals of the 15 th Plan	Six Key Focus Areas of the World Bank 2018 Systematic Country Diagnostic ⁶ (SCD)
High and equitable national income	
Development and full utilization of human capital potentials	Equitable investments and use of human capital
Accessible modern infrastructure and intensive connectivity	Creating more and better jobs for all Nepalese (infrastructure, private investment, access to finance, regulation)
High and sustainable production and productivity	Creating more and better jobs for all Nepalese (infrastructure, private investment, access to finance, regulation) Getting more from international migration and remittances
Well-being and decent life	
Safe, civilized and just society	
Healthy and balanced environment	Productive and sustainable livelihoods from Nepal's land, forests, and water Strengthening resilience to natural disasters and health shocks
Good governance	Improving public institutions in a federal Nepal
Comprehensive democracy	
National unity, security and dignity	

⁵ World Bank, 2016 “Moving Up the Ladder: Poverty Reduction and Social Mobility in Nepal”

⁶ World Bank, February 2018 “Nepal: Systematic Country Diagnostic, A New Approach for a Federal Nepal”

12. **The 15th Plan projects annual GDP growth to reach 10.8 percent by FY24 but observed growth has been far lower.** Progress on growth and other economic indicators is presented as an Annex to this assessment, which includes the April 2023 World Bank macroeconomic forecast for FY23 and FY24. The COVID-19 pandemic and the war on Ukraine, as well as domestic shocks such as import restrictions imposed in FY22 and FY23, have reduced GDP growth and contributed to higher debt stocks among other impacts. Growth has registered significantly below the targets of the Plan: instead of growth accelerating from 7.1 percent in FY19 to 10.8 percent in FY24, we observe growth contracting by -2.4 percent in FY20 before recovering to 4.2 percent in FY21 and 5.8 percent in FY22. The World Bank projects growth to reach 4.9 percent by FY24, the final year of the 15th Plan. The significant deviation between Plan targeted GDP growth and actual/forecast growth limits the achievement of related Plan objectives such as strong per capita income growth and poverty reduction.

13. **The 15th plan aims to address income and non-income based poverty and social exclusion, though a multi-sectoral approach, that aims to reach poor people, backward geographies, and excluded communities.** Currently, more than 50 poverty alleviation programs are under implementation, across sectors that include agricultural productivity, climate adaptation, disaster risk resilience, education (including vocational training and tertiary education), and health. In addition, investments were also proposed in supporting migrant workers through vocational programs that aim to up-skill aspiring migrants and provide certification and entrepreneurship support to returnee migrants. The 15th plan also aims to improve integration across poverty alleviation programs and expand the reach of social security programs.

14. **However, the targeted poverty reduction of 9.2 and 17.1 percentage points in monetary and multidimensional poverty will likely not be met. Translating poverty reduction strategies into effective policies and programs that reach the poor will require more prioritization and sequencing .** The latter strategies include: (i) identification of the poor through a proxy means test approach and linking them to current anti-poverty programs; (ii) formulation of new anti-poverty programs; (iii) implementation of skills development and training programs; (iv) improving productive employment opportunities for the poor, including through entrepreneurship promotion and minimum employment guarantee programs; (v) formulation of a new poverty alleviation policy; and (vi) ensuring access to basic needs and services for the poor.

15. **The prioritization process will need to be informed by new data on poverty and living standards from the ongoing NLSS IV survey.** These data will help update information on poverty trends and drivers of poverty reduction in Nepal. The latter will include an assessment of the importance of remittances to poverty reduction, and the economic vulnerabilities associated with subsistence agriculture. In the past, equitable improvements in welfare were driven largely by remittance incomes accounting for 27 percent of all poverty reduction between 1996 and 2011. In addition, high rates of migration also had indirect impacts on poverty and welfare by tightening rural labor supply and increasing wages on the one hand and supporting investments in health and female education on the other. Moving forward, employment related migration and remittances are likely to remain key to poverty reduction, thus, Nepal needs to implement a comprehensive migration strategy.

IV. IMPLEMENTATION, MONITORING AND EVALUATION, AND RISKS

16. **The National Planning Commission’s mid-term review of the 15th Plan was published in January 2023.**⁷ Their analysis recognizes that, in addition to the challenges identified at the time of formulation of the Plan, significant challenges such as COVID-19 have emerged that affect economic management. Quantitative targets on track for achievement include GDP per capita rising to \$1,337 by FY24, which was exceeded when national account statistics were rebased. Targets that are not on track include average annual GDP growth and the growth targets of each of its components: agriculture, industry, and the services sectors. The Commission warns that, in their view, the industrial sector’s declining contribution to growth and the rapid expansion of the services sector threaten to increase economic inequality.

17. **The ambitious poverty reduction agenda laid out in this plan will need to be accompanied by the timely design of anti-poverty programs, implementation of targeting mechanisms, and tracking of progress on key development outcomes.** The 15th plan proposed establishing a national statistical system that is aligned with the current federal system of governance and can generate the data and evidence base required to monitor and track poverty reduction in the country. Nepal’s new Statistics Act-- which lays the basis for a new federal legal and institutional data governance framework—will be key to unlocking the potential of different types of data. It will also underpin a process of evidence-based decision making and policy if it is accompanied by enabling policies that support its operationalization.⁸

18. **The 15th plan also identified key risks related to economic growth and poverty reduction and proposed mitigation strategies that require careful operationalization.** These risks include a dependance on remittance growth, the reliance on subsistence as a source of livelihoods, and the impacts of natural disasters on livelihoods and welfare in the context of a changing climate. The plan includes broad approaches for these key risks. First, the plan notes the need to improve economic returns to migration and the re-assimilation process by improving efficiencies in the migration process and investing in a (higher) skill profile of new migrants while also leveraging the skills of returnees to support domestic economic growth.⁹ To reduce reliance on subsistence agriculture, the plan proposes to support investments in agricultural productivity and entrepreneurship.¹⁰ For natural disasters and climate risks, it proposes strengthening disaster risk operational structures at all three levels of government.¹¹

19. **A federal data ecosystem will be needed to respond to the challenge of reducing poverty and vulnerability in Nepal, especially in the context of an ongoing devolution**

⁷ <https://npc.gov.np/images/category/230110051631MTR%20Final%20For%20Website%20Upload.pdf> (in Nepali)

⁸ World Bank, 2019.” Envisioning a Future Data Ecosystem in a Federal Nepal”

⁹ The risks of this significant reliance on international labor markets are amplified by the concentration of migrants in India, and four oil-dependent countries (World Bank, 2018)

¹⁰ The 2017/18 NLFS estimated that 59.3 percent of individuals above the age of 15 were engaged in at least one such subsistence activity (over the last 30 days prior to the NLFS interview). Food production, processing and storage accounted for a bulk of this type of work, with 55 percent of Nepalis (aged 15+) engaged in this activity

¹¹ Approximately 80 percent of the population is at risk from natural and climate-induced hazards and ranking 10th among the most climate-risk-affected countries in the world between 2000 and 2019 (Global Climate Risk Index 2021).

process to provincial and local governments. Supporting an inclusive growth process will require federal data systems that can track and then respond to the high degree of vulnerability alongside unequal opportunities for certain social groups and (remote) geographic areas by widening the current reach of social protection systems; and operationalizing social protection mechanisms that can be quickly scaled-up, especially in response to disasters. In the context of an ongoing policy shift towards deepening fiscal federalism, spatial disparities that underly unequal opportunities can also be addressed by incorporating spatial equity considerations into formulae that determine resource transfers from the federal to provincial governments; and by incentivizing better performance and improved accountability for equalizing such outcomes at all levels of government.¹²

20. The Plan emphasizes the importance of fiscal federalism to enable federal, provincial, and local level governments to carry out their mandates. The Plan notes the many challenges subnational governments face at this early stage of their development, including a lack of data, insufficient financial management experience, the inability to identify the expenditure needs of subnational governments, legal gaps, revenue mobilization, and internal debt mobilization. Four strategies and 18 working policies to address these challenges are listed in the Plan, including strengthening the National Natural Resources and Fiscal Commission's institutional capacity which is an area of World Bank support. As federalism in Nepal is an ambitious and recent undertaking, it is expected that deepening and perfecting the new tiered governmental system will take decades of effort. Thus, full achievement of the Plan's expected results of achieving transparent, predictable, and just intergovernmental fiscal transfers alongside subnational fiscal discipline is likely to extend beyond the timeframe of the Plan.

V. SUMMARY AND CONCLUSION

21. The need to build resilience in livelihoods that are structurally vulnerable to poverty, through policies and investments that can boost productivity and reduce the effective distances to economic activity and better jobs through connecting infrastructure, has been a long-standing challenge in Nepal. In the context of an ongoing and yet incomplete structural transformation, investments in improving productivity, both in agriculture and by better leveraging the agglomeration potential of cities, will be vital to building such resilience. Infrastructural investments that improve connectivity in Nepal have been demonstrated to play a role in increasing returns to rural agriculture, and benefits to market specialization have been shown to accrue even in smaller cities. At the same time, despite a steady movement of population into urban areas,¹³ Nepal's urbanization has not been accompanied by economic growth rates that have accompanied urbanization elsewhere in South Asia. In this context, enhancing connectivity of remote regions and public investments in infrastructure and services will be required to increase sectoral returns, and benefits to market specialization and urbanization. To the extent that improving returns to economic activities also rely on Nepal's natural resource base as a source of livelihoods, ensuring environmental sustainability of new

¹² World Bank, February 2018 "Nepal: Systematic Country Diagnostic, A New Approach for a Federal Nepal.

¹³ It is estimated that between 17 and 26 percent (based on the 2011 census and Agglomeration Index respectively) of Nepal's population lives in urban areas (World Bank, 2019).

investments (public and private) will be critical, especially given both the rising risks to climate change in Nepal, and the high incidence of these risks amongst the rural poor.

22. While it is clear from the government’s own mid-term review that macroeconomic targets including GDP growth are unlikely to be met by FY24, progress has been advancing on other goals. On the positive side, construction of priority investment projects including the Melamchi Drinking Water Project, the Tamakoshi Hydroelectric Project, the Gautam Buddha International Airport and the Pokhara Regional International Airport implemented over the past 10 years have been completed.

23. The Plan acknowledges that delays in project implementation are negatively impacting completion of public capital investments, public-private partnerships, and road infrastructure. Remedies proposed in the Plan to address these delays include starting project implementation after preparatory actions have already undertaken place, such as land acquisition, right of way, and project timelines. Three years into the Plan timeframe, unfortunately project implementation does not appear to be accelerating. As of FY23, a range of issues persist including insufficient budget and counterpart fund allocation, slow decision making, delays in procurement, safeguard issues relating to compensation and land acquisition, frequent turnover of staff, and weak staff capacity at both the federal and local level. The World Bank and development partners are currently working with the government to identify and unlock barriers delaying project implementation to accelerate development progress nationwide.

ANNEX: SELECTED ECONOMIC INDICATORS

SELECTED INDICATORS*	FY17-19 Avg	FY20	FY21	FY22e	FY23f	FY24f	FY20-24 Avg
INCOME AND ECONOMIC GROWTH							
GDP growth (annual %)	7.8	-2.4	4.2	5.8	4.1	4.9	3.3
GDP per capita growth (annual %, real)	6.5	-4.1	1.9	4.1	2.9	3.7	1.7
GDP per capita (US\$, nominal)	1125.1	1139.2	1208.1	1314.3	1346.7	1488.0	1299.3
Private Consumption growth (annual %)	5.0	3.6	4.3	5.4	2.5	3.7	3.9
Gross Investment (% of nominal GDP)	32.3	30.5	29.9	29.4	23.5	26.7	28.0
Gross Investment - Public (% of nominal GDP)	10.3	7.7	8.4	7.4	7.2	7.5	7.6
MONEY AND PRICES							
Inflation, consumer prices (annual %, EOP or MRV) ¹	4.8	4.5	..	..	..	..	..
Inflation, consumer prices (annual %, period average)	4.4	6.1	3.6	6.3	6.8	6.0	5.8
Broad Money (% of GDP)	88.9	108.8	120.5	113.5	114.2	116.6	114.7
Domestic Credit to the Private Sector (% of GDP) ²	74.6	88.4	..	..	..	..	88.4
10 year interest rate (annual average) ³	..	..	..	..	..	..	..
Nominal Exchange Rate (local currency per USD)	107.8	116.3	117.9	120.8	130.0	130.0	123.0
Real Exchange Rate Index (2015=100)	102.9	105.8	101.2	102.8	97.4	93.4	101.3
FISCAL							
Revenue (% of GDP)	21.8	22.2	23.7	23.2	21.9	22.5	22.8
Expenditure (% of GDP)	26.3	27.6	27.7	26.8	25.4	25.7	26.9
Interest Payments (% of GDP)	0.4	0.7	0.8	0.9	1.4	1.1	1.0
Non-Interest Expenditure (% of GDP)	25.9	26.9	26.9	25.8	24.0	24.6	25.9
Overall Fiscal Balance (% of GDP)	-4.5	-5.4	-4.1	-3.5	-3.5	-3.2	-4.1
Primary Fiscal Balance (% of GDP)	-4.1	-4.7	-3.3	-2.6	-2.1	-2.1	-3.2
General Government Debt (% of GDP)	25.5	36.9	40.6	41.5	41.7	41.6	40.2
External Public Debt (% of GDP)	14.7	21.1	21.9	21.1	20.5	19.8	21.1
EXTERNAL ACCOUNTS							
Export growth, G&S (nominal US\$, annual %)	3.9	-14.2	-16.9	46.0	6.2	25.4	3.3
Import growth, G&S (nominal US\$, annual %)	19.9	-19.5	22.8	24.3	-17.3	19.5	6.0
Merchandise exports (% of GDP)	2.8	2.8	3.4	4.4	3.6	3.9	3.6
Merchandise imports (% of GDP)	34.5	30.1	35.1	38.6	29.4	31.5	32.9
Services, net (% of GDP)	-0.1	0.0	-1.7	-2.2	-1.8	-1.5	-1.5
Current account balance (current US\$ millions)	-1608.4	-290.3	-2830.7	-5158.3	-1155.4	-1950.9	-2277.1
Current account balance (% of GDP)	-4.8	-0.9	-7.8	-12.8	-2.8	-4.2	-5.7
Foreign Direct Investment, net inflows (% of GDP)	0.4	0.5	0.5	0.4	0.0	0.3	0.3
Multilateral debt (% of total external debt) ⁴	..	..	..	..	..	..	..
POPULATION, EMPLOYMENT AND POVERTY							
Population, total (millions)	28.5	29.3	30.0	30.5	30.9	31.2	30.4
Population Growth (annual %)	1.1	1.8	2.3	1.7	1.1	1.1	1.6
Unemployment Rate	2.8	7.9	1.8	2.5	5.7	7.1	5.0
Inequality - Gini Coefficient ⁵	..	..	..	..	..	..	..
Life Expectancy ⁶	69.1	69.2	..	..	..	..	69.2
OTHER							
GDP (current LCU, millions)	3464008.2	3888703.7	4277301.9	4851624.7	5409129.7	6042998.0	4893951.6
GDP (current US\$, millions)	32089.8	33433.7	36286.5	40149.1	41608.7	46484.6	39592.5
GDP per capita LCU (real)	76809.2	77833.3	79284.6	82504.8	84917.3	88098.2	82527.6
Human Development Index Ranking ⁷	142.3	142	141	..	..	..	..
CPIA (overall rating) ⁸	3.4	3.4	3.4	..	..	..	..
Economic Management ⁹	3.3	3.3	3.2	..	..	..	..
Structural Policies ¹⁰	3.6	3.7	3.8	..	..	..	..
Policies for Social Inclusion and Equity ¹¹	3.7	3.7	3.6	..	..	..	..
Public Sector Management and Institutions ¹²	3.0	2.9	3.0	..	..	..	..

Notes: *.. indicator not available. E - estimate, F - forecast. Data from MFMOD unless otherwise noted.

1/ World Bank GEM database; MRV - Martre cent value.

2/ World Development Indicators Database and World Bank Staff Estimator.

3/ The HDI ranking in 2001 is in relation to 175 countries and in 2010 in relation to 169 countries. Methodological enhancements in HDI calculations have resulted in notable improvements in the countries' ranking.

Sources: MFMOD Database, World Bank WDI and GEM database, IMF.