



## भोकमीठो :

कालिकोटको एक गाउँका बृद्ध दम्पति सुख्खा रोटि खाँदै ।

Developed countries give away millions of dollars a year in foreign assistance to aid developing countries, but what are the effects? Foreign aid flows from developed to developing countries have been hailed as the solution to world poverty. However, aid is beneficial to any country no matter the circumstances needs a great deal of introspection. The influx of massive amounts of foreign aid can have deleterious effects on the governments of the receiving countries, and can end up doing more harm than good in several circumstances. However, discrimination by donor countries on the basis of standards of governance creates new complications. The current foreign aid paradigm should be overhauled, and the new system should take a more nuanced view of international development.

Changing Paradigms of Aid Effectiveness in Nepal

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गाउँको एम्बुलेन्स : सडक अभावमा विरामी बुबालाई स्वास्थ्य केन्द्रतर्फ लगेर जाजरकोटका एक स्थानीय ।

## Changing Paradigms of Aid Effectiveness in Nepal



ISBN 978-9937-2-4061-1



9 789937 240611

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PRABHASH DEVKOTA

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Of Aid Effectiveness In Nepal



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**Editor:**  
Prabhash Devkota



Alliance for Aid Monitor Nepal

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ph: 4426257  
www.abrittimedia.com

**Printed at:**

Express Colour

**Printing Support by:**

ActionAid International Nepal

**Publisher:**

Alliance for Aid Monitor Nepal  
Third Floor, Kala Mandir Bhawan  
Kupondole, Lalitpur.  
P.O. Box 2719  
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[www.aidmonitor.org.np](http://www.aidmonitor.org.np)  
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Printed in Nepal

Soft cover **Price NRs. 250**

Hard cover **Price NRs. 500**

ISBN: 978-9937-2-4061-1

First Edition 2011 (2067 BS)

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# Acknowledgement

Six decades of 'planned development' paradigm in Nepal has brought both the negative and positive criticism about rights, justice and a consolidated mission towards strengthening people's power and local democracy. No doubt in these past years there have been changes in power relations, changes in public consciousness and changes in expanding horizons of expectations. However, a major chunk of society which has been excluded from different forms of state and non state power structures is in a continuous flux of exploitation. This is where there is a big question to our public policies and the resources towards which aim to bring changes in people's life. The question is besides these ambitions why public policies and available internal and external resources have not been able to bring significant changes in the lives of the common people. This raises the question of legitimacy, accountability and transparency on the processes, governance and mechanisms of state and non state actors.

Foreign AID has always been an important area of debate within larger framework of development and rights issues. It has both positive and negative interpretations and understanding. In a way 55 years' planned development trend has been mixed up with the dynamics of foreign aid of different forms. At a time when there are controversies and questions on Nepal's development trends; foreign aid being an integral part of these development dynamics can't remain untouched. Therefore to bring the scene and unseen paradigms of aid politics, aid governance and aid effectiveness **Alliance for Aid Monitor Nepal** realized the gravity of the issues and thought to bring this in larger public domain in the form of a book.

The realities and issues of the aid debate are crucial to Nepal. So far in Nepal however, this debate has been confined in primarily to government circles and to the networks involving major bilaterals and some INGOs. Because aid in Nepal influences the future of every citizen, the debate must become far more public. At a time when Nepal is moving through transformational political stages, citizens and civil society generally



must be encouraged and enabled to join the debate about aid, to challenge and criticize when appropriate; to hold those engaged in the aid industry to account; to recognise and celebrate what is progressive and successful, to reflect on and debate on the wider issues of aid and to seek out best practice and spread it wherever possible. With an aim to engage and initiate a discourse on aid within people's politics, this forum (**Alliance for Aid Monitor Nepal**) aims to open up a creative and critical space. In this endeavor **ActionAid Nepal** and **Care Nepal** also have been part of us in our journey.

It is a matter of pleasure for Alliance for Aid monitor Nepal to bring out this book as a representative voice of contemporary academicians, researchers, development practioners and freelancers working and contributing around the issue of aid politics and aid governance in Nepal. The book aims to underscore critical realities at the ground so as to inform policy and develop a common understanding to better strategize interventions in foreign aid sector.

Despite bulks of efforts and resources, communities are forced to face multiple crises till. This has raised concerns about accountability, transparency and responsibility in our efforts, knowledge, practices, and attitudes and in the mean time it highlights the issues that have been undertaken.

Time has come for civil society, government and donors to be serious on the issues of foreign aid and its effectiveness to initiate organized actions and concrete public initiative to bring sustainable improvements in the lives of the common people.

We always appreciate the efforts of the entire team; special thanks to Dhan Bahadur Rai, Rita Shrestha, Ranjana Sharma and Breez Lal Chaudhary for their hard work. We acknowledge Mr. Prabodh Devkota for his critical suggestions and support. We sincerely would like to express special thanks and gratitude to **Mr. Bimal Phnuyal** for his advice and feedback to enrich the book and the encouragement he showed to make it happen. Nevertheless we are very much thankful to the authors without whom it would not have been a reality. Special thanks goes to Om Ashtha Rai for his hardwork in proof reading. In the meantime Alliance for Aid Monitor Nepal promises to bring other books on the sector.

Thanking you all!

Sincerely

Prof. Dr. Keshab Raj Khadka

Chair-Person

Alliance for Aid Monitor Nepal

# Acronyms:

AAA	Accra Agenda for Action
ADB	Asian Development Bank
AfT	Aid for Trade
APECF	Asia Pacific Exchange and cooperation Foundation
APP	Agriculture Perspective Plan
BBC	British Broadcasting Corporation
BIMSTEC	Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation
BOOT	Build-Own-Operate-Transfer
BPfA	Beijing Platform for Action
CBS	Central Bureau of Statistics
CDM	Clean Development Mechanism
CDPS	Central Department for Population Studies
CEDAW	Convention on the Elimination of All Forms of Discrimination against Women
CF	Community Forest
CFUGs	Community Forest User groups
CIAA	Commission for Investigation of Abuse of Authority
CPI	Consumer Price Index
UCPN(M)	Unified Communist Party of Nepal(Maoist)
CRS	Creditor Reporting System
CSOs	Civil Society Organizations
CSRC	Community Self Reliance Centre
DAC	Development Assistance Committee
DANIDA	Danish International Development Agency
DFID/UK	Department for International Development / United Kingdom
DIIS	Direct Inversion in the Iterative Subspace
DPR	Department of Petroleum Resources
DPs	Donor Partners
EnL	Endogenous and Local Resources
EnF	Endogenous and foreign aid
EU	European Unions
ExL	Exogenous and Local Resources
ExF	Exogenous and Foreign Aid
FA	Foreign Aid
FAO	Food and Agriculture Organization
FAIS	Food Aid Information System of the WFP
FCPF	Forest Carbon Partnership Facility
FDI	Foreign Direct Investment
FFW	Food-for-Work
FIP	Forest Investment Program
FINIDA	Finnish International Development Agency

FPI	Food Price Index
FPW/FNDI	First Project Worldwide/First Nations Development Institute
FY	Fiscal year
GBA	Gender Budget Audit
GDP	Gross Domestic Product
GEF	Global Environmental Facility
GFP	Gender Focal Points
GHG	Global Greenhouse Gas
GNI	Gross National Income
GoN	Government of Nepal
GRB	Gender Responsive Budget
GRBC	Gender Responsive Budget committee
GTZ	German Development Cooperation
HDR	Human Development Report
HIC	High Intensity Conflict
HLF-4	Fourth High Level Forum
IATI	International Aid Transparency Initiative
IFA	Institute for Foreign Affairs
IFSC	International Financial Services Center
ILO	International Labor Organization
IMF	International Monetary fund
INGO	International Non Government Organization
IPOs	Indigenous Peoples' Organizations
IR	International Relations
ITCSD	International Centre for Trade and Sustainable Development
JICA	Japan International Cooperation Agency
KP	Kyoto Protocol
LDCs	Least Developed Countries
LIC	Low Intensity Conflict
MDBs	Multilateral Development Banks
MDGs	Millennium Development Goals
MfDR	Managing for Development Resources
MGEP	Mainstreaming Gender Equity Program
MOF	Ministry of Finance
MOWSCW	Ministry of Women Child and Social Welfare
MPI	Multidimensional Poverty Index
MRV	Monitoring, reporting and Verification
MTEF	Mid-Term Expenditure Framework
MW	Mega Watt
NAGDP	Non agricultural GDP
NAP	National Action Plan
NDCM	Nepal Donor Consultation meeting
NDF	Nepal Development Forum
NFC	Nepal Food Cooperation
NGO	Non Government Organization
NLSS	Nepal Living standard Survey
NORAD	Norwegian Agency for Development Cooperation
NPA	Non Performing Assets
NRB	Nepal Rastra Bank
NRN	Non- Resident Nepalese
NSCFP	Nepal Swiss Community Forestry Project

ODA	Official Development Assistance
OECD	Organization for Economic Co-operation and Development
OECD-DAC	Organization for Economic Cooperation and Development- Development Assistance Committee
OPHI& HDR	Oxford Poverty and Human Development Initiative & Human Development Report
P	Panchayat Era
PD	Post-domestic Era
PEFA	Public Expenditure and Financial Accountability
PIUs	Project Implementation Units
PPP	Public-Private-Partnership
PQASSO	Practical Quality Assurance System for Small Organizations
PRSP	Poverty Reduction Strategy Paper
PRROs	Protracted Relief and Recovery Operations
PT	Political Transition
REDD+	Reduction of Emissions from Deforestation and Forest Degradation
RRR	Relief, Rehabilitation and Reconstruction
SAARC	South Asian Association for Regional Cooperation
SAFTA	South Asian free Trade Area
SAP	Structural Adjustment Programs
SAWTEE	South Asia Watch on Trade, Economics and Environment
SCF	Strategic Climate Fund
SDC	Swiss Development Cooperation
SLR	Statutory Liquidity Ratio
SMEs	Small and medium scale enterprises
SOEs	State Owned Enterprises
SSRP	School Sector reform Project
SWAp	Sector Wise Assistance Program
SWC	Social Welfare Council
TRIPS	Trade-Related Aspects of Intellectual Property Rights
UCPN (M)	Unified Communist Party of Nepal (Maoist)
UMN	United Mission to Nepal
UNO	United Nations Organization
UNIFEM	United Nations Development fund for women
UNDP	United Nations Development Program
UNFCCC	United Nations Framework Convention on Climate Change
UNFPA	United Nations Population Fund
UN-REDD	United Nations Collaborative Programme on Reducing Emissions from Deforestation
UN-WFP	United Nations World Food Program
USAID	United States Agency for International Development
USD	United States Dollar
USSR	Union of Soviet Socialist Republics
US	United States
VDCs	Village Development communities
VAT	Value Added Tax
WB	World Bank
WDR	World Development Report
WFP	World food Programme
WFP/NDRI	World Food Program/ Nepal Development Research Institute
WTO	World Trade Organization
WWF	World Wildlife Fund



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# **Introduction:**

## Effectiveness of Foreign Aid in Nepal's Development

Politics of foreign aid has become one of the most influential economic statecrafts in international relations. Foreign aid has played pervasive role in the life of the people of developing countries and will continue to play such a role in the coming decades. There is, however, a steady transition in the nature of aid springing from the patron-client network in the colonial days to economic take off and modernization logic in the cold war, to human rights, democracy, equity, good governance, civil society and sustainable development in post cold war years to post-conflict peace building and state building now in fragile states. The growing discontent with aid in the earlier years was that it has only increased bureaucratic control of the life of the people as development meant adopting the life-style and political culture of elites through their material prosperity, not the social transformation for enhancing life-choices of people. Bureaucratization of aid has diminished the potential of market economy, individual freedom and ability to reach to the needy people. Changing development concepts and policies tied with aid politics of creating dependency has engendered corruption and national ability to plan development on a rational manner. In many developing countries foreign aid has imposed the knowledge, institutions and values of dominant culture and made the people victim of aid. This means most of aid were not geared to fulfill saving, investment and foreign exchange gaps or to combat poverty, inequality and unemployment but to tie the receiving countries to the demand of donors. The result is mal-development and disharmony between state and social classes. The shifting attitude in development aid, therefore, marks its changing strategic, political and economic rationality.



The new debate, therefore, demands transparency and efficiency of “aid effectiveness” guided by prudent policies and ownership of national government to achieve better outcome of Millennium Development Goals. The aid effectiveness can be seen in the overall context of the countries in transition and their ability to overcome development deficiencies by bringing coordinated international cooperation to complement recipient countries’ overall human and non-human capacities. Growing aid fragmentation owing to undefined nature of division of labor among the aid agencies and entry of multiple actors in various sectoral areas have nourished adverse impact of the intention of aid and even weakened the government’s democratic accountability towards parliament, parties, civil society, media, private sectors and citizens. In this context, an assessment of effectiveness of aid in many sectors of a country’s political economy like Nepal can help both the policy makers and donors to understand the process of evaluation of the principles underlined in Rome, Paris, Accra and now in Busan in South Korea. The democratic principles of engagement in terms of ownership, alignment, harmonization, management of results and mutual accountability are expected to bear positive effects than the earlier strategies. In the light of these concepts the articles in this volume explain Nepal’s case reflecting various areas and suggest measures as to how aid effectiveness can be increased benefitting the well-being of its people through balanced and sustainable development.

Keshav Acharya explains the “Behavior of Foreign Aid through Recent Political Phases.” His paper divides the span of 24 fiscal years (1986/87-2009/10) into five distinct political phases: 1) 1986/87-1990-91 as the political party-less Panchayat era, (P) 2) 1991/92- 1995/96 as the post-democratic era (PD), 3) 1996/97-2000/2001 as Low Intensity Conflict (LIC), 4) 2001/02-2005-06 as High Intensity Conflict (HIC), and 5) 2006/07-2009/10 as Political Transition (PT), and examines the performance of foreign aid with respect to its support to the national budget, external economy, and the overall national economy of Nepal. There are three sources of financing development expenditures. They are foreign aid, revenue surplus (revenue less regular expenditures) and domestic borrowing. It clearly demonstrates that foreign aid is still the major source of financing development expenditures. Its share in the development expenditures ranged from a high of 49 percent in **P years to a low of 34 percent in the PD years**. Currently it stands at 39.1 percent. What is pleasing is, since the HIC years, most of it is coming in the form of grants. Revenue surplus also contributed significantly in the post democracy years. Thus, since the onset of the conflict, development expenditure has been largely relying on the ODA, that too on grants. The expenditure composition has undergone a great structural shift and increasing share of the total expenditure is consistently being financed by additional revenue efforts. During decade-long conflict, the share of development expenditure got compressed by 34 percentages. On financing of the total expenditures, revenue mobilization has been occupying prominent place. But, when analyzing the sources of additional revenue, one should be cautious.

Buoyancy of revenue coincides with the surges in remittances inflows.

Viewed in relation to the total expenditures, net ODA inflows reveal the following three striking features. First, it has consistently declined in each successive phases, while stagnating at the current PT phase. Secondly, grants have overtaken loans by a wide margin since the HIC phase. And, thirdly, net foreign loans (gross disbursement less repayment of principal and interest) have evaporated since the HIC years. Net ODA inflows which had financed a third of the total expenditures in P years, dropped to 22 percent in the PD years, further down to 18.6 percent in the LIC years, and stabilized at 13 percent since the HIC years. Net loans constituted two-third of total aid in P era, dropped down to less than three-fifth in the PD years, and little over half in the LIC years, and a negative 0.8 percent in the current transition. A negative loan flow means repayment exceeded disbursement or Nepal repaid more than what it received as fresh loans.

The relative squeeze in the size and composition of the development expenditure demands an increase in the level of ODA, so that it can at least compensate for the loss in the revenue surplus. Unfortunately, it did not happen. This reveals that donors are much more incrementalist and bureaucratic than the Government of Nepal (GoN). People's need and expectation in this situation calls for massive increase in the size of the development expenditure from current one-third to two-third. This is where the government of Nepal and its development partners need to co-work as early as possible.

It is salient to see that the onset of the conflict marked a consistent narrowing of the gap between exports and gross foreign aid. Over the years foreign aid is turning into less important sources of supporting Nepal's Balance of Payments (BOP). Nepal's external sector or BOP is getting much more reliant on remittances than any other sources. On the part of foreign aid, it is grant rather than loan which is relatively growing over the years. Nepal is getting less and less indebted. The stock of external debt increased from 2.8 years' equivalent of total annual foreign exchange earnings in P years to 3.1 years' equivalent during the PD phase. It stagnated at 3.1 years' equivalent during the LIC era and less than two years' in the HIC. In the ongoing PT phase, the total stock of external debt stands at less than a year's worth of total foreign exchange earnings.

There are three major issues that Nepal should consider in the management of the external sector of its economy. The first and the most important factor is the relative decline of exports. For GDP growth, employment generation and poverty alleviation, export promotion should be encouraged by all. Second, most of the remittance is pushing up import supported consumption boom which is not sustainable. The authorities and the private sector should find out productive avenues for remittances. Third, the government and the donors should continue to adhere to the recently unfolding grant-dominant aid strategy. At the same time, given a very comfortable debt servicing burden and a very poor current status of harnessing abundant natural resources, Nepal should not shy away from the external borrowings.

There has been a sharp decline in the share of agriculture in the aggregate GDP over the years. It declined from nearly half in the last five years of the Panchayat regime to nearly 42 percent in the democratic era. It dropped slightly to two-fifth in the LIC years. It further drops to 36.7 percent in HIC and to 34.2 percent in the PT years. Agriculture is now being consistently marginalized. During Panchayat, it received over 13 percent of the total budget. It dropped to 10.5 percent in PD, 8.9 percent in LIC, 6.3 percent in HIC and further down to 6.2 percent in PT. Except for PD phase, the same trend is evident with aid composition. Nevertheless, as a share of the total, the aid share to the agriculture has always remained higher than the government's budget share to the agriculture sector.

Nepal's debt profile is very healthy. Total debt stock spiked from 49.8 percent of GDP in P to 66.6 percent in the PD era. From then on, it is steadily declining as a percent of GDP. It declined to 64.3 percent in LIC, 60.5 percent in HIC and further down to 43.9 percent in the PT. Debt accumulation grew at a pace lower than the growth rate in GDP.

Gross foreign aid fell from 7.7 percent of GDP in the Panchayat era to 5.9 percent in the PD and to 5.7 percent in the LIC. It drastically fell to 3.7 percent in the HIC and slightly exceeded 4 percent in the PT. The drop occurred due to a sharper drop in the loan component, particularly since the HIC period. Of the total ODA, loan comprised 72.7 percent in P, 71.2 percent in PD, and 70.2 percent in LIC. It very sharply dropped to 40.5 percent in HIC and further down to 26.8 percent in the PT. It is good that grant has overtaken loans as it mitigates future contingent liabilities, that too in foreign exchange. But, what counts most is the quality rather than the size of the grant. The study suggests that the growth rate is a shadow or a mirror image of the political cycle. When polity is stable, the growth rate averages five percent; when conflict ensues and turns combative, it falls to three percent, when there is an expectation of normality, it again goes up to four percent.

Prof. Madan Kumar Dahal highlights "Nepalese Economy: Obsolescence, Underpinnings and Approaches to Sustainable Development." He says that Nepalese economy, largely a subsistence as well as high-cost one with no direct access to sea for expanding international trade, and limited transit facilities, rising interest rate on lending, high tax burden, and costly doing business, is passing through a downswing phase. Despite tremendous natural, human and cultural potentials, it suffers from poverty, inequality and underdevelopment. The economy continues to strangle under the pressure of sluggish economic growth, poor governance and rampant corruption, where a majority of the people lives in abject poverty struggling for their daily survival. Nepal's economic development is, therefore, extremely challenging almost tantamount to intractable journey through silk-road.

The international comparison illustrates that Nepal's economy is clearly trailing behind other member countries in the SAARC region. Prolonged political transition engulfed by growing risks and uncertainties with increasing inefficiency, extortion and political entrenchment jeopardized

the entire prospects for economic development. The recent macroeconomic indicators exhibit that Nepal's merchandise exports to India and overseas have declined resulting in a huge trade deficit amounting to Rs. 330.34 billion, which is estimated to be 25 percent of GDP. It has surpassed the size of budget for FY 2010/11. The size of Foreign Direct Investment (FDI) stagnated at Rs. 58 billion by mid-March 2010 generating employment for 144,513 Nepalese citizens. Nepal's tax system lacks simplicity, transparency and competitiveness, which is detrimental to attract FDI and mobilize indigenous investments. Nepal is disadvantageously placed for international trade and this is the greatest stumbling block to escape from high-cost economy. In addition, the respective governments in the past and to-day are seriously engaged in managing the crisis with little emphasis and priority over resolving crucial economic issues. The issue of modernization and commercialization of agriculture with implementation of scientific land reforms program to increase production and productivity of food and cash crops have remained outside the jurisdiction of national priority. Investment is not a constraint to growth. However, lack of visionary leadership imbued with a strong sense of political will to fulfill aspirations of the common people impedes economic progress and prosperity in Nepal.

While selecting development projects adequate attention should be provided to Medium Term Expenditure Framework (MTEF), Poverty Reduction Strategy Paper (PRSP), and Millennium Development Goals (MDGs) especially to expedite foreign assistance from donor communities for growth, poverty alleviation and employment generation. A top priority should be accorded to expedite investment in mega-projects especially infrastructure such as road and hydropower not only to create employment opportunities at home but also for achieving double-digit growth to make a substantial dent on poverty reduction. Institutional reforms are needed in education, health and nutrition policies to improve quality of human resources enabling them to compete at international labor market for middle level manpower and maximize the benefits offered by globalization. In the light of proposed restructuring of the state it is also important to empower and strengthen local bodies with emphasis on developing a strong nexus between center and the federal states.

The vision or mission of Nepalese economy should be to build a strong economic nation-state through active participation of the people ensuring a high quality of life to each individual and household within the given timeframe. The primary objectives of Nepalese economy should be to increase the magnitude of GNI from a diminutive US\$ 13 billion (as of 2009) to US\$ 100 billion and transform the economy from extremely low GNI per capita (US\$ 440) to a higher GNI per capita (US\$ 3,000) at par with middle income countries by achieving a high, sustainable, broad-based, and inclusive economic growth and eliminating absolute poverty by 2025 and, ultimately, make Nepal "Switzerland" of Asia. Despite numerous structural constraints, there are ample opportunities that Nepal could tremendously gear up the economy by stimulating its major foundations comprising hydropower,

tourism, biodiversity and remittances through foreign employment in cooperation with the private sector.

Narrating “Foreign Assistance: An Unfinished Journey,” Prof. Bishwambher Pyakural candidly affirms that Nepal’s planned development began with the infusion of foreign aid in the 1950s and now it has embarked on 11<sup>th</sup> five-year development plan. While the first four plans (1956-62, 1962-65, 1965-70, 1970-75) laid emphasis on the basic infrastructure development, only the Fifth Plan (1975-80) recognized people-oriented development and the need for egalitarian benefits. The sixth plan focused on meeting basic minimum needs of people through a reduction in income inequality and employment. The seventh plan attempted to bridge development plans and implementation with an aim to increase productivity capacity of economy by expanding physical resources. The eighth plan after the democratic change of 1990 focused on sustainable development, poverty reduction with inclusion of popular programs. With the realization of sector-based development, the ninth plan identified agriculture and forestry, water resources, industrialization, international trade and tourism development with the objective of poverty alleviation. Only in the tenth plan, Poverty Reduction Strategy Paper was aligned with special treatment of marginalized and vulnerable people. In the interlude of Maoist insurgency the two consecutive Interim Plans paid special focus on conflict-sensitive relief, reconstruction, revival of economy, and gave emphasis on good governance, effective service delivery and inclusive development process.

He unveils the pervasiveness of foreign aid in all sectors of Nepal’s political economy: agriculture, irrigation, forestry, transport, power, communication, industry and commerce and even social services. In the process national priorities shifted along with donors. Obviously, foreign aid has positively contributed to per capita GDP in the long run but it is found to be negative in the short-run implying that country suffered from a lack of aid absorptive capacity and high aid volatility. So the main issue is to identify the effectiveness of foreign aid to increase its further efficiency. The criticism that aid has actually hampered development goals of the poor countries is drawing attention to majority of aid practitioners. The rich donors are always behind their commitment to offer 0.7 percent of their gross national income as official development aid. Nepal, however, faces a large discrepancy between aid commitment and disbursement. The reasons are: lack of matching fund; weaknesses on making the claims for reimbursement; and inability to fulfill the agreed grants and loan conditionality.

If the links of foreign aid is seen to democracy, human rights, governance, liberalization and economic reforms backed by reduction of corruption and conflict in recipient countries there is a pause: Aid is effective when it is moderate in volume and counterproductive when it is puffed-up. The central debate over its contribution to national development, therefore, lingers on. Present Foreign Aid Policy, 2002 doesn’t integrate aid with priority developmental activities, and is in major overhaul. Draft Foreign Aid Policy, 2009 intends to develop and adopt a National Action Plan

(NAP) on Aid Effectiveness both by the Government of Nepal and donors, is expected to formulate roadmap on foreign aid management in the spirit of Paris Principles and Accra Agenda for Action. The time, therefore, has come to develop domestic aid policy in compatible with country's priorities and harmonize it with the *New Approach to Development* endorsed by G8 Summit.

Narayan Dhakal critically engages in a complex task of "Challenges of Managing Aid in Evolving Development Dynamics." Management of development aid in tune with new development paradigm is a most daunting challenge. The dynamics of development has now arrived at institutional and contextual concerns with more complexity in terms of aid management. Involvement of multi-level actors in aid relationship is one of the major causes of complexity. The proper use of development aid for development result requires best practices of the donors, recipients and other stakeholders as partly articulated in the Paris Declaration, 2005. But reasons behind low aid-effectiveness are exogenously imposed design of development and endogenous paucity of recipient countries and a lack of proper negotiation between the two. So a mid-way and context friendly approach of development will have to be found as an avenue for result-oriented management of aid. The development management as the nearest theoretical premise, emerged with the insights of reduced bureaucracy, increased private sectors, and improved capacity of grass root stakeholders, encompasses the issues of management of development aid. Introduction of customized approach in aid management, in between exogenous and endogenous processes, is the prime need of all development actors.

The Paris Declaration in more critical fashion is debated the high level forum in Busan of Korea in 2011. Translating Paris commitments into real life situation has remained a challenge amid evolving development orientation. Global synthesis of the phase II evaluation of the Paris Declaration reveals the five principles of aid effectiveness, country ownership has advanced farthest, while alignment and harmonization progressed unevenly and managing for development result and mutual accountability are advancing the least. Nepal participated in the second and third monitoring surveys in 2006 and 2011 respectively, and the second country evaluation of its implementation in 2010. It has raised a strong concern towards development results in Nepal. Its contribution to enhance country ownership and alignment of Development Partners strategies with the national development strategy can be considered moderate. And, its contribution to the use of country system, harmonization and mutual accountability is less plausible.

Broad approaches to development can be grouped into 'exogenous' and 'endogenous.' In developing countries, two types of fund - external resources, i.e. 'foreign aid' and internal resources, i.e., 'domestic revenue' prevail, which follow clearly two sets of values, structures and operational frameworks, resulting in conflict of interests and high transaction costs. Management of aid amid proliferated discrete projects always becomes an issue. The situation then requires harmonization. To make the actors ready

to harmonize, incentives must be aligned at one point from both 'exogenous' and 'endogenous' approaches. The mid-way approach can be developed on country by country basis by ways of customization process. Customization involves close review of two-way incentives system, which can motivate the donors, the recipients, and the civil society, including academia and business community. This is where effective management of aid takes place and can produce desired development outcome.

Bharat Pokharel's "Foreign Aid Politics in Developing Countries" sets the broader context of aid politics in general and developing countries in particular. He assumes that poor countries have huge finance gaps and, therefore, to avoid these countries from poverty trap aid collected from taxpayers of rich nations is shared to them as foreign aid. While Jaffery Sachs in "The end of poverty" argues that shock therapy of aid packages for "bottom billions" can end extreme poverty but he also reveals its profound effects on legitimacy and unseen results and goals. Massive aid has deleterious effects on receiving country's economy. There is no compelling evidence that donors care institutional quality, corruption and good governance in their aid allocation decisions. Instead study suggests bilateral aids are dictated by political and strategic interest of donors.

Colonial history and voting role in United Nations tend to explain more about the effects of aid allocations than its constructive role in building political institutions, robust economic policies and good governance of recipient countries. Massive aid influx provides an easy source of government revenue, and thus reduces the need to build an effective bureaucratic mechanism to oversee the extractive, regulative and administrative functions of the state. The limited extractive capacity, in turn, tends to deepen the government's dependence on rents, and consequently creates a "rentier state." Essentially, the influx of easy money allowed many newborn governments to "substitute aid dollars for state craft," yielding them into the state of aid dependency. High aid dependence leads to strong presence of aid agencies in recipient countries with high chances to bypass the cumbersome government's bureaucracy and poach skilled bureaucrats away from civil service towards aid-sponsored projects. This erosion of talents enfeebles the quality of aid effectiveness and government performances. Theory suggests the importance of institutional quality for economic performance the key to positive development outcome and the very goal of reforms to improve governance and reduce corruption. But as aid distorts the incentive structure for public actors, it can delay institutional reforms and, therefore, tends to be politically less desirable. Aid also creates a "moral hazard" in the recipient country by serving as a permanent soft budget constraint.

Sound policy and good economic management matter more than foreign aid for developing countries. An influential study by Burnside and Dollar finds that aid has a positive impact on growth in developing countries with good fiscal, monetary, and trade policies, but has little effect in the presence of poor policies). On the other hand, discrimination on the basis of institutional quality does not seem to be a feasible strategy for donors like



the IMF or the World Bank as these multilateral institutions cannot withhold its assistance to countries in need on the basis of their poor institutions. Multilateral organizations, therefore, must look for other ways to improve the effectiveness of their lending.

There is rarely a year when some oppressed countries, especially in Asia, Africa and Latin America are not faced with a food crisis due to a natural disaster or war. So it is paramount to highlight foreign aid as a temporary measure. Efforts should be to strengthen local indigenous civil society, and empower people by helping them learn how to help themselves. If foreign aid is hurting rather than helping them, then it is clearly in need of being restructured, so that policy and incentives can be better coordinated to achieve the desired outcomes. In the meantime, research efforts must continue to search for the ways to improve its outcome.

Simone Galimberti spotlights “A bottom up aid effectiveness approach: the case for grass roots level accountability.” The cause-effect nexus between aid and economic growth, as the real engine to take millions of people away from poverty is being questioned. In short, aid is being pushed outside its “comfort zone.” We witness, on one hand, the rise of new form of aid, more focused on social innovation and, we see attempts to reform the way of traditional aid. Within the above mentioned trend, there is the case for a more and better accountability by civil society organizations engaged at grassroots level. The *Bellagio Initiative*, *Aidinfo*, *Open Government Partnership*, *One World Trust* etc are the several attempts of moving forward the agenda of the “real aid”. Although the Busan meeting is a forum on aid effectiveness the ultimate aim is effective development. Unfortunately, there is probably something missing in the global debate on aid effectiveness: effective aid will be achieved when the accountability agenda will be fully endorsed through a new bottom up citizen centered process that keeps the common people in the driver seat of the developing agenda.

Weak coordination and weaker monitoring and evaluation framework are the realities in most of developing countries. Therefore the time is ripe for a strong action, something ambitious, a *Global Compact on Grassroots Aid Effectiveness*, for grassroots quality aid. In order to make this compact a reality, we need to review the roles and responsibilities of civil society organizations, international, locals, CBOs and NGOs. The frameworks at countries level should reflect the domains of the Paris Declaration, nominally *ownership, alignment, harmonization, results, and mutual accountability*. Community ownership as means of empowering local beneficiaries; alignment and harmonization as a compact that prescribes minimum practices and procedures to ensure how a new intervention will really fit in the local priorities set by the district authorities; and accountability defined as common responsibilities to deliver the best service at the best value for money, with highest level of participation of the local beneficiaries, if practically addressed, will offer a real opportunity to “democratize” the way aid is delivered.

Accepting the CSOs as development partners represents a new building



block in the foundations of a new aid system. Fortunately, the constitution of the *Multi Stakeholders Team on Civil Society Development Effectiveness*, formed in April 2009 under the Working Party on Aid Effectiveness of the OECD-DAC, is definitely a giant step ahead. *Open forum for CSO Development Effectiveness* came out with a stronger commitment “*The Siem Reap CSO Consensus on the International Framework for CSO Development Effectiveness*. The key is that better accountability is a precious ingredient to increase and enhance the level of credibility of CSOs.

Nepal is considered a best practice in the international arena for being able to create the conditions for better quality aid being implemented in the Country. As a sign of maturity, the upcoming *Nepal Portfolio Performance Review* (NPPR) to be held on 17<sup>th</sup> and 18<sup>th</sup> of November, will raise the important issue of “mutual accountability” that will also look at the joint responsibilities in strengthening the country system and improve the overall quality of aid delivered to Nepal. A National and regional level dialogue could be initiated in order to collect ideas, analyze current concerns and bottleneck. The selected propositions will be reformulated as a set of standards that will lead to the formulation of the *National Compact on Grass Root Aid Effectiveness* to be officially endorsed by the engaged parties. In quest of establishing the national compacts, the *Compact* could offer minimum standards for bringing aid effectiveness at local level through a set of principles and benchmarks. *The Siem Reap CSO Consensus* could be a good base for discussions.

Nepal is obviously in a good position to show and lead the way in moving forward the agenda of “real aid” at local level. Only if civil society organizations, regardless of their status will agree on working out practical ways to improve their work at local and grassroots level, Nepal will be able to fully take advantage of a new, strengthened “mutual accountability.” The citizen of Nepal will be the real winners of this bold move.

Vidyadhar Mallik focuses on “Aid Effectiveness and Nepal’s Road to Busan.” He argues that the necessity for the management of aid resources was felt in the dawn of 21<sup>st</sup> century. The OECD generated discourses around aid effectiveness with a report called *Shaping the 21<sup>st</sup> century: The Role of Development Cooperation*. Following series of international declaration to achieve development goals, in 2005, 2<sup>nd</sup> High Level Forum (HLF) promulgated “Paris Declaration on Aid Effectiveness” with 56-action commitments and 12 indicators to monitor these commitments, worldwide. The HLF-4 adopted Accra Agenda for Action to accelerate the proper implementation of Paris Principles.

Nepal’s Foreign Aid Policy, 2002 as a guiding and integral principle for the resource mobilization states that foreign aid will be directed to achieve national goal of poverty reduction. It has emphasized on concessional loans and grants, budgetary supports, use of Nepalese resource persons in the technical assistance provided by donors, one door policy for supports through INGOs and NGOs, emphasis on domestic resource mobilization, leadership and ownership of government, supportive role of Nepalese civil society,

building national capacity and partnership, soliciting an increased level of cooperation from donors, better understanding of donors with respect to sensitivity, selectivity, avoiding trial and error methods, maintaining financial discipline, reflection of financial sources in the Annual Budget and improving donor procedures (harmonization). A revised draft named Foreign Aid Policy 2010 also emphasizes on adhering to Paris Principles of aid effectiveness as was reaffirmed by the AAA and aims at transparency, accountability, predictability and sustainability by enhancing national capacities, domestic resources mobilization and optimizing the opportunities for trade and investment. Meeting of Nepal Development Forum and Nepal Port Folio Performance Review are the two pivotal instruments on mainstreaming aid debates in the country.

In 2010, Nepal Country Evaluation for an exercise on a Joint Evaluation of The Implementation of Paris Declaration was carried out by the Ministry of Finance and the development partners. It recommends the replication of sectors-based programs. MfDR has changed making aid delivery more responsive to beneficiaries. The evaluation report states the validity of indicators and says that the implementation of principle has enhanced results. The major problem found is the pervasive incentives within Nepal and DP systems. The finding hugely demands the improvement of institutional capacity, access to information and participation of all levels and proper relational needs between policy, strategy and service to meet the real needs of people. Social inclusion, good governance, state building and post conflict situation, all cross cutting themes have to be integrated within the discourse of aid effectiveness.

So at the prime hour to make Busan Forum for the sake of LDCs, Nepal has to prepare agendas with wide national/international consultations of political parties, academia, development partners, civil society and institution like AAMN. The delegates hence must come up with a single but composite voice of all stakeholders. Agendas should include aid predictability, mid-term support for reconstruction and economic growth, donor harmonization and alignment, MfDR and country ownerships. Our priorities about aid for trade, technical Assistance pooling, capacity building, public financial management, and procurement systems have to be harnessed with acute discussions and broad consultations. A general discourse on 'Development effectiveness' rather than discussions confined to 'Aid Effectiveness' sounds exciting at this stage from both accountability and delivery perspectives. Efforts to satisfy the taxpayers of both donor and recipient countries are needed and Busan HLF-4 should go a long way in this regard.

Meena Acharya while analyzing the "Aid Effectiveness Agenda and Gender Responsive Budgeting – Experience of Nepal" reveals bitter truth about the reality of aid effectiveness on the lives of rural women. The grassroots women have had little voice and influence in development and priority setting processes in Nepal. Only during the preparation of the Tenth Plan (PRSP, 2002-2007) some consultation with women groups from national to regional level took place. However, they have had very little influence on the

budgeting process. When gender quality and priorities are not adequately mainstreamed in the national development plans and the budgets, donors' own gender equality priority becomes ineffective. The Paris Declaration identifies twelve monitoring indicators for measuring public financial management, accounting and auditing systems, procurement systems, results frameworks, transparency and capacity. But none of the assessment tools incorporated elements to monitor gender and social equity. The limitation of system was acknowledged by UNIFEM, the DAC Network and CSOs over world and since 2010 new gender dimensions has been added to the monitoring formats. The 50<sup>th</sup> UN Commission on Status of women adopted "Financing of Gender Equality and Empowerment of Women" and Nepal is obligated to it and it has introduced GRB since the FY 2007/08. This was preceded by a series of Gender Budget Audit (GBA) of several sectors. Thereafter, a new system of budget classification was introduced, with specific focus on 13 ministries.

With Aid Effectiveness agenda Gender Budget Audit and Gender Responsiveness acquired new importance for gender mainstreaming into the mechanism and instruments used in planning and managing development programs. Under Nepal's GRB guidelines, each proposed program has to be scored in accordance with indicators developed by the Gender Responsive Budget Committee (GRBC) led by Ministry of Finance. Programs scoring 50 percent marks or more are classified as "directly responsive," those scoring 20 to 50 percent as "indirectly responsive" and those scoring less than 20 percent as "neutral." The allocation to directly and indirectly gender responsive programs has been increasing slowly.

But Nepal's GRB system has encountered difficulties in implementation because of conceptual and practical capacity problems. She, therefore, suggests that the scoring methodology does not mesh with indicators used in different sectors and so has not been applied systematically. Nepal's GRB system needs to encompass the complete budget cycle and include detail assessments of each with respect to transformative, adequacy, non-discriminatory and monitoring system. Another big challenge to make GRB operational is training and capacity building of the Gender Focal Points in all ministries, planning units in government and local bodies. The focus of GRB has to be broadened from soft sectors like agriculture, health, education, etc to other relevant sectors like law, home, police etc. It is equally crucial that all economic policies are to be filtered through gender and social inclusion lenses.

Dr Tim Cadman and Dr Tek Maraseni discuss "Governing Emissions Reduction: REDD+ and Stakeholder Perceptions of Institutional Legitimacy." They argue that there exist varied perceptions of institutional governance greatly across the sectors and regions, but respondents from the global South rate the mechanism higher than those in the North, irrespective of their sector with implications for the current design and future directions in *market-based approaches to climate change management*. The globalization of politics has led to a commensurate growth of global governance.

Traditional global governance as a matter for individual countries via balance of power politics has now changed into a modern global governance not dominated by nation-state. Multilateral institutions in particular have become central, now differentiated between government and governance. New governance, by contrast to previous approaches, is envisaged as a positive process of learning and a system of more democratic mechanism and dynamic interplay between civil society, business and public sector over the issue of corporate social responsibility. Hence it is significant to identify whether the policy programs aimed at reducing greenhouse gas emission are solving the problems and changing behaviors or making perverse outcome for development.

REDD is an initiative to reduce greenhouse gas (GHG) emissions which allows 'avoided deforestation' in to be included in market-based carbon trading mechanisms. It is effectively a payment in exchange for actively preserving existing forests. It is now formally referred to as REDD+ in the wake of the United Nations Framework Convention on Climate Change (UNFCCC) Conference of Parties (COP) 15 in Copenhagen. It is linked to the Kyoto Protocol (KP) and the Protocol-related Clean Development Mechanism (CDM). The United Nations Collaborative Program on Reducing Emissions from Deforestation and Forest Degradation in Developing Countries (UN-REDD) manages the technical and financial components of the initiative, with the assistance of the United Nations Development Program (UNDP) and the Food and Agriculture Organization (FAO). The Forest Carbon Partnership Facility (FCPF), via the World Bank, provides funding aimed at biodiversity conservation of forests and sustainable use through a range of country-level projects. The Forest Investment Program (FIP) is part of the World Bank's Strategic Climate Fund (SCF), and provides funds to specific sectors and projects to pilot new activities and build capacity in existing activities aimed at tackling climate change. The Global Environmental Facility (GEF), created by the World Bank in 1991, is a partnership arrangement made up of 178 countries, NGOs, the private sector and international institutions.

To ensure that REDD+ meets expectations as one of the solutions to climate change it will require a robust, transparent, inclusive and independent monitoring system capable of addressing governance realities on the ground. Monitoring, reporting and verification (MRV) are essential tools, otherwise REDD+ will go the way of the CDM with over complex rules for many developing countries. The relationship between the CDM and REDD+ remains unclear. REDD+ requires governance arrangements that can deliver large-scale emissions reductions. Inclusiveness of representation of forest dependent people, civil society organizations, and the private sector, as well as systemic transparency are also necessary.

There is an inherent and ongoing tension between sustainable development, and climate governance, for example. Contradictions are evident in the Kyoto Protocol in particular. These realities reinforce the domination of rich countries over poor, whilst alienating the poor from their land and decision making over common resources. Developing countries

argue that developed countries should take the lead in reducing emissions; developed countries in return argue that they were unaware of the impacts of emissions previously and that it is fairer to allocate burden sharing on the basis of current emission levels.

Studying stakeholders' attitudes regarding the evolving governance of REDD+ provides insights into the relative influence of specific sectors, and the quality of the initiatives as a whole. The surveys use an analytical model based on a framework of principles, criteria and indicators of governance quality. The framework of the study is based on a review of governance attributes identified from the fields of international relations, comparative politics, public administration and broader governance theory.

The results would appear to confirm some academic concerns regarding the quality of REDD+ governance arrangements. It reveals the potential existence of a participation gap between financial 'insiders' (such as government) and 'outsiders' (environmental NGOs) regarding REDD+ governance quality. But the results are from a short-term study, and one with relatively few participants. The surveys nevertheless do provide some insights into the quality of governance but are not definitive in their own right. However it is worth making the point that quality-of-governance standards would make it easier for potential and actual participants in global environmental governance systems like REDD+ to determine whether they should engage in a given initiative or not. Standards would also allow potential and actual investors to determine the 'governance risk' of climate change investments.

On "Green Governance" BK Pokharel sets sustainable development in Nepal's political context. Following restoration of democracy in 1990, forest sector governance is one of the few sectors in Nepal which is undergoing massive transformation from conventional technocratic stereo-typed bureaucracy to a pro-poor and democratic public service. Still, it faces a paradox: on the one hand the forest service has started to collaborate with civil society organisations; on the other hand, it suffers from ill-governance practices in matters of policies and regulations. The decision making process is heavily influenced by short-term political and personal interests lacking democratic attributes of public hearing, mass meetings and public poll.

Forestry sector was supported by various donors for period ranging from 5 years to more than 20 years. They contributed on an average US\$20 million per year, totalling about US\$190.8 million in the last twenty years. Most of the aid is spent in kind as facilitation support, infrastructure and capacity building, consultancy services to enhance quality service delivery, social empowerment and technical assistance, and only 20-30% of the total aid is estimated to have spent in cash at local user group and household levels. But local investment of forest users' is much higher than that of total development aid. For instance, in Nepal-Swiss Community Forestry Project (NSCFP), it is estimated that cost borne by community forestry user groups was almost 71% of total cost, whereas donors' and government's share is only 16% and 13% respectively. Role of donors in forestry has been significant

but their impact has been mixed. Community forestry is successful in terms of its visible impact on environmental conservation whereas biodiversity and watershed management, private forestry, non-timber forest products, and research sectors have been largely ignored.

Despite of its huge and successful operation throughout the country, the value of community forestry to Nepal's economy is not well recognized in terms of its overall economic contribution. There are no mechanisms to link community forestry impact monitoring data with the national data because the major part of the nationally unaccounted budget of community forestry borne voluntarily by local communities is larger than the revenue collected by Department of Forest. So, the implication is that forest management through community forestry is the more efficient in terms of revenue generation. In addition to the economic benefits mentioned above, community forestry contributes as a vehicle of social inclusion, gender equality and rural development.

Laxman Acharya and Bidya Nath Koirala critically analyze "Foreign Aid and Education in Nepal: Some Critical Issues" in the historical context. They argue that since 1950s Nepalese governments seemed more open towards the foreign world in order to modernize the country. Being neutral towards superpowers they attracted as much foreign aid as possible. Nepal accepted all forms of aid. As a result, a wide range of donors from capitalist to communist countries, from bilateral to multilateral sources, and even from missionary organizations to INGOs provided assistance to Nepal. All kind of donors have entered Nepal, some with even hidden motives where foreign aid became their entry points. Likewise, the ruling party and government of Nepal also have their own hidden agenda with foreign aid inflow and has been a means to stay in power. Foreign aid has emphasized a lot for the democratization of the country and mainstreaming the deprived section of population in development process. Still, a large number of populations are economically, socially and politically excluded from the mainstream development. They have physically participated in political and development process but neither they are able to put their view nor are their voices heard and heeded. There is also a big gap between elite and marginalized and their relationships as ruler and ruled persists. The impact of foreign aid in Nepal is found having paradoxical results.

Nepal's first Educational Plan was formulated by the financial and technical assistance of USAID. Almost all of the bilateral and multilateral agencies have programs in education sector. The first loan was accepted for Mahakali Rural Integrated Development Program. The visible up and down trend of foreign aid in education makes sense that educational aid has come in a haphazard way rather than in a planned way. In comparison to other sectors, Nepal's education sector is getting more and more dependent on aid. Basic and Primary Education Program (BPEP, 1992-2004), Education for All (2004-2009) and School Sector Reform Program (SSRP, 2010-2015) are the examples. Foreign aid contributes around one-sixth of total educational expenditure and influences the total education investment of the country.

For instance, despite huge investment, the number of public school is shrinking while the number of private school is expanding. Can this be assumed as an unintended effect of foreign aid against public system? This shows that the return of educational investment is not only unproductive but also harmful in many ways.

They point out the contrasting philosophical difference between donors and recipient in giving and taking foreign aid. Looking at the state of aid-driven development process and the socio-economic stagnancy, Nepal's position is nearer to Marxist's theoretical premise. The debate hence gives an idea that the output of development process yielded more unintended with less targeted results wherein the role of foreign aid has been crucial. Hence, they conclude, the time has come to recognize the answers of development failure and illegitimacy of foreign aid in education sectors.

Miriam Bishokarma presents a case study of Himalayan district in her article "Does Food Assistance Matter? It is about the Impacts of Food-for-Work in Mugu. Quoting Amartya Sen's argument that food insecurity mainly springs from social inequalities and failing entitlements, the author adds that entitlements are embedded in the political economy of a society, framed by the ways of distribution of money and productive resources, and by dynamic formal and informal laws, policies and international agreements. Research on social vulnerability to food insecurity further embedded the entitlements approach into a longer-term historical perspective, taking into the account famine and the recovery. So a way to reduce households' or people's vulnerability to food insecurity would be to support their entitlements by increasing their assets and endowments on which their entitlements are based, or to secure them from selling their assets in times of crisis. This is the idea of so called "productive safety-nets." Such a safety-net approach is applied by "Food-For-Work" of the UN-WFP. The impacts of food assistance are differentiated into insurance- and transfer-effects that translate into livelihood decisions and actions. While FFW's positive contribution is the relaxing of household assets constraints, and helping households to preserve assets, it might simultaneously lead to a decline of on-farm activities in favour of food-for-work, or the loss of traditional ecological knowledge, reducing the longer-term coping capacity of recipients, adding up to a "dependency-syndrome."

In Karnali region with the adult malnourishment rate of above 54 percent is the most food insecure area in country. Especially worse is the situation in Mugu district confirmed by a sample survey, conducted in 28 percent of the villages comprising 117 households, based on a stratified random sampling and through various participatory tools, including social mapping, wealth ranking, seasonal calendar, and trend-analysis. The findings revealed that households are characterised by chronic food insecurity form of low production entitlements, unreliable exchange entitlements and different degrees of vulnerability to food insecurity, determined by broader social, political, economical, and cultural aspects. In comparison to those working in NGOs or governmental jobs, worse-off households often engage in



irregular unskilled daily wage labour and thus earn much less. A common strategy among the worse-off groups is also the working migration of men to India. The study revealed that the insurance effects of food assistance were minimal. There is a lack of transparency as villagers assume that the selection of VDCs for the distribution of support was determined by powerful political leaders. Lack of transparency, and longer-term planning on side of the WFP, which is itself dependent on donors' funding decisions hinder the proper application of food assistance as a full-fledged safety-net. It reveals the food assistance's transfer effects were mainly positive for both household's assets-preservation and contribution to assets-creation.

Food assistance through FFW does help people secure their assets during the crises, and increase their overall feeling of well-being and security. Contrary to the accusation that food assistance would result in the decline of recipients' ability to deal with shocks, the study shows that food assistance does not replace other mechanisms of food acquirement but that it rather is an *additional* source of food on which people can rely for their short-term relief. The ultimate goal of food assistance can therefore be described as entitlements protection, and the reduction of vulnerability to food insecurity through an active entitlements *promotion*, including fostering people's ability to cope with shocks and crises on their own. Safety-nets can be regarded as a valuable first step towards this goal. However, in order to cover the entitlements promotion aspect safety-nets should be complemented by cargo-nets, which actively support people in climbing out of poverty through assets-creation. Obviously, food assistance can always only be a part of the solution and must be embedded into broader developmental programmes, designed in cooperation with the government, the donors and civil society. Such a strategy must be based on the needs of food insecure populations.

Chandan Sapkota narrates "Food Security and Aid in Nepal." He says that the steady rise in global food prices has crossed the highest threshold of food crisis now. Not only food prices but also inflation is piercing the Nepali economy. The World Food Program reveals 3.7 million Nepalese are at food-risk as Nepal Government mentions a national food surplus of 110,000 tones in FY 2010/11. Still, 38 districts in Nepal face deficit food production. This consistent skyrocketing of food price could push more people below absolute poverty line. Domestic production deficit is the major reason for the price hike. It generated shocks in local production. The declining supply of agricultural goods at the global level affects food prices in local market as well. The prices are expected to remain at higher levels impacting vulnerable and low-income people. Hence government and donors have a critical role in both lowering food prices and protecting vulnerable population from harsh poverty and malnourishment. Since achieving MDGs is one of the top priorities of donors, the multi-dimensional impact of food process will have an impact on the progress to MDGs and warrants developing partners' focus and major intervention. The amount of aid to food remains un-estimated so far in Nepal. But multilateral and bilateral donors such as WFP, USAID, DFID, ADB and WB, among others, are contributing to address food insecurity



in the country. Aid should primarily focus on increasing production and productivity in 38 food deficit districts. Given the terrain land in hilly districts, right kind of intervention with respect to local context like providing in-kind assistance either food or other necessary households in return of manual works can be considered to reduce the unemployment as well.

He formulates a number of suggestions to overcome food crisis in Nepal. First, there should be higher investment on increasing agricultural production and productivity so that production deficit can at least be narrowed down. Second, provide unhindered distribution of agricultural items in the market while controlling carteling. Regular monitoring of product market by government and implementation of successful cases of good governance by donors can address market inefficiencies and distortions. Third, set up institutional measures to facilitate smooth regional agricultural trade to meet Nepal's food demand. Fourth, addressing emergency situation in the country presupposes the creation of a fully functional regional food bank. The 14<sup>th</sup> SAARC Summit held in New Delhi in 2007 agreed to establish SAARC Food Bank, which is expected to serve as a regional food security reserve for SAARC member countries during normal food shortages and emergencies. Finally, it is high time political leaders, and officials at National Planning Commission, Ministry of Finance, Ministry of Agriculture & Cooperatives, and Ministry of Commerce & Supplies woke up and acknowledged the fact that rising food prices and a potential food crisis pose a real economic threat and could engender political instability. In this context, donors and government have to look at short term and long term options to tackle food insecurity.

Ganga Datta Acharya interlinks hunger and poverty as close and interdependent phenomena. Inadequate access to productive resources such as land, irrigation, seeds, inputs, credits and markets or other sustained means of incomes is the root cause of hunger and malnutrition. Globally, food insecurity is largely a situation created not by lack of food but by poverty and exclusion which deny people access to food. This is true for Nepal as well. Due to the persistent exclusionary value system and practices, all types of productive resources-land, forest and water- as well as other livelihood opportunities available in the societies have virtually been captured by the high-caste male elite classes. With the adoption of Structural Adjustment Programs (SAP) in mid 1980s, nearly 30 years of rampant hegemony of the market-led model of economic growth has been in practice in Nepal that has clearly demonstrated the increased privileges for the few, increased concentration of wealth in hands of few elites and increased inequality resulting into persistent problem of chronic poverty and food insecurity.

The food insecurity problem of Nepal largely bears structural features, but the dominant mode of interventions is technical in nature. Nearly all interventions of Ministry of Agriculture and Cooperatives or WFP or Nepal Food Corporation, all are exclusively production focused and the centrally designed production focused interventions are obviously less relevant or useless for resource poor people particularly landless or marginal

cultivators who live in complex, diverse and risk prone niches adopting multiple livelihoods portfolios. Therefore, food security challenge is not to just produce enough food but ensure required level of food energy intake at household level. Food insecurity is a question of mal distribution of resources and inequality.

Paras Kharel presents “A critical assessment of Third Global Review of Aid for Trade.” The Aid for Trade (Aft) initiative, launched under World Trade Organization (WTO) in 2005, aims to integrate developing countries into the global trading system and also takes an account of the several unsuccessful trade-related technical assistance issues in Least- Developed Countries (LDCs). The monitoring and evaluation of Aft is steered under three mechanisms. First, the WTO and the Organization for Economic Cooperation and Development (OECD) publishes an annual report titled “Aid for trade at a glance” and evaluate the project at the global level based on the OECD’s Creditor Reporting system (CRS). Second, a section on Aft is included from both donors and partners in their respective trade policy review documents. Third, the Periodic discussions on Aft issues occurs within the trade and development committee of the WTO.

Realizing the shortcomings of the present monitoring and evaluation system, South Asia Watch on Trade, Economics and Environment (SAWTEE), Kathmandu and the International Centre for Trade and Sustainable Development (ICTSD), Geneva developed a methodological framework for conducting research on assessing the effectiveness of Aft in six developing countries: Cambodia and Nepal in Asia, Malawi and Mauritius in Africa and Jamaica and Peru in the America. The research made use of both primary and secondary information. Data source from Overseas Development Assistance (ODA) was used for extracting information on Aft. The major findings of research in Nepal showed the Aid for Trade has been more or less growing in Nepal since 2002, in line with the global growth; and the growth has been higher in the recent period (2006-09) compared to the base period (2002-05). The distribution of Aft flows across recipient countries is highly unequal, slightly more so than the distribution of overall ODA.

Most of the analyses in the Report are based on commitments rather than disbursements. In terms of commitment, Aft has become additional but not on disbursement from ODA. Sustainability of Aft is doubtful mainly because of the lack of government’s contribution to the project and prediction of a large number of donors to hire their own consultants rather than building capacity of the local institutions and experts. Hong Kong WTO Ministerial Declaration in 2005 recommended four pillars on Aft. The First pillar is, Additionality, predictability and sustainability. Second is the Effectiveness pillar where ownership, alignment, donor coordination and impact are considered. Coherence is the third pillar where South-South Aft and the coherence of Aft and climate funding is focused. Three additional aspects are considered under the forth pillar: emphasis on grant than a loan, bridging the gap of demand-supply and the countries’ absorption capacity.

While trade has been mainstreamed by half of the partner countries it is

one of the sixth strategies of the current three-year plan in Nepal. The Nepal study finds that most donors are yet to mainstream trade in the planning and implementation of their aid strategy in Nepal. There is inadequate sensitization and awareness about AfT. The Report finds that alignment is improving but the strengthening of partner countries system and aligning aid still lacks. Delivering aid through parallel implementation units is serious issue in Nepal's case. The finding based on the responses from the partner countries says raising awareness about trade's contribution on development and improving the delivery of AfT are its major impacts.

Jagat Basnet indicates Foreign aid in Nepal synonymous to development projects, and so are the elites and development. One cannot exist and function without other. This sentence enough manifested why and how aid is coming in Nepal and how it has been contributing the interest of elite and rulers. The upper social classes derived the major benefits from foreign aided development. The need to legitimize such a power gave foreign aided development the halo of a 'people-oriented development' while at the same time increasing the dependence of the lower classes.

From decades, the World Bank has been promoting market-based approaches to land management through its lending practices and policy advocacy. This means privatization of land rights, both through the conversion of customary rights into marketable titles as well as disengagement of the state, and legal reforms necessary for western style land markets to function. He raises the role of civil society and the real tillers for genuine land reform, increase productivity and food security. His suspicion remains with big IFIs as they are providing the aid to grab the land in different countries, promoting especially market-led, willing buyer and willing seller model of World Bank. Although Nepal has no multinational companies but national elites have been grabbing the rural land in the name of land plotting and commercialization of farming.

## **Conclusion**

Development aid seeks to bridge the gap between wealth disparity in society through sharing and caring. Giving the poor, fragile and developing countries choices about contextual policies encourages them to uplift the well-being of their citizens through inclusive, balanced and sustainable development. There is little option for developing countries to prosper without aid. As global public goods the ethics of aid should, therefore, aim to offer possibilities to self-help in the long run and contribute to global, regional and national security, stability, development and peace. Aid effectiveness in this context presumes a coherent, coordinated, effective and positive impact of aid in the recipient countries and overcome their complex problems from poverty alleviation, food security, economic development, gender empowerment, education, HIV/AIDS to climate change. It also seeks to avoid duplication of projects, unnecessary competition, fostering clientalism and generating social and political conflicts. The crisis of development requires addressing "mutual interest" and complementing the need of society for

freedom and social justice, imperative of the state for order and stability and urgency of liberal international order based on negotiated social contract, not just maintenance of hierarchy of power without global accountability.

Many post-state issues like HIV/AIDs, spread of disease, famine, terrorism, climate change, trade and technology are globally interconnected requiring cooperative solution. In this context, aid effectiveness can resolve many of Nepal's post-conflict and post-state challenges. Definitely, foreign aid has contributed to Nepal's education, health, infrastructural development, agriculture, forestry, communication, and complemented resource gaps in a number of other areas. The more it contributed to soft power of consciousness the greater the demand for it. The *raison d'être* of development aid is premised on expanding the structure of economy. The social modernization of Nepal and its exposure are other two important areas. But, Nepal's history of planned development has faced its own distortions created by its own institutional weaknesses, such as absence of institutional memory in aid negotiation, negotiation without sound preparation, weak articulation of development priority, non-utilization of even aid, lack of coordination among the donors, weak governance, political instability, frequent reshuffle of personnel's in development projects, weak monitoring of aid impact, problem of inter and intra-ministry coordination, etc. Improving the national integrity system of the Nepalese state is one strategy while capturing the synergy of state, market and civil society is the other for aid effectiveness.

As a result, despite the aid policy to spend at least 60 percent of money on program implementation there is an absence of institutional mechanism to do so. Therefore, in each plan formulation the same problems crop up again and again making the proper management of aid disbursement problematic. Strengthening of procedure and mechanism are other keys to improve aid effectiveness and innovation. Donor countries have, therefore, to enhance the capacity of Nepal's public and private institutions and development strategies while Nepalese government has to devise a coordinating mechanism to prevent growing aid fragmentation and enforcing the transparency and accountability of the stakeholders of society including media, civil society and private sectors. The success of aid effectiveness lies in achieving its targeted outcome.

– Dev Raj Dahal  
– Prabhash Devkota



# 1

## Behavior of Foreign Aid over a Quarter of a Century

– Keshav Acharya

**THIS** paper attempts to examine the behavior of foreign aid with respect to its support to the national budget, external economy, and the overall national economy of Nepal over recent political phases of Nepal. For this purpose, the paper splits a span of 24 fiscal years (1986/87- 2009/10) into five distinct political phases. It begins from the last five years (1986/87-1990-91) of the party-less Panchayat era (P). A mass political movement resulted in the restoration of multi-party democratic parliamentary system in 1990 and adoption of a new constitution and holding of the general election in 1991. The paper classifies 1991/92- 1995/96 as the post-democratic era (PD). In 1996, the Communist Party of Nepal (Maoists) [UCPN (M)] went underground and called for the capture of the state power by dint of arms. The conflict lasted for over a decade. The paper classifies armed-conflict into Low-Intensity Conflict (LIC, 1996/97-2000/2001) and High-Intensity Conflict (HIC, 2001/02-2005-06). With the signing of the Comprehensive Peace Agreement (CPA) between CPN (Maoists) and the pro-parliamentary seven party alliances and the consequent Madhesh uprising, all parties agreed to restore the parliament that was dissolved by King Gyanendra in 2004, draft an Interim Federal Democratic Republican Constitution and form an all party government in 2006. Even after successful election for a Constituent Assembly in 2008, the people continue to endlessly wait for the conclusion of the peace process and a new constitution. Hence the period 2006/07-2009/10 is described as a period of political transition (PT).

There are certain caveats before proceeding. All the statistics used here are the average of the numbers of years in each phase, sum total of the five

divided by five. It is done because agreement on foreign aid, its disbursement to the government, the government's spending of the aid money and final reimbursement by the donor has been a lengthy bureaucratic process. The averaging over the period is expected to normalize the impact of delay on agreement, commitment, disbursement, spending, and the outcomes. The paper doesn't talk monotonously on ODA alone. As ODA, from both the donors' and recipient's perspectives, is geared to improving the socio-economic life of the country and its citizens; the paper in the process related aid with various macroeconomic variables such as total expenditures and its components, revenue, domestic borrowings, sources of foreign exchange earnings, debt burden, and its servicing and structural evolution of the Nepali economy over time. Though drawing on the impact of external aid on poverty and equity is of interest and profound importance, this paper stops short of doing this due to the scope, space and time constraints. It is empirically evident that in Nepal foreign aid is shrinking in relative importance compared with the size of the total budget, domestic revenue mobilization, various sources of foreign exchange earnings and the **GDP**. The paper begins with the importance of foreign aid in the national budget followed by its role in the external sectors of the economy. The third section will briefly touch upon the relative role played by the foreign aid in the national economy.

## **Foreign Aid in the National Budget**

The table below makes a comparative assessment of the evolution of expenditure composition over time and financing structure of the budget in terms of revenue, foreign aid (decomposed into loans and grants), and domestic borrowings. Here, foreign aid refers to the Official Development Assistance (ODA) channeled through the national budget. It refrains from looking into the source (multi-lateral, bilateral) and sectoral disbursement and allocations (agriculture, industry and physical, and social infrastructure and so on).

**Table 1.1. Foreign Aid in the Budget (Rs. Millions)**

	Panchayat Era	Post-Democracy Era	Low Intensity Conflict Era	High Intensity Conflict Era	Political Transition Era
	(1986/87-1990/91)	(1991/92-1995/96)	(1996/97-2000/01)	(2001/02-2005-06)	(2006/07-2009/10)
Total Expenditure	17368	35303	62506	93394	193577
Regular	5746	13665	36046	67960	129433
Development	11622	21638	26460	25434	64144
Revenue	8224	20142	38470	62282	129689
Domestic Borrowing	2311	2419	4722	8652	21680
Foreign Loans	4881	7823	11161	7471	10056
Repayment of Principal and Interest on Foreign Loans	1022	3363	5169	7113	10236
Net Foreign Loans	3859	4460	5992	358	-180
Foreign Grants	1837	3319	5639	11505	25263
Total Foreign Aid	5696	7779	11631	11863	25083
Revenue Surplus (Revenue Less Regular Expenditure)	2478	6477	2424	-5678	256

**Notes:**

1. The figures in each cell have been derived by adding annual figures in the group and dividing it by the number of the years in the group.
2. From FY 1998/99, expenditures have been classified into recurrent, capital and principal repayment. This table for comparison purpose adds principal repayment to recurrent and counts it as regular; capital expenditure is taken as development expenditures.
3. All figures are at current prices.

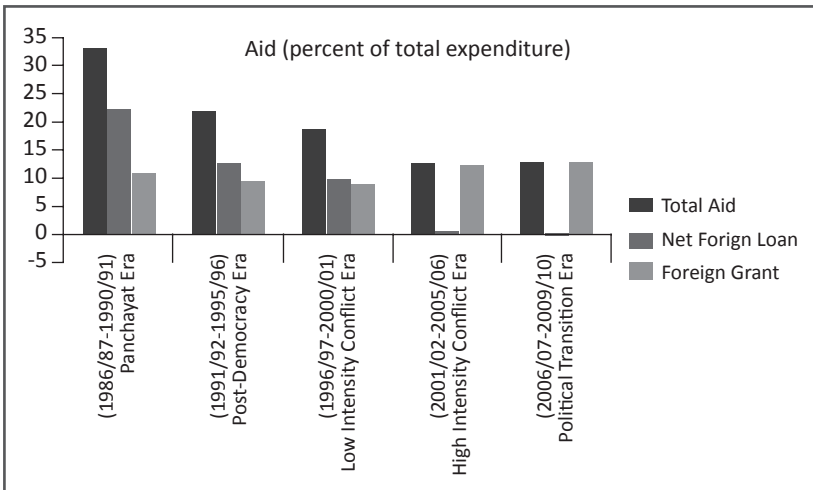
Source: *Economic Survey 2010/2011, GoN/MoF*



**Table 1.2 Foreign Aid in the Budget**

	Panchayat Era	Post-Democracy Era	Low Intensity Conflict Era	High Intensity Conflict Era	Political Transition Era
	(1986/87-1990/91)	(1991/92-1995/96)	(1996/97-2000/01)	(2001/02-2005-06)	(2006/07-2009/10)
<b>A. In Percentage of Total Expenditure:</b>					
Regular	33.1	38.7	57.7	72.8	66.9
Development	66.9	61.3	42.3	27.2	33.1
Revenue	47.4	57.1	61.5	66.7	67.0
Domestic Borrowing	13.3	6.8	7.6	9.3	11.2
Total Aid	32.8	22.0	18.6	12.7	13.0
Net Foreign Loan	22.2	12.6	9.6	0.4	-0.1
Foreign Grant	10.6	9.4	9.0	12.3	13.1
<b>B. In Percentage of Development Expenditures:</b>					
Total Aid	49.0	34.0	44.0	46.6	39.1
Net Loans	33.2	20.6	22.6	1.4	-0.3
Grants	15.8	13.4	21.4	45.2	39.4
Revenue Surplus	21.3	29.9	9.2	-22.3	0.4
Domestic Borrowings	19.9	11.2	17.8	34.0	33.8
<b>C. Repayment of Principal and Interest on Foreign Loan as percent of:</b>					
Total Aid	17.9	43.2	44.4	60.0	40.8
Gross Foreign Loans	20.9	43.0	46.3	95.6	101.8

Source: Table 1.1



A look at the Table 1.1 and 1.2 demonstrates two distinctive patterns. First, the expenditure composition has undergone a great structural shift; and second, increasing share of the total expenditure is consistently financed by additional revenue efforts. For instance, in the final five years of the Panchayat era, regular expenditure comprised one-third of the total, while development expenditure comprised two-third of the total expenditures. Coming down to the present phase of the protracted political transition (FY 2006/7 onwards), this period, it has been the other way round: regular expenditures progressed to two-third and development expenditure regressed to one-third. There has been only a marginal shift in the post-democracy era. The major shift occurs with the onset and the intensification of the conflict. The share of regular expenditure went up from 38.7 percent in PD years to 57.7 percent in the LIC years. This represents an increase of 19 percentage points in a period of five years. And a further increase by another 15 percentage points in the years of HIC, making up 73 percent. Thus, during the decade-long conflict, the share of development expenditure got down by 34 percentage points. Most of the increase in regular expenditures was lumped as internal security expenditures - recruitment, trainings, and deployment of army and police. A part of the increased regular spending was also set aside for salaries and other recurrent expenses for education and health sectors. In the period after the signing of the CPA, the share of regular expenditure declined, the spending was siphoned off from internal security to vital infrastructure projects such as mid-hill highway, Sikta irrigation and Kathmandu-Tarai Fast Track. The socio-political and cultural gains from the conflict are yet to be quantified; but there is no denying that conflict killed greater development opportunities.

On financing of the total expenditures, revenue mobilization is increasingly on high. In the Panchayat era, revenue financed less than half of the total expenditures. It exceeded comfortably above half in the PD phase,

more than three-fifth in the LIC years and two-third thereafter. Including gross domestic borrowing, the share of domestic resources in the financing of total budget increased consistently in each phase: from three-fifth in P era to nearly four-fifth in the ongoing PT phase. However, the conflict has contributed to increase reliance on the domestic borrowing. Nevertheless, the progress made by revenue is far ahead than the reliance put on the domestic borrowing.

It is quite satisfactory to note that revenue has been buoyant in recent years. In fact, in all the four years actual revenues have always exceeded the target by two to four percent. But, when analyzing the sources of additional revenue, there is reason to be cautious. Buoyancy of revenue coincides with the surges in remittances inflow. This fuelled consumption which was met more by import rather than domestic production. Increased customs and VAT were the direct outcomes. Banks paid more corporate taxes by making profits from financing burgeoning imports and real estate. Thus one needs to look into the trade-off between yawning trade gap and the sterling revenue performance. Viewed in relation to the total expenditures, net ODA inflows reveal the following three striking features. First, it has consistently declined in each successive phase, while stagnating at the current PT phase. Secondly, grants have overtaken loans by a wide margin since the HIC phase. And, thirdly, net foreign loans (gross disbursement less repayment of principal and interest) have evaporated since the HIC years. Net ODA inflows which had financed a third of the total expenditures in P years, dropped down to 22 percent in the PD years, further down to 18.6 percent in the LIC years, and stabilized at 13 percent since the HIC years. Net loans constituted two-thirds of total aid in P era, dropped down to less than three-fifth in the PD years, and little over half in the LIC years, and a negative 0.8 percent in the current transition. A negative loan flow means repayment exceeded disbursement or Nepal repaid more than what it received as fresh loans.

In a post-conflict, low income country like Nepal, foreign aid needs to be compared with development, rather than total expenditures. There are three sources of financing development expenditures. They are foreign aid, revenue surplus (revenue less expenditures) and domestic borrowing. A look at panel B Table 1.2 demonstrates that foreign aid is still the major source of financing development expenditures. Its share in the development expenditures ranged from a high of 49 percent in P years to a low of 34 percent in the PD years. Currently it stands at 39.1 percent. The good thing about it is, in the HIC years, most of it is coming in the form of grants. Revenue surplus also contributed significantly until the post democracy years. But the conflict induced swelling of regular expenditures, pulled down the revenue surplus into insignificance in the LIC years, was negative to the extent of 22.3 percent in the HIC years, and is currently less than half of one percent. A negative revenue surplus denotes to a situation wherein the entire revenue falls short of even the regular expenditure. The pathetic shrinkage in revenue surplus is being offset by increasing reliance on the domestic borrowing. Thus, since the onset of the conflict, development

expenditure has been largely relying on the ODA, that too on grants. But, one has to take into account the bitter reality of relative squeeze in the size and composition of the development expenditure itself. In such situation, one expects a sharp increase in the level of ODA, so that it can at least compensate for the loss in the revenue surplus. Unfortunately, it did not happen. It is implicitly suggestive of the fact that donors are much more incrementalist and bureaucratic than the Government of Nepal (GoN). On the part of the GoN too, it should have stepped up its efforts in rapidly securing the disbursement of the aid already committed by the donors. But the entire GoN machinery got bogged down in coping with and abating the conflict. People's need and expectation, in the current juncture, calls for significantly increasing the size of the development expenditure from current one-third to two-third. This is where the government of Nepal and its development partners need to co-work as early as possible.

### **Foreign Aid and the External Economy**

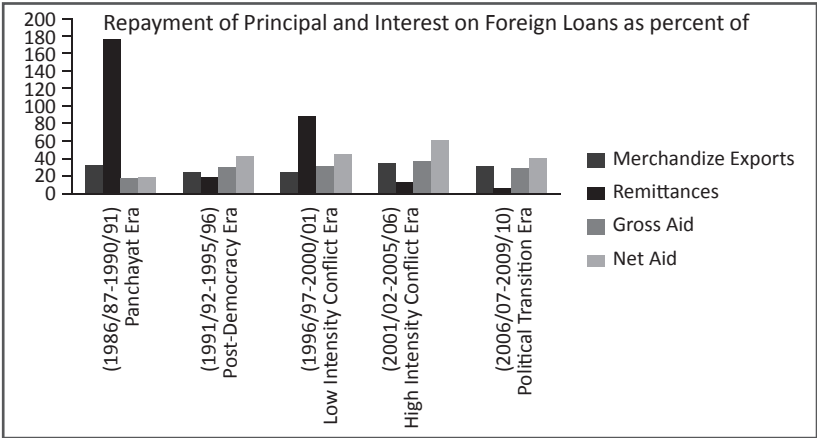
This section examines the relative importance of foreign aid in comparison to Nepal's total amount of foreign exchange earnings, particularly with respect to merchandise exports and remittances. It also examines the size of external debt stock in relation to the total foreign exchange earnings. Finally, this section also looks into the debt servicing burden: repayment of principal and interest on foreign loans in comparison to the total foreign exchange earnings and its principal components; the exports, remittances, and aid inflows.

In the P era, ODA was the single largest source of foreign exchange receipts in Nepal. It was followed by merchandise exports, while remittance was nominal. There was a significant turnaround in the PD years, when remittance exceeded all the other sources of foreign exchange earnings. It was followed by exports, while foreign aid inflows were relegated to the third place. In the LIC years, exports topped the list of foreign exchange earnings which was followed by aid and then by remittances. In the following two phases of HIC and PT, remittances dominate all other sources of foreign exchange earnings followed by exports and foreign aid.

**Table 1.3: Foreign Aid and the External Economy (Rs. Millions)**

	Panchayat Era	Post-Democracy Era	Low Intensity Conflict Era	High Intensity Conflict Era	Political Transition Era
	(1986/87-1990/91)	(1991/92-1995/96)	(1996/97-2000/01)	(2001/02-2005-06)	(2006/07-2009/10)
Total Foreign Exchange Earnings	11345	32265	55320	115128	271915
Merchandise Exports	3396	13358	20848	21194	33981
Remittances	580	18907	5874	53531	163764
Stock of Foreign Loan	32304	100271	171001	225990	249969
Foreign Loans	4881	7823	11161	7471	10056
Less, Repayment of Principal and Interest	1022	3363	5169	7113	10236
Net Foreign Loan	3859	4460	5992	358	-180
Foreign Grant	1837	3319	5639	11505	25263
Total Foreign Aid	5696	7779	11631	11863	25083
Gross Foreign Aid	6718	11136	16800	18976	35319

Note: Same as table 1



**Table 1.4 Foreign Aid and the External Economy**

	Panchayat Era	Post-Democracy Era	Low Intensity Conflict Era	High Intensity Conflict Era	Political Transition Era
	(1986/87-1990/91)	(1991/92-1995/96)	(1996/97-2000/01)	(2001/02-2005-06)	(2006/07-2009/10)
<b>In percent of total Forex Earnings:</b>					
Merchandize Exports	29.9	41.4	37.7	18.4	12.5
Remittances	5.1	58.6	10.6	46.5	60.2
External Debt Stock	284.7	310.8	309.1	196.2	91.9
Gross Aid Inflows	59.2	34.5	30.4	16.5	13.0
Net Aid Inflows	50.2	24.1	21.0	10.3	9.2
Net Foreign Loans	34.0	13.8	10.8	0.3	0.1
Foreign Grants	16.2	10.3	10.2	10.0	9.3
Repayment of Principal and interest on Foreign Loans	9.0	10.4	9.3	6.2	3.8
<b>B. Repayment of Principal and Interest on Foreign Loans as percent of:</b>					
Merchandize Exports	30.0	25.2	25.0	33.6	30.1
Remittances	176.2	17.8	88.0	13.3	6.3
Gross Aid	15.2	30.2	30.8	37.5	29.0
Net Aid	17.9	43.2	44.4	60.0	40.8

Source: Table 1.3

An intriguing fact about the whole trend is that with the onset of the crisis, the gap between exports and gross foreign aid is consistently narrowed down. Incidentally, in the PT years, foreign aid exceeds exports by a small margin of 0.5 percent of the total foreign exchange receipts. What clearly emerges is the fact that over the years and phases, foreign aid is turning into less important sources of supporting Nepal's Balance of Payments (BOP). Nepal's external sector or BOP is getting much more reliant on remittances than any other sources. On the part of foreign aid, it is grant rather than loan which is relatively growing over the years.

On the external debt burden, let us look into the stock and flow terms. Nepal is getting less and less indebted. The stock of external debt increased from 2.8 years' equivalent of total annual foreign exchange earnings in P years to 3.1 years' equivalent during the PD phase. It stagnated at 3.1 years' equivalent during the LIC era and less than two years' in the HIC. In the ongoing PT phase, the total stock of external debt stands at less than a year's worth of total foreign exchange earnings. This is an outcome of two factors. The first and the foremost factor is the continuous surge in remittances; and the other, though of lesser importance, is a turn-around in the composition of aid - from predominance of loans in the earlier years to grants in the successive years. While viewing external debt servicing in flow terms, the scenario is consistently improving. Repayment of principal and interest on foreign loans amounted to nine percent of total foreign exchange earnings in the PD years. It started to decline steadily from LIC years; 9.3 percent in LIC, 6.2 percent in HIC, and to a further low of 3.8 percent in the ongoing PT years. This means, Nepal can service a far higher volume or size of foreign loans, thanks to workers' remittances. Debt servicing amounted to 30 percent of exports and 1.8 times of remittances in the P years (panel B of table 1.4). It improved to a quarter of exports and 17.8 percent of remittances in PD years. Currently it is 30.1 percent of exports and a meager 6.3 percent of remittances. Even compared to gross ODA inflows, debt servicing amounted to 15.2 percent in phase P, 30 to 38 percent in phases PD, LIC and HIC and stands at 29 percent today.

There are three major issues that Nepal should consider in the management of the external sector of its economy. The first and the foremost important factor is the relative decline of exports. For GDP growth, employment generation and poverty alleviation, export promotion should be encouraged by all. It seems the surging of remittances inculcated complacency and inertia on the part of the authority and the private sector. Recently poor export performance has sounded the alarm to all. Secondly, remittances are responsible for pushing up import supported consumption boom which is not sustainable. The authorities and the private sector should find out productive avenues for remittances. Third, the government and the donors should continue to adhere to the recently unfolding grant-dominant aid strategy. At the same time, given a very comfortable debt servicing burden and a very poor current status of harnessing abundant natural resources, Nepal should not shy away from external borrowing. But this

demands capacity building in the government on project identification and prioritization, cost estimation and speedy implementation.

## Foreign Aid and the National Economy

This section reflects on the structural evolution of the Nepali economy over the various political phases. While doing so, it will also look into the sectoral growth patterns and trends. Given the dominance of agriculture in employment and the national output, it will make a comparative assessment of the budget outlays made on agriculture *vis-à-vis* non-agricultural sectors. Similar comparison will be made of total aid disbursement on agriculture and non-agricultural sectors. Finally, as the theme of the paper is foreign aid, it will compare the stock of domestic and foreign loan and also the annual flows of ODA and its component with the GDP.

There has been a sharp decline in the share of agriculture in the aggregate GDP over the years. It declined from nearly half in the last five years of the P era to nearly 42 percent in the PD era. It dropped slightly to two-fifth in the LIC years. It further dropped to 36.7 percent in HIC and to 34.2 percent in the PT years. A close look of table 3.1 reveals a clear cut pattern of a sharper drop from P to PD and from LIC to HIC. Let us first look into high drop years. From P to PD marks a regime shift. De-licensing, decontrol, deregulation and privatization of economic activities after the restoration of the multi-party democracy in the early 1990s enhanced the spectrum of private investment particularly in non-agricultural activities. Relatively larger gains in NAGDP occur in PD and HIC. When the conflict turned violent, agriculture sector bore the full brunt of it. First, the well-to-do rural households were threatened with confiscation of their property, extortion, kidnapping and even murder. They fled to safety from conflict-torn villages. This had disastrous impact not only on agriculture, but the entire rural economy. Second, both the rebel and the government launched recruitment drive in their respective security forces. This squeezed the supply of farm workers. Third, the young boys and girls from poor rural households found new employment opportunities in the oil-rich gulf countries and Malaysia. This further squeezed the supply of farm labour. Fourth, right from the restoration of the multi-party democracy, agriculture and rural sector completely lost the patronage and support from the government.

Thus, what emerges as conclusion is the fact that a sharp or a mild drop in the output share of agriculture is a direct function of the extent of shock. The massive the shock the larger the drop, and the milder the shock milder the drop! This explains a faster pace of non-agriculturization in PD and HIC, and a slower pace in LIC and PT.



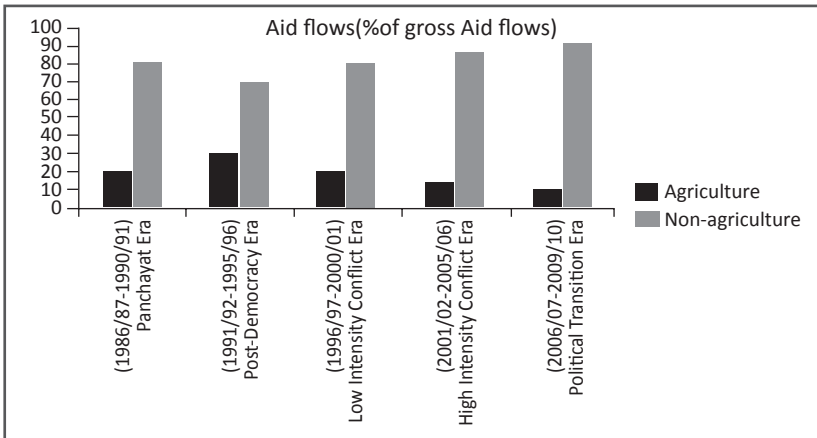
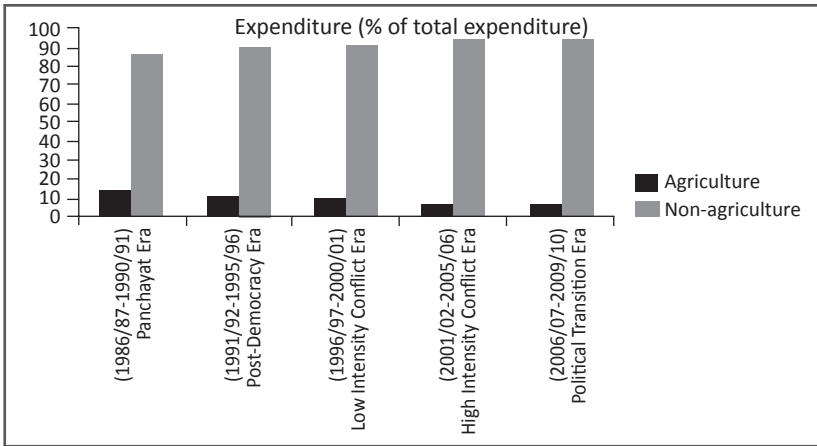
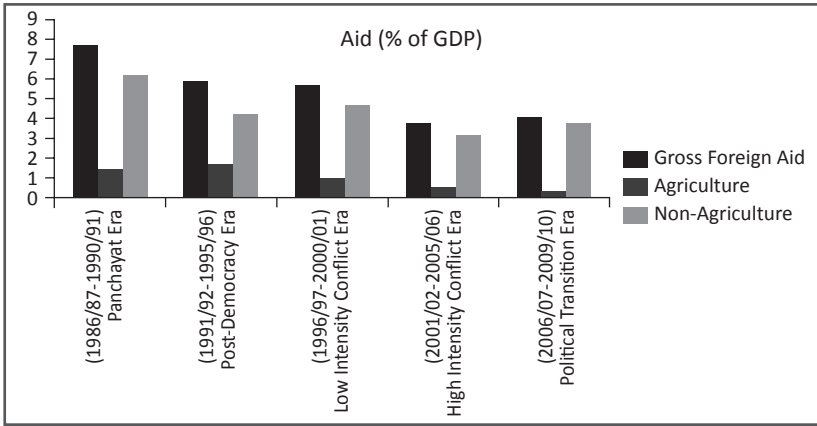
**Table 3. Foreign Aid and the National Economy (Millions Rs.)**

	Panchayat Era	Post-Democracy Era	Low Intensity Conflict Era	High Intensity Conflict Era	Political Transition Era
	(1986/87-1990/91)	(1991/92-1995/96)	(1996/97-2000/01)	(2001/02-2005-06)	(2006/07-2009/10)
GDP at factor cost (Current Ratio)	87194	190249	331813	510205	850334
Agriculture	43158	79660	131245	187218	291047
Non-Agriculture	44036	110589	200568	322987	559287
Gross Foreign Aid	6718	11142	16800	18976	35319
Agriculture	1295	3251	3210	2577	3238
Non-Agriculture	5423	7891	13590	16399	32081
Total Debt Stock	43380	126718	213514	308809	373357
Domestic	11076	26447	42513	82819	123388
Foreign	32304	100271	171001	225990	249969
Gross Foreign Aid	6718	11142	16800	18976	35319
Grants	1837	3319	5639	11505	25263
Loans	4881	7823	11161	7471	10056
Period Average Growth Rate	5.2	5.0	3.2	3.1	4.1
Agriculture	4.0	1.9	3.2	3.3	2.8
Non-Agriculture	6.3	7.3	5.7	2.9	4.9
Budget Outlay on Agriculture (Regular + Development)	2364	3693	5550	5917	11937

**Table 1.6 Foreign Aid and the National Economy**

	Panchayat Era	Post-Democracy Era	Low Intensity Conflict Era	High Intensity Conflict Era	Political Transition Era
	(1986/87-1990/91)	(1991/92-1995/96)	(1996/97-2000/01)	(2001/02-2005-06)	(2006/07-2009/10)
In Percent of GDP					
AGDP	49.5	41.9	39.6	36.7	34.2
NAGDP	50.5	58.1	60.4	63.3	65.8
Total Debt Stock	49.8	66.6	64.3	60.5	43.9
i. Domestic	12.7	13.9	12.8	16.3	14.5
ii. External	37.1	52.7	51.5	44.2	29.4
Gross Foreign Aid	7.7	5.9	5.7	3.7	4.1
i. Grants	2.1	1.7	1.7	2.2	3.0
ii. Loans	5.6	4.2	4.0	1.5	1.1
Gross Foreign Aid	7.7	5.9	5.7	3.7	4.1
i. Agriculture	1.5	1.7	1.0	0.5	0.3
ii. Non-Agriculture	6.2	4.2	4.7	3.2	3.8
Total Expenditure	19.9	18.6	18.8	18.3	22.8
In Percent of Total Budgetary Expenditure					
Agriculture	13.6	10.5	8.9	6.3	6.2
Non-agriculture	86.4	89.5	91.1	93.7	93.8
In Percent of Gross Aid Inflows					
Agriculture	19.3	29.8	19.1	13.6	9.2
Non-Agriculture	80.7	70.2	80.9	86.4	90.8
Period Average Growth Rate (in Percent)					
GDP	5.2	5.0	3.2	3.1	4.1
AGDP	4.0	1.9	3.2	3.3	2.8
NAGDP	6.3	7.3	5.7	2.9	4.9

**Source:** Table 3



A look at Table 1.5 and 1.6 suggests that the growth rate is a shadow or a mirror image of the political cycle. When polity is stable, the growth rate averages five percent; when conflict ensues and turns violent, it falls to three percent, and when there is a lull in the conflict, it again goes up to four percent (panel D). As expected, when non-agricultural sectors gain prominence, the overall growth rate swings with the growth rate of this sector. Of the five observations in the table, it is only once the agricultural growth rate exceeds the non-agricultural growth. In HIC, agriculture grows by 3.3 percent and non-agriculture by 2.9 percent. Yet, the 3.1 percent GDP growth rate is the lowest in the series. This is because a higher growth rate in the sector with a 36.7 percent of the aggregate production weight cannot compensate for a lower growth in the sector with a much higher 63.3 percent production weight in the GDP.

Let us now briefly reflect on the composition of the total budget split between agriculture and non-agriculture. A look at panel B of table 1.6 demonstrates that agriculture is being consistently marginalized. During P era, it received over 13 percent of the total budget. It dropped to 10.5 percent in PD, 8.9 percent in LIC, 6.3 percent in HIC and further down to 6.2 percent in PT. Except for PD phase, the same trend is evident with aid composition (panel C). Nevertheless, as a share of the total, the aid share to the agriculture has always remained higher than the government's budget share to the agriculture sector. With the food deficit widening each year, and this spilling over into the deficit in international trade, both the government and donors as well as the private sectors should come forward aggressively in the development of the agriculture sector. To address malnutrition, rural poverty and widening socio-economic inequality too, agriculture deserves much more than what it is getting so far. Or else, neglect of agriculture and rural Nepal will again sow the seed of future conflicts in the country.

As illustrated by Table 1.6 Nepal's debt profile is remarkably healthy. Total debt stock rose from 49.8 percent of GDP in P to 66.6 percent in the PD era. From then on, it is steadily declining as a percent of GDP. It declined to 64.3 percent in LIC, 60.5 percent in HIC and further down to 43.9 percent in the PT. One interesting observation to note here is that in phase P total debt stock exceeded NAGDP by a small margin. It exceeded by a wider margin in the PD. Such margin continued to narrow down in LIC and HIC. In the PT phase, total debt stock amounted to only two-third of NAGDP. Of the total debt stock, external debt has always remained below NAGDP. Of the total debt stock, external debt comprised 74.4 percent in P, 79.1 percent in PD, and 80.1 percent in LIC. It again dropped to 73.1 percent in HIC and to 67.0 percent in PT. This means debt accumulation grew at a pace lower than the growth rate in GDP. Another factor behind falling external debt ratio is a falling share of loan in the total aid disbursements. Because of political expediency, Nepal for long continued to suffer from an underemployment equilibrium trap. Given the abundance of natural and human resources endowment, Nepal's growth performance has always remained far below its potential. Once Nepal reaches the trajectory of its potential output, it

can absorb a far higher level of debt than today. But even to harness and transform these endowments into output, employment and welfare; the country needs resources in the form of finance, technology, management and market know-how; from ODA, from FDI and from Nepali investors, including the NRN.

To briefly touch upon foreign aid as measured in terms of the GDP, gross foreign aid fell from 7.7 percent of GDP in the P era to 5.9 percent in PD and 5.7 percent in LIC. It drastically fell to 3.7 percent in HIC and slightly exceeded 4 percent in the PT (panel A of 1.6 ). The drop occurred due to a sharpe drop in the loan component, particularly since the HIC period. Of the total ODA, loan comprised 70.2 percent in P, 71.2 percent in PD, and 70.2 percent in LIC. It sharply dropped to 40.5 percent in HIC and further down to 26.8 percent in the PT. It is good that grant has overtaken loans as it mitigates future contingent liabilities, that too in foreign exchange. But, what counts most is the quality rather than the size of the grant. What one must look into is: has it contributed to increase output, employment and exports? Has grant contributed to lower down socio-economic inequalities (seeds of conflict) across region, gender, class, caste and ethnicity? One should also look into whether or not foreign aid, grants in particular, helped to forge strong social bond and social stability.

## **Conclusion and Recommendations:**

This paper was intended to evaluate the behavior of foreign aid over five distinct political phases of Nepal. It covered a period of 24 years: from fiscal year 1986/87 until 2009/10. The attempt was made to evaluate the aid behavior in terms of fiscal and BOP support and also with respect to its size and role in the national economy, through GDP. During this period, Nepal passed through two events of far reaching political consequences. One can call them paradigm shift in Nepal's political development. The first was the overthrow of the Panchayat system, a *sin qua non* for absolute monarchy, in 1990. And the other was the overthrow of the monarchy itself and ushering in the republican era in 2006. In between, Nepal suffered over a decade long violent armed conflict.

As almost all of Nepal's donors, whether bilateral or multilateral, subscribe to western values and philosophy of freedom of speech and the press, periodic election, respect for opposition, independence of the judiciary and free market; after restoration of democracy, a larger section of the population expected a quantum leap in the volume of foreign aid and a meaningful and sustainable improvements in the quality of their life and livings.

Over the years, revenue, supported by domestic borrowings, gained prominence in financing total budget. As a share of the total budget, the size of domestic resources increased from 61 percent in P to 78 percent today, whereas the share of foreign aid fell from one-third to 13 percent. Nevertheless, foreign aid still remains a major source of financing, much needed developmental spending. Had the conflict not swelled the size of

regular spending once and forever, the revenue surplus would have dwarfed foreign aid in supporting development expenditures. However, Nepal should thank its donors for elevating the size of grants *vis a vis* loans, particularly since the HIC years. There is also a strong ground for displeasure as the donors failed to compensate for the conflict-induced fall in revenue surplus.

Another aspect of aid is the BOP support. Here too, the role of foreign aid has fallen from very significant level to least important level over time. Foreign aid's share in annual foreign exchange earnings has fallen from half during P era to consistently down to 13 percent in the current transitional phase. It was solely due to resurgent remittance inflow that pushed down the relative contribution of exports and aid towards the bottom. But the remittance euphoria is causing policy complacency, which may put the economy to the fate of the Dutch disease. An emerging worry for Nepal's economic managers is a consistent under-performance of exports *vis-à-vis* imports in the recent years. Nonetheless, as of today, Nepal's external position remains very healthy whether viewed from the size of total foreign exchange earnings or from the viewpoint of debt servicing burden.

From the viewpoint of national economy, the Nepali economy has undergone a significant structural shift. The output share of agriculture, which was nearly half in P has gone down to 34.2 percent in PT. This means an average rate of decline of over 0.6 percentage points every year. The rapid drop occurred during the time of intense political shocks of far greater magnitude: from P to PD and from LIC to HIC. Nepal's debt profile, whether external or domestic, remains very healthy which leaves enormous scope for further debt absorption capacity.

Both the government and donors, the government more so, has completely ignored agriculture since the restoration of the multiparty democracy. This could be cited as one of the factors behind the eruption of violent conflict in the late 1990s that lasted until the first sixth year of the new millennium. Nepal is still recovering from the trauma of the conflict. Finally, the conflict had tellingly adverse effect on the growth rate. It is because the conflict contributed to shift in the deployment of resources, away from the infrastructures such as irrigation, roads, bridges, airports, drinking water to police, armed forces and the armaments.

On recommendations, there is a need for serious introspection on domestic factors that impede the absorption and deployment of committed aid resources. Why the cabinet, ministers, and civil service scramble for allocation from the domestic resources, while committed external resources remain unutilized and no request even being made for reimbursement from the donors? Donors also need to see how can they simplify and expedite the release of committed resources. There is a pressing and an urgent need to understand normatively what should come first: awareness? empowerment? protest? or decent employment?, increased productivity? output, export promotion, and import substitution? social harmony and stability?

Beginning from the new millennium, remittance has pervasive influence on the economy and the society. Remittance alone exceeds all other

sources of foreign exchange earnings combined together. It contributed to consumption, imports, and real estate boom. One need to carefully evaluate the trade-offs that remittance is causing to the national economy. On the one hand remittances helped find employment for Nepali youth and gave Nepal's BoP a boost, stability of the exchange rate, and expectations on inflation. It also contributed to the cessation of conflict. On the other hand, it pushed up Nepal's consumption in comparison to GDP from 88.3 percent in 2001 to 92.6 percent in 2010. During the same period Nepal's imports increased from 33.2 percent of GDP to 37.4 percent in 2010. Thus, it is clear that a significantly larger proportion of remittances fed into consumption through ballooning imports. Any shock in a source country for remittance whether the form of disaster, a prolonged riot, or a sustained fall in oil prices will have a huge impact on Nepal's economy, politics and society. In the same context, all out fiscal, monetary and all other efforts should be made by all to encourage exports to its rightful place in the national economy.

Finally, for an inclusive, labor-intensive, and sustainable growth that can pre-empt conflict; agriculture deserves much elevated infusion of investment and modern technology.

# 2

## **Nepalese Economy:** Obsolescence, Underpinning and Approaches to Sustainable Development

-Madan Kumar Dahal

**NEPALESE ECONOMY**, largely a subsistence as well as high-cost economy with no direct access to sea for expanding international trade, and limited transit facilities, rising interest rate on lending, high tax burden, and costly doing business, is passing through a downswing phase circumscribed by poverty and stagnation. The economy is strangled by sluggish economic growth rate, poor governance and rampant corruption, where a majority of the people lives in abject poverty struggling for their survival. The international comparison illustrates that Nepal's economy is conspicuously trailing behind other member countries in the SAARC region. Prolonged transition engulfed by growing risks and uncertainties with increasing inefficiency, corruption and political entrenchment jeopardized the entire prospects for economic development. In addition, the respective governments in the past and to-day are terribly engaged in managing the crisis with little emphasis and priority over resolving crucial economic issues. Investment is not a constraint to growth of Nepal, but lack of visionary and determined leadership with strong political commitment to fulfill aspirations of the common people is detrimental to economic progress and prosperity in Nepal. The vision or mission of Nepalese economy should be to build a strong economic nation-state through active participation of the people ensuring a high quality of life to each individual and household within the given timeframe. The primary objectives of Nepalese economy should be



to increase the magnitude of GNI from a diminutive US\$ 13 billion (as of 2009) to US\$ 100 billion and transform the economy from extremely low GNI per capita (US\$ 440) to a higher GNI per capita (US\$ 3,000) at par with middle income countries by achieving a high, sustainable, broad, and inclusive economic growth and eliminating absolute poverty by 2025 and, ultimately, make Nepal the “Switzerland” of Asia. Despite numerous structural constraints, there are ample opportunities for Nepal to gear up the economy by stimulating its major foundations comprising hydropower, tourism, biodiversity and remittances through foreign employment in cooperation with the private sector.

## Introduction

Nepal is a tiny landlocked Himalayan country with a size of 147,181 square kilometers ranging from 70 to 8,848 meters altitude (Mt. Everest) surrounded by rapidly expanding two neighborhood economies viz., India in the East, West, and South and China in the North. Nepal’s geo-physical setting and time-zone location assume strategic significance in South Asia (Dahal, 2004). Nepal’s territory runs all along 885 kms from east to west having non-uniform, mean width of 193 kms north to south at the latitude of 26°22’ N to 30°27’ N and longitude 80°4’ E to 88°12’ E. The country encompasses three ecological regions: mountain, hills and terai (plain) blessed with tremendous bounty of nature. Nepal is rich in biodiversity comprising ecosystem, species, and a broad variety of topography experiencing tropical, mesothermal, microthermal, tiga and tundra climates, which provide 60-80 percent of rainfall during the monsoon season from July to September (Dahal and Inoue, 1994).

The nation possesses 2.3 percent of the world’s hydro resources attributable to four principal river systems, the life-line of Nepalese economy viz., Koshi (east), Gandaki (central), Karnali (Far-west) and Mahakali (Far-west). The theoretical hydropower potential is estimated to be 83,000 MW, and per capita hydropower capacity is assumed to be second highest next to Brazil. Nepal, the Shangri-La of the World, is bestowed with gorgeous mountains, magnificent panorama of flora and fountains, beautiful lakes, valleys and basins, medicinal herbs, precious stones, and sub-tropical forest. Nepal possesses magnificent biodiversity especially the forest resources, which are of great value from the point of economic development.

Nepal is the most popular tourist hub and a global destination for tourists from all over the world. There exists a vast potential for heritage tourism, white-water tourism, eco-friendly tourism, health tourism, mountain tourism, safari and adventure tourism. In addition, Lumbini- the birth place of Lord Buddha, rich cultural heritage, *pagoda* and *stupa* style art and architecture, gateway to Tibet and Bhutan, and pleasant climate in most parts of the country are basic and prominent characteristics of tourism instrumental to attract a large number of tourists in Nepal. Preliminary geological surveys reveal that subterranean resources such as iron, copper, mica, gold, lead and zinc, limestone, slate, mineral oil and gas, coal nickel, sulphur, graphite,

dolomite are available in the country. However, the extent and commercial potential of these mineral deposits are not yet known. With total assets of 26.7 million population, 6,000 rivers and rivulets, 5,000 species of vascular plants, 175 species of mammals, and 850 species of birds, Nepal's territory is double the size of Sri Lanka, 3.5 times greater than Switzerland, 6.7 times bigger than Israel, 23 times smaller than India, and 68 times less than the size of China (Dahal and Inoue, 1994). The striking features of Nepalese economy reveal that agriculture productivity and rainfall steadily increases from west to east, poverty is more acute and widespread from south to north, and migration tends to be skewed from north to south.

Agriculture is the biggest but subsistence sector with built-in dependency syndrome, where still more than 70 percent of the total population derives their livelihood directly from agriculture encapsulated by staggering magnitude of disguised unemployment, mounting rural indebtedness and a high incidence of poverty with 74 percent of the households possessing less than one hectare of land (CBS, 2008). The contribution of manufacturing sector is compressed to less than 6 percent of GDP in recent years attributing to prolonged transition, poor industrial relations and lack of investment-friendly environment. Although population below national poverty line declined from 30.9 percent in 2007 (WDR, 2011) to 25.4 percent by the end of 2010 (TYIDP, 2010-12), the Oxford University/UNDP Research Team employing Multidimensional Poverty Index (MPI) revealed that population below absolute poverty line is as high as 65 percent of the total population in Nepal (OPHI & HDR, 2010).

The poor and ultra-poor have extremely limited access to economy for leading towards a dignified economic life (Dahal-a., 2009). In recent years, the prices of consumption goods, intermediate articles and luxury items including urban land increased manifold attributing to both demand-pull and cost-push inflation. Nepal's economic development is, therefore, extremely challenging and sometimes it is tantamount to intractable journey through silk-road (Dahal, 2010).

The international comparison as of 2009 illustrates that Nepal's economy is conspicuously trailing behind other member countries in the SAARC Region and China with respect to selective macroeconomic indicators such as GNI (US\$ 13 billion), GNI per capita (US\$ 440), economic growth rate, population below national poverty line, external debt and FDI net inflow (table 2.1).

**Table 2.1 : An International Comparison, As of 2009**

S. N.	Country	Population (in million)	GNI (in US\$ billion)	GNI per capita (US\$)	Econ. Growth Rate (In %)*	Popn. Below national poverty line %	External Debt (US \$ billion)	FDI net inflow (US \$ million)
1.	Nepal	29.0	13.0	440	4.5	**31.0	3.7	38.0
2.	Bangladesh	162.0	95.0	590	6.3	40.0	23.6	674.0
3.	Pakistan	170.0	173.0	1,020	2.8	32.6	49.3	2,387.0
3.	India	1,155.0	1,369.0	1,180	8.2	28.6	230.6	34,577.0
5.	Sri Lanka	20.0	40.0	1,990	6.9	22.7	15.1	404.0
6.	China	1,331.0	4,778.0	3,590	9.6	***15.9	378.2	78,193.0

**Source:** World Development Report, 2011; and IMF: World Economic Outlook, April 2011; \* Estimated Economic Growth Rates for 2011, which is 8% for Afghanistan, 6.5% for Bhutan and 6% for Maldives. Nepal's actual growth rate is 3.5% for FY 2010/11; \*\*According to UNDP/Oxford Research Team (2010) population below absolute poverty line is estimated to be as high as 65% in Nepal; \*\*\* Population below \$1.25 a day.

For example, GNI of Sri Lanka (US\$ 40 billion), Bangladesh (US\$ 95 billion), Pakistan (US\$ 173 billion), India (US\$ 1,369 billion), and China (US\$ 4,778 billion) is estimated to be fairly higher when compared with Nepal. Similarly, GNI per capita of Bangladesh (US\$ 590), Pakistan (US\$ 1,020), India (US\$ 1,180), Sri Lanka (US\$ 1,990) and China (US\$ 3,590) have distinctly remained higher the GNI per capita of Nepal. As of 2009 the share of agriculture, industry and services sectors in Nepal is estimated to be 34 percent, 16 percent and 50 percent of GDP respectively (WDR, 2011).

## Current Economic Situation

In recent times, Nepal's economic growth rate is inordinately low confined to 3.5 percent against the target of 5.5 percent as envisaged in the 3-Year Interim Development Plan (TYIDP), 2010-2012 (appendix 2) and 4.5 percent estimated in the budget for FY 2010/11 (Budget Speech, 2010). Despite poor economic performance in the past, growth rate is estimated to remain at 5 percent in 2011 (Budget Speech, FY 2011/12). The year on year (y-o-y) inflation is hovering around 9.6 percent against the target of 7 percent specified in the Monetary Policy formulated by Nepal Rastra Bank (NRB) for FY 2010/2011 and that was revised to 9 percent during the mid-term evaluation (NRB, July 2011). The recent macroeconomic indicators exhibit that Nepal's merchandise exports to India and overseas have declined resulting in a huge trade deficit amounting to Rs. 330.34 billion, which is estimated to be 25 percent of GDP and surpassed the size of budget for FY 2010/11. During the period magnitude of merchandise imports marginally swelled-up compared to last year against a diminutive exports attributing to

rapidly diminishing comparative and competitive edges previously enjoyed by Nepal over exportable items such as carpet, garment, handicrafts, *pashmina*, and herbal products at regional and global markets.

As of recent statistics, share of exports in total trade structure is found to be 14 percent, while imports constitute 86 percent. The share of trade with India alone is as high as 67 percent and the extent of trade deficit with India is alarmingly widening. This is evident of increasing dependency with India and other partners of development in the world. The economy witnessed, for the first time after many years, a negative balance of payments situation until the last ten months of FY 2010/11 and that marginally increased to a surplus of Rs. 2.93 billion at the end against the target of Rs. 9 billion in FY 2010/11. The magnitude of gross foreign exchange reserves downsized at Rs. 270 billion in mid-June 2011 as compared to Rs. 271.7 billion in mid-June 2009, which is sufficient to sustain imports of merchandise goods and services only for about 7.3 months (NRB, FY 2010/2011).

The growth rate of remittances sharply declined from 51 percent in FY 2008/09 to 10.1 percent during FY 2010/11. Although it is extremely difficult to be specific about the size of foreign employment and remittances in Nepal, inflow of remittances according to official statistics marked Rs. 259.93 billion during FY 2010/11, which is estimated to be 23 percent of GDP (appendix 1). The crude and conservative estimation suggests that size of foreign employment surpassed two million, spread over several leading destinations comprising Malaysia (33%), Gulf Countries (62.5%), and South Korea, Hong Kong and other countries (4.5%) as of August 2010/11 (Dept. of Foreign Employment, 2011). In addition, it is assumed that approximately one million workers are employed particularly in blue color job in India.

The number of industries permitted for foreign investment till FY 2009/10 went up to 1,898 with a total project cost of Rs. 143 billion and a total fixed cost equal to Rs. 1,120 billion. The size of Foreign Direct Investment (FDI) stagnated at Rs. 58 billion by mid-March 2010 generating employment for 144,513 Nepalese citizens. The contribution of foreign exchange earnings from tourism sector remarkably declined from 4.1 percent in 1994/95 to 2.4 percent of GDP during FY 2010/11 (Economic Survey, Vol. 2, July 2011). In this context, on July 16, 2011 Asia-Pacific Exchange and Cooperation Foundation (APECF) announced its ambitious plan to raise US\$ 3 billion to develop *Lumbini* as an international pilgrimage Center for Buddhists from all over the world (APECF, 2011).

Although revenues are buoyant and revenue/GDP the ratio is estimated to be 15.3 percent (appendix 1) with growing fiscal and budget deficits, efforts towards internal revenue mobilization are inadequate to effectively supplement requirements for additional capital expenditures. The structure of taxation is massively dominated by indirect taxes (Dahal, 2009) comprising VAT, Customs Duties and Excise Duties and its contribution is as high as 63 percent of total revenue, while the share of direct taxes especially income tax leveled at 20 percent and the contribution of non-tax revenues marked 17 percent in FY 2010/11. Employing per capita income criterion tax burden

is relatively higher in Nepal as compared to other member countries in the SAARC region.

Nepal's tax system lacks simplicity, transparency and competitiveness, which is detrimental to attract FDI and mobilize indigenous investments. Since elasticity of taxation is found to be below the unity (0.9), there is tremendous scope for tax reforms in Nepal (Dahal, 2009) especially to design a competitive tax structure through setting-up of Central Revenue Board, a semi-autonomous body at Ministry of Finance, Government of Nepal (MOF, 2009). The following table provides a comparative scenario of tax structure in selected countries with respect to GNI per capita, tax effort ratio, income tax rate, corporate tax rate and VAT rate (table 2.1):

**Table 2.2 : GNI Per Capita, Tax Effort Ratio, Income Tax Rate, Corporate Tax Rate, and VAT Rate, As of 2008**

Countries	GNI Per Capita US\$	Tax Effort Ratio	Income Tax Rate%	Corporate Tax Rate%	VAT Rate%
Nepal	400	10.9	20	20-30	13
Bangladesh	520	8.5	25	27.5	15
Pakistan	980	10.6	20	35	16
India	1,070	17.7	31	34	12.5
China	2,940	17	20	20	10
Saudi Arab	15,500	5.3	2.5	20	0
Singapore	34,760	13	20	17	7

*Source: Wikipedia March 2010; World Development Report 2010; Website: <http://www.taxrates.cc>*

In recent years, size of the national budget rapidly swelled-up due to increase in unplanned expenditures with penetration of a large number of politically motivated small and big projects. The budget for current FY 2011/12 is estimated to be Rs. 385 billion with huge fiscal and budget deficits to be conventionally off-set by growing internal (Rs. 37.4 billion) as well as external borrowings (Rs. 29.6 billion). Unfortunately, the ratio of capital expenditure to total budget is conspicuously low in comparison to recurrent expenditures, and this is estimated to be 38.6 percent in FY 2011/12 (Budget Speech, FY 2011/12). The major problem associated with the implementation of capital expenditure is as need under-spending, which is primarily attributed to prolonged transition engulfed by fragile political situations with growing crisis of confidence, lack of enduring peace and stability and poor investment-friendly environment. These are major factors to spur economic growth in Nepal and also indicative of poor economic strength that marginalized the prospects for economic development. The quantum of total outstanding debt estimated to be 32 percent of GDP leveled at staggering size of Rs. 430.6 billion (appendix 1) with addition of

interest free loan (US\$ 43 million) provided by IMF under rapid credit facility especially to help improve and correct balance of payments disequilibrium in Nepal (IMF, 2010). Of the total loan, foreign debt constitutes 63 percent, while internal borrowing is comprised of 37 percent as of FY 2010/11.

Nepalese economy suffers from acute shortage of Indian currency due to rapidly growing negative balance of trade with India. Altogether 67 percent of all types of goods comprising consumption, intermediate and luxury goods are imported from India. In recent times, consequently, Nepal Rastra Bank (NRB/Central Bank of Nepal) sold US\$ 2.46 billion to Reserve Bank of India (RBI) for meeting requirements of Indian currency in Nepal equal to Rs. 178.1 billion during 11 months of FY 2010/11 and thereby reducing widening trade deficit with India (NRB, July 2011). Moreover, exchange rate of Nepalese currency (IC Rs. 1 = NRs. 1.60) is fixed with Indian currency pegged with US dollar for a long period and also Nepalese currency is not convertible to Indian currency. This is further manifestation of Nepal's increasing dependency particular on India, which must be improved through expediting exports to India that calls for reviewing existing Nepal-India Trade Treaty.

During the same period commercial banks suffered frequently from liquidity crunch relatively for a long span due to increasing credit-deposit (C/D) ratio as high as 90 percent, declining Statutory Liquidity Ratio (SLR), withdrawal of money from bank deposits to invest in stock market and purchase gold and ornaments, increasing flow of remittances through *hundi* and capital flight, sudden rise in the government cash balances, holding of cash in informal sector, low interest on deposits and growing size of NPA. Although NRB made a series of interventions by providing Rs. 75 billion short term loans under repo and reverse repo auctions and also extending refinancing facilities to development banks and finance companies as a lender of the last resort, commercial banks further pressed to NRB for additional liquidity to mitigate the existing problem facing financial institutions. However, deposit mobilization at commercial banks leveled at Rs. 656 billion as of June 2011 and loans and advances increased to Rs. 574.6 billion during the same period (NRB, July 2011). A majority of commercial banks failed to balance investment portfolio management resulting in excessive concentration of loan to real-estate sector and share margin lending as high as 60 percent.

NEPSE Index rapidly declined from around 814 in mid-February 2008 to a minimum 297.6 in mid-June 2011 (Nepal Stock Exchange, June 2011). In recent years, IMF has been apprehensive of growing number of commercial banks (31), development banks (87), finance companies (80), cooperatives (22,646) and micro-credit institutions, NGOs with limited banking facilities (45), and postal saving units (117) (Economic Survey, July 2011) and strongly recommended to review quantity as well as quality of services provided by financial institutions in Nepal. Prolonged liquidity crisis is a threat to smooth functioning of economy, which is entirely attributed to lack of financial discipline and effective corporate governance in financial institutions

accompanied by poor supervision of NRB. Under these circumstances, risks and uncertainties in financial organizations have greatly increased adversely affecting the confidence of people in the banking system.

The ugly and unhealthy competition among the banks to maximize profit hastily, non-existence of credit rating agencies and lack of corporate governance with *malafied* intention and mal-practices of the Management and the Board to approve loans against vulnerable projects, over-valuation of collateral by the valuers, and extremely weak and poor supervision and governance of NRB are major factors responsible for breakdown of financial institutions in Nepal. However, NRB has initiated tremendous efforts to resolve liquidity crisis interwoven with financial discrepancies through various monetary measures including the proposals for merger and insurance of deposits amounting to Rs. 200,000.

In recent times, mushrooming grow of cooperatives the State is a more sensitive issue that they do not fall under the jurisdiction of NRB but governed by Department of Cooperatives, Government of Nepal. The cooperatives, mostly confined to urban areas, have been successful as in mobilizing a large sum of deposits by providing higher interest rates but without being tied-up with production and multi-purpose activities like *Amul Dairy* and *Lizzat Papad* in India. In recent times, therefore, credibility of financial institutions including cooperatives is on test, for their performance is unpredictable with poor corporate governance leading to increasing risks and uncertainties.

The economic meltdown in the US and other industrialized economies during 2008-10 occurred due to fraudulent relationship among investors, financial institutions and credit rating agencies that completely overlooked the significance of maintaining a minimum level of ethics, morality, and honesty in business deal and banking transactions (Dahal, 2009). Recent debt ceiling crisis in the US is also aftermath of overspending in excess of available resources and fiscal indiscipline resulting into raising a historic size of debt ceiling as high as US\$ 1.5 trillion <http://www.fxtrade.onada.com>.

## **Risks, Uncertainties and Assumptions**

Nepal is passing through the transition engulfed by increasing inefficiency, corruption and political entrenchment that jeopardized the various prospects of economic development. In addition, the respective governments in the past and to-day are terribly engaged in managing the crisis with little emphasis and priority over to resolving crucial economic issues. Although Nepal is situated at strategically important location and time zone in Asia, geophysical limitation and landlocked situations have greatly increased transportation costs leading to high-cost economy and adversely affected its competitiveness to expand and strengthen international trade and make the economy one of the fabulous shopping centers in the world (Dahal et al., 2008). With rugged topography Nepal is disadvantageously placed for international trade and this is the greatest stumbling block leading towards high-cost economy.

Not only Nepal's trade deficit with India is growing alarmingly but also



balance of payments situation is found to be unprecedentedly negative during last ten months of FY 2010/11. The existing Nepal-India Trade Treaty is not in favor of increasing exports to India due to imposition of unfavorable conditions, which include value added provision for local raw materials and labor, quantitative restrictions and sensitive and negative list. This requires moving towards "zero tariff regime" separately with India and China to promote Nepal's exports to neighboring markets with a population of 2.5 billion. Although this arrangement would lead to a loss of revenue equivalent to approximately Rs. 25 billion from customs duties at the initial stage, reserve of Indian currency would tremendously increase through export promotion and remittances, which would be instrumental to appreciate Nepali currency and determine the exchange rate at par with India currency in the long run.

This is a challenging proposition and, therefore, it is necessary to magnificently strengthen Nepal's economy through improving competitiveness in viable areas of economy to make a quantum leap forward in the economic front. The grim reality is that Nepal's economic development would remain awkward and backhanded unless exchange rate between Nepal and India is determined at par through employing prudent economic policies to improve terms of trade with India in favor of Nepal. The average household economy of hills and mountains is relatively poor and extremely fragile in comparison to the households in *terai* with better productivity, infrastructure, industrial-base and easy access to India. Therefore, the issue of improving subsistence economy of hills and mountains is also a crucial agenda to deal with the problem of regional development and inclusive growth that requires immediate attention of the State.

The report published by ADB emphatically illustrates that "investment is not a constraint to growth in Nepal, but lack of visionary and determined leadership with strong political commitment to fulfill aspirations of the common people" is detrimental to economic progress and prosperity in Nepal" (ADB, 2009). Although investment/GDP ratio is as high as 30 percent (Economic Survey, July 2011), economic growth rate evidently remained dormant. Nepal, in recent times, increasingly lost her comparative advantage and competitive edges for variety of reasons over specific and conventional exportable products noted above at the regional and international markets, and new high value crops suitable for viable exports have not yet been fully identified except in the case of *Yarshagumba*.

The issue of modernization and commercialization of agriculture with implementation of scientific land reforms program to increase production and productivity of food and cash crops have remained outside the jurisdiction of national priority. Although government emphasized on the commercialization of agriculture, major political parties do not favor large or estate farming but fragmentation of holdings by lowering down prevailing level of land ceiling through implementation of what they call it scientific land reforms program. Under these circumstances, it would be virtually impossible to attain the objective of Green Revolution through mechanization of agriculture in small holdings. The existing dual ownership of land has



conspicuously discouraged investment in land for its improvement from either side - absentee landlord and tenants. The investment of both the government and private sector is minimal against what is urgently required to sustain agriculture development.

In addition, a variety of subsidies have been provided to purchase chemical and organic fertilizer and seeds of high yielding varieties in order to boost production and productivity of agriculture sector. The government has the provision for 50 percent subsidy on the capital expenditure to the small farmer cooperative institutions in the purchase of machinery and equipment for processing cardamom, tea, coffee, ginger, nut and honey. Subsidies are given to farmers on electricity tariff and credit to the cooperatives and private sector. Subsidies will also be provided to establish laboratory, pesticide, seed production and packing, which are also crucial to enhance competitiveness of farmers and compete with Indian products (Budget Speech, 2011). Therefore, subsidy is sensitive as well as vital instrument to increase production and productivity of agriculture and improve efficiency and competitiveness of farmers. Thus, the issue of taxing agriculture sector requires not only greatly moving towards modernization and commercialization through promoting agro-enterprise and agri-business but also developing national consensus among major political parties to decide what kind of land reforms system would be appropriate for agriculture development in Nepal.

The productivity index especially of food crops evidently remained constant for over a long period (Economic Survey, July 2011) and consequently, Nepal imported 25,000 MT rice from India for meeting urgent requirements of the people living in food deficit areas especially western hills and mountains during FY 2009/10. The productivity index of manufacturing goods increased at snail's pace. Also there is apprehension that inflow of FDI as well as indigenous investments are often disrupted primarily due to extremely inadequate infrastructure with unprecedented long hours of load-shedding, poor industrial relations with rigid labor laws and tax regulations, frequent *bandh* and strikes, and scarce resources to funding mega-projects resulting in poor contribution of manufacturing sector confined to less than 6 percent of GDP. Most of the industries are running far below the capacity, and many units operating in industrial corridors especially in *terai* remained virtually closed for more than 200 days in a year. Although overall impacts of global economic meltdown on Nepalese economy have been moderately less severe in recent times, lack of peace and political stability jeopardized the possibility for developing physical infrastructure especially road and hydropower, tourism, biodiversity, and promoting foreign employment and remittances in Nepal.

Nepal's inability to match growing demand for semi-skilled manpower in the international labor market due to poor quality of human resources has created adverse impact on foreign employment and remittances. Every year, around 400,000 labor force is added in the labor market of Nepal and of which, 300,000 are absorbed in the international labor market, and there is still scarcity of job for remaining 100,000 labor forces at home. In compatible

with the spirit of market economy and liberalization it is not the liability of the government but private sector to play the lead role for creating employment opportunities at home by setting-up of small and cottage and medium scale industries. Employment opportunities could also be created by attracting FDI on a greater quantum in large-scale joint ventures and industries on priority areas such as hydropower, tourism, biodiversity and manufacturing sectors in cooperation with neighboring economies, industrialized countries and other partners of development.

Private sector is the prime vehicle for economic development and government should play the role of a facilitator. In Nepal, unfortunately, both the government and private sector are extremely vulnerable in terms of their capacity and governance required for effectively providing services to the people and thereby accelerating the pace of economic development. There is, therefore, need to simultaneously improve efficiency and governance of both the government and private sector with increasing transparency and accountability by mobilizing technical and financial assistance provided by WTO and other multilateral financial institutions to Least Developed Countries (LDCs).

Despite induction of market economy, liberalization and privatization especially after 1990, Government of Nepal adhered resiliently to the policy of sustaining a large number of State Owned Enterprises (SOEs) enjoying monopoly (for example, Nepal Oil Corporation, Nepal Airlines, National Trading Ltd., and Nepal Electricity Authority popularly known as white elephants), which are entrapped into huge losses with extreme inefficiency, rampant corruption, over-manning and political interference. With prevailing horrible situations in public enterprises in recent years, the government has transferred more than Rs. 80 billion to public enterprises waiting for privatization for a long time, which is extremely slow for unknown reason. This immediately demands for designing a pragmatic policy to decide the fate of SOEs either by stimulating the process of privatization on fast-track or, alternatively, moving towards company limited, joint venture with foreign companies, public-private-partnership (PPP) and, finally, dissolution through liquidation.

The Office of Auditor General in its annual report categorically referred to increasing volume of irregularities as high as Rs. 162 billion till FY 2010/11, which is evident of gross violation of fiscal discipline in government offices (OAD/Nepal, 2010). The latest report published by Transparency International (TI) shows that Nepal falls within the group of most corrupt countries in the South Asia region while ranking for 180 countries (Transparency International, 2011). The Failed States Index 2011 exhibits that Nepal occupies 27th position in the list of 177 countries and the business climate is also not congenial to promote business activities in Nepal (Doing Business Report 2011). This is the manifestation of economic backwardness with notorious examples of inefficiency and corruption.

The "Foreign Investment and Technology Transfer Act 1992" (FITTA, 1992) has been considered a powerful instrument to attract FDI in Nepal

and, therefore, it is imperative to review in conformity with the principles of WTO, SAFTA and BIMST-EC. There is also a need to expedite agro-based and manufacturing exports, FDI and remittances with effective induction of economic diplomacy through Nepal's diplomatic missions abroad (IFA, 2009). Tourism development and foreign employment are conditioned to stiff competition at regional and global markets that require improving efficiency to increase competitiveness in both sectors. Although Nepal is rich in biodiversity especially medicinal herbs like *yarshagumba* and many other life saving drugs, flagship and ownership over a single *Aurvedic* and herbal product under TRIPS have not been established so far. Nepal's thrust for maximizing benefits from WTO, SAFTA and BIMST-EC through promoting regional and international trade have been disrupted by prolonged transition and poor governance.

The future of *Mahakali (Tanakpur-Pancheswar Multipurpose Project)* Treaty held in 1995 between Nepal and India with a view to generate 6,000 MW of electricity is yet mysterious. This is most unfortunate example of India's indifferent attitude towards Nepal's economic development that DPR is not at sight even after 15 years of ratification of treaty at mid-night by a two-third majority in the parliament of Nepal. In recent years, despite stereo-type claim and campaign for profound and tested relationship with neighboring countries, no single mega-project is in operation in Nepal in cooperation either with India or China. Both India and China, economically giant neighbors, were premier donor countries to Nepal during 1950s, 1960s and 1970s but their status have been relegated to its lowest ebb in the group of donor communities in recent years with a combined contribution of less than 6 percent of total external assistance (Dahal, 2008). The fault lies in us, not with our neighbors, for political powers failed to capture trickle-down effects and galvanize a maximum cooperation from neighborhood economies from their miraculous economic progress.

At this critical juncture, *Mahakali* Treaty with Nepal is not a priority for India and, therefore, there is also need to reordering of priorities compatible with sustaining higher growth rates with frontal attack on poverty. The total 751 MW electricity including 54.3 MW of thermal and solar production of 100 KW has been generated by the end of FY 2009/10 (Economic Survey, FY 2010/11). However, electricity production is limited to 400 MW during the winter and 572 MW during rainy season (Concept of Government and Future Program, 2010) against the local demand for hydropower estimated to be 972 MW as of 3-Year Interim Development Plan, 2010-2012 (appendix 2). Although government aims at producing 2,500 MW of hydropower to eliminate load shedding by next 4.5 years (Ministry of Energy, 2011), this is most painful that Nepal with highest per capita hydropower potential, next to Brazil, is facing acute shortage of electricity that plunged the entire nation into darkness and the process of economic development retarded to its lowest level. In addition, not only cost of electricity production is conspicuously higher but also tariff rates are exorbitant as compared to other countries in the SAARC region.

The long term vision of the hydropower sector is to develop hydropower based on optimal utilization of water resources to meet the domestic power demand and export the surplus while expanding the development and services in order to contribute to improving the livelihood of Nepalese people. The Government of Nepal has envisaged a strategy to develop hydropower estimated to be 820 MW (short-term 5 yrs) by the end of 2007. Similarly, the government has the plan to develop hydropower estimated to be 2,230 MW (Medium-term 15 yrs) by 2017 and, subsequently, 22,000 MW (long-term 25 yrs) by 2027. Following attainment of these targets, electricity will be available to 60.0 percent HHs including 1,500 MW for export to India and Bangladesh. Harnessing of water resources and developing hydropower will ensure both sustainable high growth and substantial poverty reduction not only in Nepal but also in South Asia region (Water Resources and Energy Commission, 2001). As envisaged in Water Resources Strategy 2002 and current evaluation of hydro electricity development, programs will be formulated to generate at least 25,000 MW within forthcoming two decades (Economic Survey, 2009). However, India is the only market to export surplus hydropower and this demand for a high-level agreement between Nepal and India to facilitate market for surplus electricity generated through mega-projects initiated by bilateral, regional and multi-lateral funding. Thus, harnessing of water resources and developing hydropower is not only an economic and technical issue but also a serious political concern of utmost significance for both countries (Dahal, 1992).

Prolonged economic downswing is more precarious than political predicament. Galloping recurrent expenditure against small size and under-spending of capital expenditure, rapidly falling exports against alarmingly growing imports, decelerating comparative and competitive edges over viable exportable items to international market, declining growth rate of tourists arrival and remittances, negative balance of payments situation and gradually declining international reserves, frequent liquidity crunch, poor integration of domestic economy with global economy, extremely limited employment opportunities at home, inadequate infrastructure with increasing load-shedding, poor governance, prolonged transition and political instability, absence of elected bodies at local levels, inefficiency, and rampant corruption are major impediments to economic development in Nepal (Dahal-b, 2010).

The major challenges to Nepalese economy are, firstly: (1) How to transfer excessively dependent population from agriculture to more productive non-agriculture sector (manufacturing, services and tertiary) through creating employment opportunities by attracting FDI and promoting indigenous investment in cooperation with private sector and thereby reducing extent of absolute poverty to zero? The process of economic transformation will help increase efficiency and competitiveness of rest of the farmers attached to agriculture and boost-up production as well as productivity. Over the years, productivity index of food crops remained almost constant, while index for cash crops moderately increased during the same period. Secondly:

(2) How to more effectively integrate Nepalese economy through trade and investment especially with neighborhood (India, China) economies, regional (SAFTA; BIMST-EC) as well as global economies and maximize benefits from globalization through promoting exports in which comparative advantages and competitive edges do exist ensuring a high, sustainable, broad-based and inclusive growth rate? and, thirdly: (3) How to mobilize bilateral, regional and international cooperation on a greater quantum especially from neighboring countries, development partners from OECD countries, WTO and multilateral funding agencies (ADB, World Bank, IMF, UNDP etc), and effectively maximize the productivity of foreign aid.

## Approaches to Sustainable Development

The vision or mission of Nepalese economy should be to build a strong economic nation-state through active participation of the people ensuring a high quality of life to each individual and household within given timeframe (Dahal, 2004). The primary objectives of Nepalese economy should be to increase the diminutive magnitude of GNI from approximately US\$ 13 billion as of 2009 to US\$ 100 billion and transform the economy from extremely low GNI per capita (US\$ 440) to a higher GNI per capita (US\$ 3,000) at par with middle income countries by achieving a high, sustainable, broad-based, and inclusive economic growth and eliminating absolute poverty by 2025 (medium scenario) and; ultimately, make Nepal the “Switzerland” of Asia (high scenario), especially by:

- (a) Increasing production and productivity of agriculture particularly high value crops through modernization and commercialization of agriculture (APP, 1995) in conformity with the spirit of Green Revolution, and also enhancing productivity of manufacturing sector through improving industrial relations;
- (b) Penetrating bilateral, regional and international markets through expediting exports of viable products with comparative advantages and competitive edges such as carpet, garment, handicraft, *pashmina* and lintel;
- (c) Maximizing benefits from neighborhood economies through moving into “zero tariff regime” especially with India and China separately and creating a ‘revolving fund’ to initiate mutually beneficial mega-projects, and also expediting similar efforts with Euro Zone, The US, Scandinavian countries (Denmark, Sweden, Norway and Finland) and Asia-Pacific region especially Japan, Australia and New Zealand;
- (d) Attracting considerable degree of FDI in priority sector especially infrastructure (hydropower, road and tourism sector), and the target should be to produce required level of electricity for eliminating load-shedding by 2015 and, subsequently, export surplus electricity to India.
- (e) Mobilizing both FDI and indigenous investments to construct highways connecting north-south, east-west and India border, and the SAARC region;

- (f) Exploring possibility for sea-route for expanding international trade connecting Bay of Bengal, Indian Ocean, and Arabian Sea;
- (g) Creating a hub for international tourism, and preserving biodiversity with commercial viability;
- (h) Promoting decent and safe foreign employment at lucrative destinations by developing quality human resources as per requirements of international labor market and maximizing flow of remittances through official channels;
- (i) Promoting small and medium scale enterprises (SMEs) with private sector investment and developing large scale industries and mega-projects at the initiation of private sector by attracting FDI, which would immensely help create employment opportunities at home; and
- (j) Creating an International Financial Services Center (IFSC) by 2015 and mobilizing investment capital to accelerate development for the whole region (high scenario) (Dahal, 2004).

Nepal is surrounded by rapidly expanding economies competing each other to become global economic power with for which they need huge investment-capital and financial services. A modern International Financial Services Center located at Nepal could meet these requirements of neighboring countries India, China and also SAARC countries, which will help create a unique opportunity for Nepal to prosper in the 21<sup>st</sup> century. “International Financial Services Center (IFSC) will help create employment opportunity at all skill levels, provide revenue to treasury, strengthen information technology, improve status of infrastructure, and increase financial credibility of the nation” (Collins et al., 1996).

### **The strategic objectives should be to:**

- (a) Substantially increasing GNI with double-digit growth rate ensuring a high GNI per capita exceeding US\$ 3,000 (average of middle income economies) per annum within the said timeframe;
- (b) Providing employment to each economically active population;
- (c) Combating inflation by increasing production and productivity of both agriculture and manufacture sectors in the long-run;
- (d) Reducing absolute poverty from 25 percent to zero percent by 2025; and
- (e) Improving efficiency and competitiveness, and governance in all spheres and fighting against rampant corruption.

### **The strategy for economic development should be directed towards:**

- (1) Sustaining exports of carpets, garments, handicrafts, herbal and medicinal products, tea, cardamom and lentils (pulses) to international markets with identification of new products including yarshagumba.
- (2) Reviewing Nepal-India Trade Treaty to expedite exports to India

- and reduce growing extent of trade deficit with India.
- (3) Promoting import substituting industries, in addition to export promoting industries, such as fertilizer, cotton textile, cement and sugar at suitable locations on the basis of comparative advantages and competitive edges;
  - (4) Promoting both indigenous and foreign investment through newly established Investment Promotion Board and establishing industries in Special Economic Zone;
  - (5) Initiating joint ventures with India and China for developing infrastructure - road and hydropower especially mega-projects for not only meeting domestic demand but also exporting surplus electricity to India, China and South Asia region and thereby creating win-win effects to the whole region;
  - (6) Ensuring employment opportunities at home by establishing small and cottage, medium as well as large scale industries at the initiation of private sector through attracting FDI especially from NRR (non-resident Nepalese) and also mobilizing indigenous investment;
  - (7) Developing a master plan for promoting tourism and creating a regional hub and make Nepal a model tourism country of the world within 15 years from now in cooperation with private sector (Budget Speech, FY 2011/12);
  - (8) Increasing investment in infrastructure especially road and electricity at the initiation of private sector through attracting FDI;
  - (9) Increasing investment in soft sector by attracting FDI in joint ventures especially to establish polytechnic institutes and teaching hospital and research centers (Institute for Medical Sciences) at par with international standard;
  - (10) Developing IT sector for meeting international demand for IT experts;
  - (11) Preserving biodiversity for neutralizing adverse impact of global climate change and strengthening efforts towards commercialization of biodiversity;
  - (12) Developing quality human resources for meeting growing demand for middle level manpower at international labor market, and maximizing and effectively utilizing remittances for productive use;
  - (13) Developing national consensus on establishing International Financial Services Center (IFSC) in Nepal;
  - (14) Strengthening capacity of both government and the private sector by improving efficiency and governance;
  - (15) Mobilizing and effectively utilizing external resources, and maximizing productivity of foreign aid;
  - (16) Improving efficiency of Commission for Investigation of Abuse of Authority (CIAA) and preserving independence of judicial authorities such as Special Court, Appellate Court and Supreme



- Court to fight corruption and injustice; and
- (17) Developing national consensus on establishing International Financial Services Center in Nepal.

## Conclusion

In conclusion it is recommended that efforts should be made to gradually reduce the extent of disguised unemployment in informal sector and promote self-employment in both rural and urban areas. A top priority should be to expedite investment in mega-projects especially infrastructure such as road and hydropower not only to create employment opportunities at home but also for achieving double-digit growth with substantial poverty reduction. Since employment is a key to development, it is also necessary to promote safe, decent and lucrative employment at home and abroad by imparting technical and vocational education comprising basic knowledge of English, Mathematics and Computer, which would certainly help increase the flow of remittances. There is also need to modulate education, health and nutrition policies to improve quality of human resources instrumental to compete at international labor market for middle level manpower and maximize the benefits from globalization.

While selecting development projects adequate attention should be provided to Medium Term Expenditure Framework (MTEF), Poverty Reduction Strategy Paper (PRSP), and Millennium Development Goals (MDGs) especially to expedite foreign assistance from donor communities for growth and poverty alleviation. In addition, it is essential to develop infrastructure by attracting FDI in cooperation with private sector such as: (a) High-ways and expressways connecting east-west across mountainous region and north-south across three ecological regions; (b) Railways connecting India across east-west terai; (c) Ropeways with country-wide networking; (d) Construction of international airport at Lumbini, Biratnagar and Pokhara; (e) Building of fast-track tunnel road connecting Kathmandu and Hetauda, and construction of outer ring-road in Kathmandu valley under BOOT arrangement; (f) Operation of electric train in Kathmandu Valley; (g) Construction of railway connecting Khasa, Chinese border and Lumbini via Kathmandu; (h) Construction of cross-border railway links between Nepal and India via major southern customs points; and (i) Production of hydropower equal to 2,500 MW to meet domestic requirements and eliminate load-shedding by 2015, and also for exporting surplus electricity to India in future.

In addition, NRN should be encouraged to develop hydropower, construct star hotels, operate cable cars at important tourist destinations and run trolley bus services in major cities, establish hospitals and educational institutions at international level, and preserve and develop biodiversity especially ecosystem and species for commercial utilization. Economic corridors, export processing zones, and special economic zones should be set-up at various industrial locations, and dry-ports should be constructed to speedily back up



the process of industrial development with recently approved Investment Board under the Chairmanship of Prime Minister.

In the light of proposed restructuring of the state it is also important to empower and strengthen local bodies with emphasis on developing a strong nexus between the center and federal states. The government should, therefore, consider the proposal for restructuring of the federal states on the basis: (a) that number of states should be a maximum of seven including the Kathmandu Valley to be administered separately by the Central Government, and Karnali Pradesh with special status; (b) that federal states must have north-south axis not only for ensuring national unity and integrity but also to promote smooth flow and judicious sharing of resources and maximize benefits and provide equal access to mountain, hill and terai for economic cooperation provided by neighboring countries; and (c) that state must be preferably a economically viable unit so that existing backward and remote hilly areas would have opportunity to strengthen economy in partnership with relatively developed areas.

Despite numerous structural constraints, there are ample opportunities that Nepal could tremendously gear up the economy by stimulating its major foundations comprising hydropower, tourism, biodiversity and remittances through foreign employment in cooperation with private sector. The development strategy for a burgeoning economy like Nepal must be directed towards gradually shifting from aid to trade; from dependence to interdependence; from poor to good governance; from conflict to consensus, and from disgusting to excellent performance supplemented by enduring peace and stability with determined and visionary statesmanship to ensure a secured and safe destiny for thirty-million Nepalese people eagerly awaiting to enjoy optimistically blissful days in not too distant future. Since Nepalese economy is characterized by high-cost and subsistence with alarmingly growing dependency, it is essential to formulate the national budget and periodic plans by propagating the theory of interdependence to accelerate the pace of economic development. Finally, there is also need to develop national consensus on prime economic issues among major political forces, and formulate a long-term perspective plan (a road map) ensuring a double-digit inclusive growth with substantial poverty reduction. A vibrant economy with robust economic growth is antidote to extreme poverty, corruption and underdevelopment for a viable economic nation-state.

## Appendices

### Appendix 1: Macroeconomic Indicators

Description	2006/07	2007/08	2008/09	2009/10	*2010/11
GDP at current prices (Rs. in bln.)	727.83	815.66	988.05	1,171.90	1,346.81
Gross consumption/GDP	90.2	90.2	90.6	92.6	93.3
Gross domestic savings/GDP	9.8	9.8	9.4	7.4	6.7
Gross investment/GDP	28.7	30.3	31.7	35.0	30.2
Export/GDP	8.2	7.3	6.9	5.2	4.9
Import/GDP	26.8	27.2	28.8	32.3	28.9
Consumer price index (% change)	6.4	7.7	13.2	10.3	9.6
Total revenue (% change)	21.3	22.7	33.3	25.4	14.7
Total govt. expenditure (% change)	20.5	20.8	36.1	18.2	17.9
Revenue/GDP**	12.1	13.2	14.5	15.4	15.3
Tax revenue/GDP	9.8	10.4	11.8	13.3	13.1
Total govt. expenditure/GDP	18.4	19.8	22.2	22.2	23.0
Budget deficit/GDP	4.1	4.1	5.0	3.5	3.8
Total outstanding debt (Rs. in bln.)	320.4	366.0	399.8	403.9	430.6
Per capita outstanding debt (Rs.)	12,117	12,331	13,505	14,292	14,905
Total outstanding debt/GDP	44.0	44.9	40.3	34.5	32.0
Total deposit (Rs. in billions)***	N.A.	N.A.	505.7	676.0	795.3
Total lending (Rs. in billions)***	N. A.	N. A.	358.51	495.2	622.6
Total deposit/GDP	46.0	51.7	55.5	52.5	50.8
Total domestic credit/GDP	49.5	53.6	56.1	55.0	55.2
Remittance income (Rs. in billions)	97.69	142.68	209.70	231.73	259.53
Remittance income/GDP	13.8	17.5	21.2	19.8	19.3
Current account balance/GDP	-0.1	2.9	4.2	-2.8	-0.4
Balance of payments (Rs. in billions)	5.90	29.68	41.28	-3.63	-8.0
Foreign exchange reserves (Rs. bln.)	165.13	212.62	286.54	268.91	263.13
Exchange rate US\$****	70:49	65.02	76.88	74.54	72.39

**Source:** Economic Survey, July 2011; \*Estimates based on eight months; \*\* Revenue/GDP ratio includes both tax/GDP and non-tax/GDP ratio; \*\*\* As of mid-July 2008, mid-July 2009 and mid-July 2010; and \*\*\*\* Annual average of buying and selling rates.

## Appendix 2: Quantitative Targets

Indicators	Status as of 2009/10	Target 3-YIDP, 2010/11-2012/13
Annual average economic growth rate (%)	4.4	5.5
Annual average agriculture sector growth rate (%)	3.3	3.9
3. Annual average growth rate of non-agriculture sector (%)	5.1	6.4
Population below poverty line (%)	25.4	21
Average annual employment growth rate (%)	3.0	3.6
Women using health worker for maternity (%)	29	60
Contraceptive prevalent rate (%)	50	56
Total birth rate for 15-49 years of age (%)	2.9	2.6
Maternal mortality rate (per 100,000)	229	170
New born babies mortality rate per 1,000 live births	20	16
Infant mortality rate per 1,000 live births	41	36
Child mortality rate per 1,000 live births	50	40
Population with access to drinking water (%)	80	85
Population with access to sanitation facility (%)	43	60
Net enrolment in primary level (%)	93.7	98
Districts headquarters connected with road (number)	71	75
Telephone including mobile per 100 density	27	55
Electricity generation (installed capacity)	691	972
Population with access to electricity (%)	56.1	65
Land under irrigation (Ha)	1,227,000	1,425,725
Forest covered area (%)	39.6	40
Total length of road (Km)	19,447	20,122

**Source:** Economic Survey, July 2011.

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# 3

## Foreign Assistance -- a Journey that didn't take too far

–Professor Bishwambher Pyakuryal

### **Priorities in Development Plans**

The history of development of Nepal begins with the first five year plan implemented from 1956. To date, a total of 11 plans have been implemented. The first plan (1956-62) was followed by the Second (1962-65), Third (1965-1970), Fourth (1970-1975), Fifth (1975-1980), Sixth (1980-85), Seventh (1985-90), Eighth (1992-1997), Ninth (1997-2002), Tenth Plan in 2002-2007, and Interim Plan (2007-10) covering a period of over five decades.

Compared to the four consecutive Plans (1956-62, 1962-65, 1965-70, 1970-75) that laid emphasis on building basic infrastructure, the Fifth Plan (1975-80) acknowledged people-oriented development and egalitarian distribution built in the production process. The underlying principle in the Fifth Plan was significantly different since its objective was not only to maximize the output but also to make output consistent with the minimum felt needs of the people (NPC, The Fifth Plan, 1975). The basic objective emphasizes mass-oriented production and maximum utilization of labor force. The Sixth Plan (1975-80) spelt more loudly on meeting minimum basic needs of the people by adding new dimension in the planning objectives. Reduction in income inequality, by increasing alternative employment opportunities was therefore the priority of the Sixth Plan. Specific objectives were to increase production at a higher rate by increasing opportunities for productive employment. In view of this, the Seventh plan attempted to narrow down the gulf between planning and implementation. To achieve this goal, it aimed at building up the productive capacity of the economy by

focusing on conserving and expanding the physical resources.

The eighth plan, following popular movement of 1990, was meant to address the aspiration of the people raised during the movement. With inclusion of few popular programs, this plan chiefly focused on sustainable development, poverty reduction and on reducing regional disparities. Despite the fact that Nepal continues to adopt reform programs, it was realized later that the program should be tied up with sectoral priorities. The Ninth Plan was tied up with prospective planning, and accordingly, priority areas were identified. In this plan the area of priorities were agriculture and forestry; water resources; human resource and social development; industrialization, tourism development and international trade; and physical infrastructure. Nevertheless the objective was to alleviate the poverty.

The Tenth Plan came as Nepal's Poverty Reduction Strategy Paper (PRSP) with the main objective of poverty alleviation. The other objectives, closely tied up with poverty alleviation, were to achieve broad-based sustainable economic growth, social sector development, rural infrastructure and targeted programs for targeted people. This plan acknowledged the need for special treatment of marginalized and vulnerable groups of the society as they failed to reap the benefit of urban sector development.

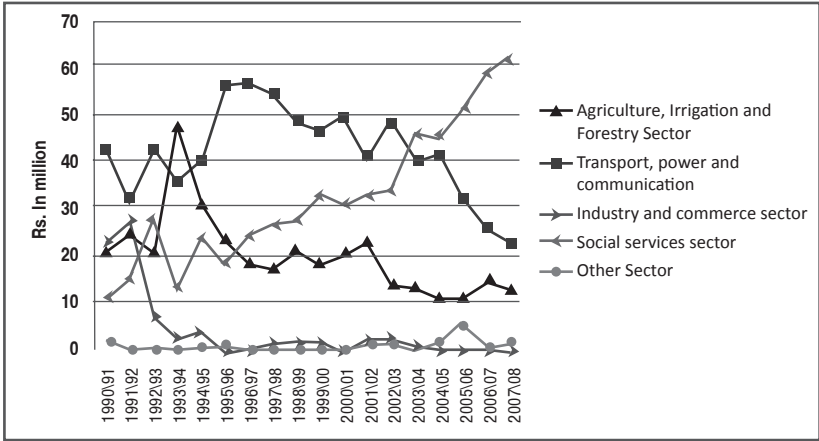
Two consecutive Three year Interim Plans came after the end of a decade-long Maoist insurgency in Nepal. The prime focus of the plan was for relief, reconstruction, rehabilitation, reintegration and revival of the economy. Special focus was placed on inclusive growth to accommodate marginalized groups on developmental activities. Nevertheless, the overall objective was to alleviate poverty through pro-poor broad based economic growth. It also gave emphasis on promoting good governance and effective service delivery, increase in investment in physical infrastructural, social development and inclusive development process.

## **Sectoral Allocation**

As Nepal underwent a shift in its development priorities over the years, so has been the case for areas financed by foreign aid. The areas of finance and priorities both have changed from donors perspective. When Nepal was following socialism fueled by dependency doctrine of newly independent states in world, the priority areas of Nepal was the establishments of public enterprises. Therefore, in early years, Nepal received aid for industrialization along with transport, communication and other physical infrastructure.

The sectoral allocation of foreign aid shows that Nepal has been receiving aid on the areas of agriculture including irrigation and forestry sector; Transport, Power and Communication; Industry and Commerce Sector; Social services sector.

**Figure 1: Sectoral Allocation of Foreign Aid (1990-2007)**



*Source: Calculated from Economic Survey 2003/04 and 2008/09, MoF*

During early 90s, Nepal received sizeable foreign aid in transport, power and communication followed by industry and commerce; and agriculture. A year after Nepal implemented the eighth five year plan in 1992, the agriculture sector received highest share of foreign aid. However, this trend discontinued following years and again, transport, power and communication sector continued to receive highest share of foreign aid flow in Nepal. This shows a divergence between National plan’s priority and actual areas of funding. Nepal continued to receive a larger share, though declining, on transport, power and communication up to FY 2003/04. Trend reveals that social sector has been financed with its increasing share over the year right from early 1990s up till now. After 2003/04, social sector has been receiving a highest share of foreign aid in Nepal. The industry and commerce sector has been receiving a nominal share of foreign aid in recent years.

While Nepal had different policy priorities at different National Plans, there are no one-to-one correspondence between policy priorities and areas with higher investment. This is not only an isolated case of national expenditure on less prioritized areas through domestic source of financing expenditure; rather the same goes with foreign aid. For example, despite major poverty thrust given during the Eighth and Ninth Plan period, the external resource allocation as outlined above does not demonstrate strong linkage between focused priority and resource allocation. The total resource flow during the period of 1990 to 1998 in the basic social services sectors, which includes primary schooling, drinking water and sanitation, primary health, and family planning, has increased on an average annual rate of 11.4 percent.

However, the total volume of aid is found to be inadequate to address the poverty reduction objective. During the same period, an average annual rate of increase in the education sector remained 5.3 percent. In the year



1998, the total disbursement from all external sources to basic social services amounted to US\$ 59.4 million. Similarly, the disbursement in the education sector amounted to US\$ 27.8 million, representing 6 percent of the total disbursement. The education sector suffered a decline of 37.3 percent in 1998 as compared to 1997. Although before 2002 the inflow of aid did not show proper matching with the need and priority of the nation, the situation has improved after that period. The main reason behind that is the implementation of foreign aid policy and tenth plan based on poverty reduction strategy paper. If we take development expenditure as a measuring rod for judging prioritization of the sectors, then estimated development expenditure during the first MTEF period (2002/3-2004/05) is highest for energy sector (23,164 million) followed by agriculture, forestry and fisheries (19268 million) and transport (13189 million). The aid received by Nepal during 1998-2005, as mentioned above, also follows the same order. This is the indication of donor group's consistency with priority of the country (Pyakuryal, Adhikari and Dhakal 2008).

There is no doubt that foreign aid has contributed to the development of Nepal. In his study, (Bhattarai Spring 2009) found that aid is positively related to per capital real GDP in the long run. He also concludes that aid effectiveness increases with the increase in good policy environment in the long run. Therefore, the crucial issue here is not whether foreign aid has contributed to GDP and development of Nepal; rather the issue is whether foreign aid has been effectively used? Has it been able to channelize most productive sectors so that development activities can be accelerated? Is there scope of improving allocative efficiency of foreign aid?

External assistance is not value free. The aid targeted for developmental projects is often alleged to have been directed towards the political and strategic interests. However, if the key objective of ODA is to promote development, it should have a measure to link aid to the priorities of the recipient countries. Therefore, managing foreign assistance has usually been quite poor to access aid to needy countries in general and targeted beneficiaries in the recipient countries in particular.

## **Contribution of Foreign Assistance to Development Goals**

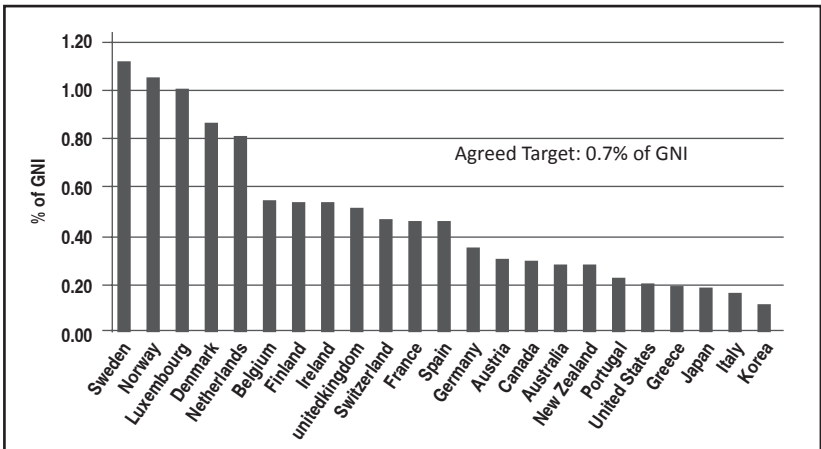
The criticism that aid has actually done more harm than good to development goals of the poor countries is drawing attention of majority of aid practitioners. Professor Easterly (2006) is of the view that foreign aid has not achieved much to achieving development goals. He states, "A tragedy of the world's poor has been that the West spent \$2.3 trillion on foreign aid over the last five decades and still had not managed to get twelve-cent medicines to children to prevent half of malaria deaths. The West spent \$2.3 trillion and still had not managed to get four-dollar bed nets to poor families. The West spent \$2.3 trillion and still had not managed to get three dollars to each new mother to prevent five million deaths". It indicates a tragedy that so much well-meaning compassion did not bring expected results for needy

people. The donors' approach has merely been to delink sizeable amount of assistance with need-based priority.

This section elaborates the reasons for declining the volume of foreign aid; the conditionality imposed by the donors and its implications; and difficulties created by inadequate access of the grant to poor countries. Such elaboration is helpful to find out why foreign aid has not supported development goals of the recipient countries.

The conditional aid loans based on policy reforms provided to Africa and many other countries including Latin America just remained discouraging. Easterly says the evidence is stark: \$568 billion were spent on aid to Africa, and yet the typical African country is no richer today than 40 years ago. The structural adjustment failed linking policy reforms and economic growth (Ibid).

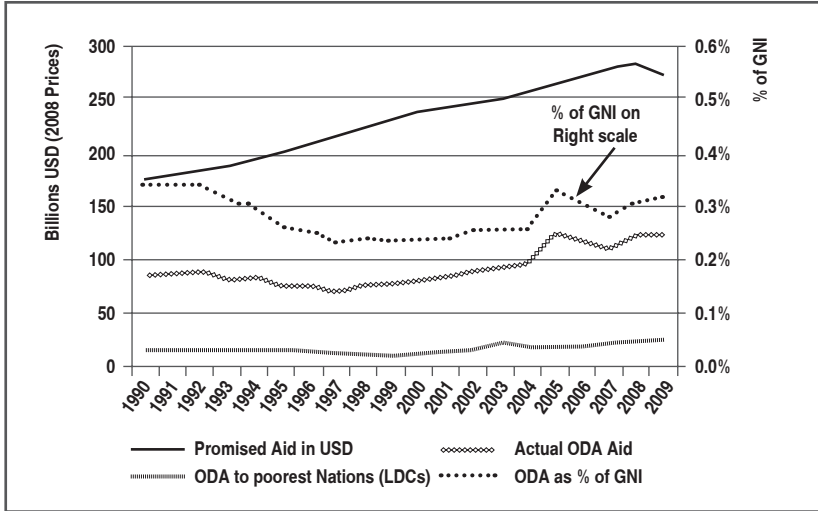
**Figure 2: Net ODA 2009 as percent of GNI**



Source: OECD, April 2010

The rich donors are always behind their commitment to give away 0.7% of their gross national income as official development aid. The OECD reveals, when aid is broken down by regions over time, the poorest countries get less of the foreign aid. For example, of the aid that has been delivered, roughly a quarter seems to have gone to the poorest regions from all Development Assistance Committee (DAC) aid since 1970. The figures show Net ODA in US dollars term is not discouraging. However, net ODA as a percent of GNI is still below the commitments (OECD 2010). The level of aid did not increase with the increase in GNI of rich countries. Instead of 0.7%, the amount of aid has been around 0.2 to 0.4%, some \$100 billion short during 1990-2009.

**Figure 3: Official Aid 1990-2009**



Source: OECD, April 2010

There are number of factors that have led to the decline in aid. Some of the reasons include an ideology shift on the part of governments and markets; increasing number of countries competing for development funds; and donors’ differing interpretation on what constitutes development assistance. Similarly, there have been significant increases in non-development aid. The expanded categories of ODA involve debt relief; administrative costs; grants to NGOs and domestic agencies to support emergency relief operations; provision of surplus commodities of little economic value; and technical co-operation grants to pay for the services of nationals of the donors’ countries.

However, some recent findings on the contribution of foreign aid to nation’s development goals show some positive results. The findings show developmental aid is satisfactory but not enough. For example, the 2008 Survey on Monitoring the Paris Declaration covering close to US \$45 billion of development aid in altogether 55 countries shows that both the donors and recipient countries have made some progress towards achieving the international commitments. The early implementation of the Paris Declaration also shows that there has been a significant and tangible strengthening of national development policies and strategies (Deutscher and Fyson 2009).

The Nepalese experience too reveals the same concerns. There has been, indeed, a large discrepancy between aid commitment and disbursement. The trend shows that the problem has been even more serious during the last decade. Since flow of foreign aid is also the function of governance, such high discrepancy is attributed to political instability in the country during those time periods. Such variations between commitment and disbursement have its implication for budgetary practice in Nepal.

The budget is prepared on the basis of commitment. The reduction in the commitment inevitably will have negative impact on the achievement of development goals. The reasons for the differences between the commitment and disbursements have been attributed to lack of matching fund; weaknesses on making claims for reimbursement; and inability to fulfill the agreed grants and loan conditionality.

## **Aid Effectiveness**

Often foreign aid is criticized for not contributing to economic growth in general and poverty reduction in particular. Foreign aid or (development assistance) is regarded as being too much, or wasted on corrupt recipient governments despite any good intentions from donor countries (Shah 2010). While there are also number of issues for effectiveness of foreign aid, for example- higher level of democracy, human rights, governance, liberalization and economic reforms backed by decelerating state of corruption and conflict in recipient countries; the central debate is over its contribution to national development of any nation. It is argued foreign aid being supply side driven attribute solely to motives and objectives of donors; and therefore not contributing to developmental activities of national priorities.

The review of available literatures reflects, in development economics, policy reforms occupy key position in crucial development dialogue both in developed and developing countries. Literatures on aid effectiveness show varying impact under various policy environments with differing quality of governance. Aid effectiveness study on Nepal shows that the relationship between aid and per capita real GDP is found to be negative in both aggregate and disaggregated forms in the short-run implying that the country suffers from lack of absorptive capacity and high aid volatility (Bhattarai, 2005). Aid is effective when it is moderate in volume and counterproductive when it increases in size i.e., when it exceeds the absorptive capacity (Brynt 2005). High level of aid erodes institutional quality, increases rent-seeking and corruption, therefore, negatively affects growth (Knack 2000).

## **Aid: Costs and benefits**

Draft Foreign Aid Policy, 2009 intends to develop and adopt a National Action Plan (NAP) on Aid Effectiveness both by the Government of Nepal and donors, which is expected to formulate roadmap on foreign aid management in the spirit of Paris Principles on Aid Effectiveness and Accra Agenda for Action. Foreign Aid Policy will help develop a common aid effectiveness platform as envisaged through NAP which will lead Nepal's aid regime towards properly identifying key priority areas, contribute to harmonization and bring out sustainable outcomes.

Foreign aid has both cost and benefits to the recipient and donors. To some extent aid has been an investment in maintaining global stability. Globally, about one billion survive on less than \$1 a day. The challenge is to bring about real change in the lives of children and families living in extreme

poverty. In case of Nepal, access to aid has not been a problem. The key obstacle to address people's expectations for better life through aid-oriented priority projects lies in the inability to utilize aid.

About Rs. 48 billion foreign aid was committed to Nepal by development partners during the FY 2008/09. By July 9, 2010, Nepal has received Rs. 97 billion foreign aid commitment. In relation to the encouragement received by increasing aid commitment, as stated above aid, utilization has been minimal (MOF, Budget Speech, 2010).

There are tons of money in wasteful and ineffective economic development aid and other nonessential accounts. Since World War II the United States has spent nearly \$1 trillion (in 1997 dollars) on foreign aid. The impact remained discouraging. Countries that received assistance experienced debt, dependency and poverty. USAID admits, in 1993, much of the investment financed by it and other donors between 1960 and 1980 has disappeared without a trace and government-to-government transfers could not generate self-sustaining economic growth. Not only this, over US\$2 billion investments in Zaire served no purpose (Bandow 1997).

## Conclusions

Nepal's foreign aid policy (FAP) is undergoing a major overhaul, since the first FAP, 2002 was promulgated. The revised version appeared in 2008 and again in 2009 for policy endorsement by successive Nepal Development Forums. Despite these efforts, review shows Nepal still needs to bring about comprehensive reform programs to address changed global environment to competitive lending procedure and Nepal's proposed model for fiscal decentralization under the federalist characteristics. Nepal's current policy has failed to use the resources productively and maximize the benefits especially for the deprived groups of people. Overemphasis of political restructuring at the cost of economic restructuring by country's political process is inexcusable with regards to strengthening aid utilization capacity.

At a policy level, as long as foreign aid is not designed to integrate with priority developmental activities, periodic assessment of the impact of foreign assistance will always be marginalized. This has created a huge gap in collecting information on the impact of aid in inflation, exchange rate and other critical indicators so necessary for public expenditure management and the formulation of appropriate fiscal and monetary policy to contain inflation. The time therefore, has come to develop domestic aid policy compatible with country's priorities and harmonize it with the *New Approach to Development* endorsed by G8 Summit.

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# 4

## Challenge of Managing Aid in Evolving Development Dynamics

-Dhakal, Narayan<sup>1</sup>

*Development initiatives taken after introduction of the Marshall Plan could not perform well in most of the developing country contexts. One reason behind low performance is exogenously imposed 'blueprint' of development imposed with aid flow. Another is paucity of capacity and preparedness in the recipient countries for owning and leading own development process and internalizing outcomes. Each development approach of two extremes, namely "Exogenous" and "Endogenous" offered only one-sided incentives to the development actors for managing aid so as to achieve development results. This paper reviews concepts of development approaches, with special focus on the two extremes and attempts to explore whereabouts of aid management initiatives in the evolving development dynamics. It concludes that pragmatic avenue for effective aid management could be mutually customized development approach, where context matters the most.*

*Key words: exogenous, endogenous development, incentives, aid effectiveness, capacity.*

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1. Email: narayan\_dhakal@yahoo.com. Part of this paper is based on PhD dissertation on "Socioeconomic Evaluation of the Donor Harmonization" submitted by the author to the Graduate School of Economics, the Kyoto University, Japan in 2007.

## 1. Introduction

Systemic development thinking accompanied with development aid started only after World War-II. Particularly, U.S. President Truman's proposal of development aid to Greece and Turkey and the Marshall Plan, the reconstruction aid to Western Europe in 1947 were the signpost to understand the root motivating factors to present day development aid. One argument believes that externally designed and imposed development models with 'one-size-fits-all' assumption have been limiting performance of development aid by unknowingly restricting recipient ownership and leadership that are essential for aid and development effectiveness. Another argument revolves around deficiency in recipient capacity that potentially hinders the path to aid and development effectiveness.

Review of development dynamics along the course of development history reveals that proper use of development aid for development result requires best practices of the donors, recipients and other stakeholders as partly articulated in the Paris Declaration, 2005. Focused studies on implementation of the Paris Declaration find hesitations in many of the stakeholders. The reason behind this hesitation and tensions is deep-rooted intuition on rigid development models of exogenous and endogenous nature. A mid-way and context friendly approach of development will have to be found as an avenue for result-oriented management of aid. By ways of examining literatures and content analyses, this paper reviews major models in light of aid management and identifies customized approach, where incentives of stakeholders can be taken into account with a view to facilitating easy acceptance and implementation of the best practices agreed upon by development actors.

## 2. Development Concept

The concept of 'development' emerges with the 'development economics' during the 1940s. Sen (1988) gives credit to Sir William Petty, for his work on "Political Arithmetic" published in, 1691 for introducing development economics, while Todaro (2000:7) believes that it is post-war phenomenon emerged particularly for development of Asia, Africa and Latin America and is arguably different from "modern neo-classical economics" and "Marxist command economics". It is because of complex contextual background characterized by ideological, historical and cultural diversity. Visibly, two sets of the context (developed and underdeveloped) surfaced development economics as a separate branch of knowledge (Sen, 1988; Lucas, 1988; Meier and Rauch, 2000). Besides, other branches of development-related knowledge gradually emerged under the broad framework of 'development economics'.

'Development administration', emerged during 1950s serves as another conceptual base specific to the mobilization aid in the third world country context. It aims at administratively regularizing and legitimizing the development outcome (Clarke, 1996 in Saifullah, 2001). However, as McSwite (1997) worries, the issue of legitimizing public administrative



theories themselves remain vague and debatable amid normative paradoxes of 'democracy', 'bureaucracy' and 'social disharmony' requiring more concerted scientific pursuit.

'Development management' emerged with the insights of reduced bureaucracy; increased private sectors; and improved capacity of grass root stakeholders, encompasses the issues of management of development aid. It pleads for co-existence of multi-level stakeholders through resolving conflicts, harmonizing, empowering and democratizing the local community to maintain governance in the development process. It also encompasses 'exogenous' and 'endogenous' development approaches (Montgomery, 1995; Clarke, 1996 cited in Saifullah, 2001).

'New public management' emerged with the belief that market oriented reform of public sector leads to cost-efficient government that considers beneficiaries as customer and citizen as shareholders. More recently, the concept of 'new governance' emerged in light of newly developed instruments of public actions that transformed public management from 'provider' to 'arranger' of public services with capacity of harmonization and collaboration among various tools and multilevel actors (Salamon, 2002). This had a lot to do with aid management practices.

Seemingly, 'development management' is the nearest theoretical premise that pleads for better management of development aid to produce effective development results. Realizing effective and tangible development results is the motto of 'aid and development effectiveness' as articulated in the Paris Declaration, 2005.

### **3. Dimensions and Dynamics of Development**

'Development' is a multi-dimensional phenomenon. Economic dimension believes on 'economic growth' managed and distributed through 'new job creation' and 'trickle down' effects (Elkan, 1995; Meier and Baldwin, 1957). United Nation's Human Development approach is more social dimension of development. Paul P. Streeten cited in Todaro (2000:77) believes that human development aspects like malnutrition, disease, illiteracy, slums, unemployment and inequality induce people to be capable of recognizing and enjoying the development outcome. Capacity to improve productivity is both social and economic concern that seemingly requires going beyond the conventional market approach. Lewis T. Preston cited again in Todaro (2000:77) views: Development theory by itself has little value unless it is applied, unless it translates into results, and unless it improves people's lives. These result concerns are indicators for aid effectiveness and development effectiveness which is the main slogan of "Aid harmonization."

Development has also been seen from a perspective of individual value system, where value differences, i.e., "value heterogeneity" and the assimilation of heterogeneity by way of development process, i.e., "value endogeneity" are at the root of developmental problem. Different perceptions about real indicators of development, like 'well-being', 'happiness', 'freedom' etc. are outcome of value differences. Failure to

understand these differences are major causes to policy failure (Sen, 1984; 1988; 1999a; 1999b). The Sen Approach puts people's happiness, capabilities, entitlement, well-being, opportunity, participation, and freedom of choice in the centre-stage of development, that greatly influence contemporary policy of development aid as well (Akiyama et al., 2003; World Bank, 2006). These concerns are also considered in the present day aid management.

Dasgupta (1993) views development as curbing 'destitution' and enhancing 'well-being' of the people, from economic perspectives. 'Destitution', the extreme condition of 'ill-being', results in personal calamity and social weakness that are obstacles to productivity and 'development.' Author argues for role of the government to provide adequate diet and health care to enhance the 'well-being' of the individual and the society for achieving meaningful 'development.' Government can adopt an appropriate, productive and contextual aid policy through 'resource allocation mechanism' that potentially enhances 'well being'.

Current paradigm of development is dominated by broad institutional aspects of interconnected public-private ties grounded on social and contextual reality. Tools for this are local ownership, local leadership and capacity development of the beneficiaries (North, 1990; Stiglitz, 1998a; 1998b). Thus dynamics of development has been changed over time in the face of success and failures of the development process from macro to micro impact on real life.

Earlier exogenous development models, like Walt W. Rostow's 5 stages of economic transformation and "Harrod-Domer" model, where additional investment leads to increase in national output were based on the Marshall Plan experiences in the developed society (Meier and Rauch, 2000; Todaro, 2000), which may not always be of appropriate use in the developing countries context. Bauer (1970) argues that the Marshall Plan is not comparable to development aid because the context of the then Western Europe and present day developing countries are totally different. There was abundant amount of social capital in Western Europe and the period of Marshall Plan was only for four years, while developing countries have been receiving aid for the decades. In this context, Bauer (1970:34-35) writes:

The economies of Western Europe had to be restored while those of [developing countries] have to be developed. Europe after 1945 was demonstrable short of capital resources, especially stocks of food and raw material, but not in the necessary human resources and market opportunities. Its peoples had the attitudes, motivations and institutions favourable to development, as was clear from the performance of Western Europe for centuries before the Second World War.

Riggs (1964) has developed 'prismatic model' from public administrative standpoint, which is known as little more revolutionary model of development. The theme is that the transformation of traditional society into modern society takes place either 'exogenously' or 'endogenously'. Riggs is sceptical to Western models of exogenous development for being too inductive, ethnocentric and less of use in developing countries. He

thought no earlier development theories cared for administrative capability and found out the configuration of implementing forces prevailing in the non-Western society. The author divides the world societies into 'traditional', 'modern' and 'prismatic' (Riggs, 1964; Levy, 1966: 38, 60). In the same line, Kautsky (1972) views that modernization takes place either from inside (i.e., endogenous) or from outside (i.e., exogenous) influences having many implications on political and societal structure and their sustainability.

"Dependency" theorists see the world economic system as 'centre' and 'periphery' representing 'developed' and 'underdeveloped' world, respectively. The prosperity of the former is dependent on the destitution of the later. Therefore, 'centre' has perverse incentive to make the 'periphery' economically dependent on it. Dependency is defined as 'exogenous' influences (economic, political and cultural) on national development policy (Dos Santos, 1970; Sunkel, 1969; Ferraro, 1996; Akiyama et al., 2003). This school views aid as alien concepts and perceives management of aid from nationalist perspective.

There is another soft type of international dependency approach to development, which believes that the underdevelopment is the result of faulty and inappropriate advice imposed by international experts who are flown to developing countries as a component of aid. "These experts offer sophisticated concepts, elegant theoretical structures, and complex econometric models of development that often lead to inappropriate or incorrect policies" (Todaro, 2003: 125).

'Endogenous' growth theorists tried to indigenize the rate of technological progress giving importance to the production of new technologies and human capital. Advantages over other competitors and improving productivity are taken as the incentives for investment. 'Endogenous' theorists believe in the 'virtuous cycle' where the knowledge associated with the innovation spills over to the other economic actors leading them innovate new knowledge (Naffziger, 2006; Todaro, 2006; Elkan, 1995). One of the criticisms of this theory is that it could not explain the 'context' that greatly contributed to non-convergence.

Theory of 'self-reliance' appears as an antithesis to dependency theory. The main idea behind this is that every society relies on its own strength and resources determined by its members' energy, its natural and cultural environment. The natural stage of development is the way of life, which the people escape when the dependency becomes unbearable. This is an attractive and humane approach to development (Hettne 1984: 78.). From donor perspective, 'self-reliance' is defined as one's own efforts to achieve difficult goal; change the status-quo; and promote development by and for oneself without depending on outside help (Akira and Yasutami, 1998: 8-9). A poor country may not have critical amount of financial, human and social resources to run its basic functions in competitive world. Therefore, absolute 'self-reliance' may not be possible in the globalized world. However, it is imperative that developing countries utilize aid to achieve 'self-reliance' (Dhakal & Ueta, 2007).

'Sustainable development' is one of the emergent and widely discussed ecological concepts of development. Originally, the term was introduced in 1987 by Brundtland Commission as "... meeting the needs of the present without compromising the ability of future generations to meet their own needs" (UNO, 1987: 24). This concept helped to convert conventional rivalry relationship between 'growth' and 'environment' into the supplementary relationship. This induced aid agencies to adopt 'environmental modernization' strategy (Jones, 2006: 210). Sustainability has entered into development discourse as a part of nexus among 'poverty', 'inequality' and the 'environment'. The environmental degradation is an issue of poverty because poverty exacerbates degradation. Similarly, degradation exacerbates poverty by reducing well-being (Akiyama et al., 2003). As time passes on, the original strict environmental sense of 'sustainable development' expanded to the longevity of the social impact of development and projects (Ostrom et al., 2002:8). Aid policies of both the donors and the recipient countries have been greatly influenced by the approach of "Sustainability".

'Basic needs' concern put forward by the International Labour Organization (ILO) in 1976 also occupied substantial space in the development literatures. 'Basic needs' is defined as minimum consumption requirements of a family; including food, clothing, shelter, and other essential services, including education, health and so on. During 1980s, 'basic needs' was taken as primary objective of the development. Productivity is also the function of the fulfilment of the 'basic needs' because an individual with empty stomach cannot be productive. Poor people have willingness to work but they lack assets. Therefore, they must get subsidy (Streeten et al., 1981: viii, 8). Proponents of 'basic needs' approach argue that the growth approach could not be inclusive of the poor. Therefore, world anti-poverty program get focused on equality (Myrdal, 1970). It has drawn attention of development thinkers and practitioners from growth to higher living standard; institutional changes; role of social capital and human capital. Aid management issues have also to be changed accordingly over time.

Since early 1990s to date, the 'new views' are prevailing with high importance of the institutions, formal and informal 'rules of the game', in economics. 'New views' seem to be continuation of 'basic needs' approach, which contributed to devise human development indicators to measure development qualitatively. Much of the aid today is operating on basis of 'new views'. Unlike earlier economists who considered 'industrialization' as the indicator of development, 'new views' believe on the "presence of appropriate institutions". Development is taken as institutional success while underdevelopment as institutional failure. Studies have identified that the trust, cooperation among the economic agents, judicial systems etc were the institutional factors of success in East Asian Economies. The failures in transitional economies, including Russia were due to the lack of institutions. Institution is a vague term that encompasses all type of formal and informal establishments (Coase, 1937; North, 1990; Olson 1965; Stiglitz, 1998a; and Williamson, 1975).

'Social Capital' approach of development, where social cohesion and mutual interactions occurs for mutual benefit and the associations, networks, clubs etc facilitate the growth by increasing trust among the member of communities. Co-operation among members of a group creates habits and attitudes towards interactions among members and non-members (Collier, 1998; Putnam et al., 1993; 1995a; 1995b; 2000). Ideas of social capital, institutions and culture are interrelated because cultural values are elements of social capital as well as foundation for institutional structure (North, 1990). It is not easy to promote social capital merely by development aid. It requires changes in laws, bureaucratic structure etc., which may be politically unpopular. Therefore, Hayami (2001) views capacity development of rural community with support of aid could be the most appropriate path to development. At the same time, there must be adequate incentives for rural community to induce them to join development activities with full capacity. Recently, Uzawa (2005) coined new term "social common capital" as a form of 'social capital' comprising of common property, public goods and institutions.

Thus, the dynamics of development has now arrived at institutional and contextual concerns with more complexity at hand in terms of aid management. Involvement of multi-level actors in aid relationship is one of the major causes of complexity. What incentives do the actors perceive from aid business is a crucial issue for aid management, which requires separate inquiry.

#### **4. Managing Aid for Development Effectiveness**

Management of development aid in consonance with contemporary development paradigm is a daunting challenge for it is perceived as per convenient of the major actors- different donors, different recipients, business community and the civil society organizations both in the North and the South. The Marshall Plan itself was conditional while offering up to \$20 billion to the Europe for reconstruction. The European nations were asked to plan, lead and take ownership of their own program under Marshal Plan. These conditions were important elements of effective aid management and were part of incentives for Europe. At the same time, the plan required the Europe to import goods from the United States using US ships so that US economy would benefit (Dhakal & Ueta, 2007). Thus, the incentives of the Marshall Plan for Europe were it helped them in hard time; and for donor, it pumped the donor's economy and helped meet strategic interest. However, the Marshall plan proved that participation, ownership and leadership of beneficiary had contributed to quick reconstruction and development.

The recent orientation in regard to aid management can be found in the Paris Declaration, 2005, implementation of which has already been monitored thrice and evaluated twice, globally. The Paris Declaration is a collection of ambitious but visionary political commitments made at higher level articulating 56 commitments around ownership, alignment, harmonization, result-based management and mutual accountability for

effective and efficient management of aid. The 12 indicators were reaffirmed in the Accra Agenda for Action in 2008. It is almost set to be looked into The Paris Declaration in more critical fashion in the forthcoming high level forum in Busan of Korea in 2011. Translating Paris commitments into real life situation has remained a challenge amid evolving development orientation.

Global synthesis of the phase II evaluation of the Paris Declaration reveals that it is still relevant in many of the countries to improve quality of aid management, partnership, transparency and their impact on development results. As compared to the pre-2005 situation, the Paris Declaration has brought about crucial tempo of reform in aid management. Of the five principles of aid effectiveness, country ownership has advanced farthest, while alignment and harmonization progressed unevenly and managing for development result and mutual accountability are advancing least (DIIS, 2011).

Being one of the signatories to the Paris Declaration, Nepal also participated in the second and third monitoring surveys in 2006 and 2011 respectively, and the second country evaluation of its implementation in 2010. Both the surveys registered some progress but indicated long way to go. The second monitoring survey, among others, revealed that there were still 106 parallel Implementation Units and 36 percent of aid flow do not use formal budgetary channel in Nepal (MoF, 2006). If it is calculated on average per donor basis, it reaches nearly 56 percent as hinted in the preliminary draft of the third survey report. Findings of the third survey are yet to be published, officially.

The findings of country evaluation of the Paris Declaration in Nepal are in line with global findings except in regard to development result. It revealed that the Paris Declaration is still relevant in Nepal, particularly in the context of undergoing political, social and economic development. It has raised the strong concerns towards development results in Nepal. Its contribution to enhance country ownership and alignment of Development Partners strategies with the national development strategy is moderate. However, its contribution to the use of country system, harmonization and mutual accountability is less plausible. Changes observed by the evaluators in terms of intermediate outcomes as well as development outcomes are more influenced by the natural phenomena of change, including strong desire for transformation than by the Paris Declaration per se. Having said this, the consideration for implementation of the Paris Declaration has plausibly contributed to develop the level of assertiveness and confidence in major development actors in Nepal (MoF, 2010).

Nepal is found to be proactive in terms of creating demand of the use of good practices in aid management. Government capacity were shown by expressing readiness to take lead in conducting and managing various aid related national and international fora, like Nepal Development Forum (NDF), Nepal Portfolio Performance Review (NPPR) and similar networks, taskforces, and initiatives for transparency, data sharing and so forth for aid effectiveness. (MoF, 2010). However, there are problems experienced in

bringing all the donors working in Nepal into the framework of Paris style aid management.

## **5. Managing Aid in Exogenous and Endogenous Development approaches.**

Complex and multi-dimensional process of development demands 'endogenous' development because development cannot be patterned beyond aspirations of local people. Transfer of knowledge, technology, institutions etc must not impede endogenous development but help it get off the ground (Ribes et al., 1981). 'Innovation', i.e., the process of discovery and 'adaptation', i.e., the borrowing by other society with necessary modification are two major dimensions of 'development.' In some society, process of development is innovative because their own "endogenous forces" motivate them to pursue the process. By contrast, other may be influenced by innovation of the developed society and transform themselves through adaptive process influenced by exogenous pressures (Riggs, 1964: 39; Gutelman, 1981:32). Riggs argues that the elites in transitional societies are normally persuaded by Western forces to take lead in the process of transformation in their own society. This is 'exogenous' model because "non-Western" societies responded to the impact of the "industrialized West". By contrast, the 'pre-modern' societies of Europe, like England, France, Holland had exercised 'endogenous' development because "aggressive middle class" rather than elites and aristocrats of these societies had passion to change and pursued scientific and industrial revolutions (Riggs, 1964: 39).

Galtung (1979) cautioned to use localized approach to avoid negative side effects transmitted from developed to developing countries with aid and technology. He prescribes for a right mix of "alpha" type (e.g., hard or rigid type) and "beta" type (e.g., soft or flexible type) as appropriate technology. In his own words:

The more basic the need to be met, the more should the technology be "soft" and tied to smaller social units, giving them a survival capability even in crises, less exposed to the vulnerability of "hard" technology. [However] the basic argument favours an open mind on these issues, and encouraging an experimental, non-dogmatic attitude, combining the two types of technology rather than gambling on one type only (Galtung, 1979: 2).

Gutelman (1981) argues that development is outcome of inevitable knowledge acquisition process either through 'innate creativity of society, or through 'exogenous transfer of knowledge.' In many cases, mid-way between 'exogenous' and 'endogenous' became feasible, as shown by history of development. Gutelman (1981) further argues that the conversion of Celtic Gaul into Gallo-Roman<sup>2</sup> in remote history and modernization of Japan in the recent history were examples of the combination of exogenous and endogenous development.

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2. In history of Europe, the Roman Empire tookover 'Celtic Gaul' in 121 BC. Gallo-Roman was the Romanized culture of 'Gaul' under the rule of Roman Empire.



Njoh (1999) assessing implication of exogenous forces in urban planning development of Sub-Saharan Africa, finds that development outputs were more beneficial to the donors than the recipient. The author suggests for careful transfer of technology so that utility is maximized; damage to indigenous technology is minimized; and adaptability are ensured (Njoh, 1999).

In Caracas of Venezuela, the role local population played in production process based on foreign models was disappointing in terms of the acquisition of new knowledge. A rudimentary endogenous system of organization in Rancho district led to new and original town planning solutions (Chombard de Lauwe, 1981). The author comes up with many contrasting instances of endogenous and exogenous development in terms of monopoly of the industrialized West in technology and information of and their domination in the underdeveloped world (Ibid, 1981).

Grefe et al. (1981) present three endogenous mechanisms for transfer of knowledge in economics. First, 'activation of internal debates', second, comparison between economics and other disciplines, and third, reconsideration of existing subject matters of economics. The author also suggests five areas for research in this regards. One of the most promising areas is making full use of local economic knowledge with mutual customization so that both exogenous and endogenous contents create synergies.

Gunn (1990) observes historical development trends in Somalia and identifies 'static interventionist' and 'dynamic adaptive' model for what Riggs calls 'exogenous' and 'endogenous' respectively. The former model, as author argues, assumes poverty in local economy and social resources requiring large aid interventions while the later assumes existence of various indigenous options. Both polar approaches have own pros and cons and combination of both is workable than new separate model (Gunn, 1990).

Jun (2005) views endogenous development as the latest development paradigm that advocates for co-existence, cooperation, environmental protection and development. "Global civil society" is the key actor in this new paradigm. Hainsworth (1999) carries out case study in a poor society in Vietnam and identifies that the poor do have choices, though limited, and are careful rational decision makers than the rich because irrational decision costs high, which the poor cannot afford.

FWP/FNDI (2006) examines three different cases of community development projects in South Dakota, Uganda and Ecuador and finds four tiers effects. First, 'fully exogenous' model does not generate benefit to local people and does not minimize project risks. Second, 'partially exogenous' model generates partial benefits with 'incentives' for risk minimization. Third, mix of 'exogenous idea' and 'endogenous design' generates direct benefit and risk minimization mechanism. Finally and importantly, local community fully owns the programs with endogenous idea and design mixed with supplementary funding and technical assistance of donors. Therefore, a tailored development paradigm systematically achieves people-centred,



sustainable and self-reliant development while exogenous models are economics-centric that ignore indigenous people. Development happens from within; it is not done or made from outside.

As discussed above, broad approaches to development can be grouped into 'exogenous' and 'endogenous.' In developing countries, two types of fund - external resources, i.e. 'foreign aid' and internal resources, i.e., 'domestic revenue' prevail, which follow clearly two sets of values, structures and operational frameworks, resulting in conflict of interests and high transaction costs. Management of aid amid proliferated discrete projects always becomes an issue. The situation then requires harmonization. To make the actors ready to harmonize, incentives must be aligned at one point from both 'exogenous' and 'endogenous' approaches. A tabular framework developed by Dhakal and Ueta (2007) shows the combination of aid and domestic resources in 'endogenous', 'exogenous' and 'customized' development approaches and analyzes incentives compatibility (See, Table-3.1).

**Table 3.1: Potential Framework for Incentive Alignment**

	Endogenous (En)	Exogenous (Ex)	Customized (C)
Local Resources (L)	'EnL' Ethnocentric	'ExL' Redundant	'CL' Utopian
Foreign Aid (F)	'EnF' Unattainable	'ExF' Egocentric	'CF' Pragmatic

**Source:** Dhakal and Ueta (2007)

Combination of 'endogenous' and 'local resources' (EnL) is 'ethnocentric', i.e., guided by cultural supremacy. It is ideal for the recipients because local community can have greater choices. Beneficiaries within the context are master of their destiny because they do not need to follow alien concept of development. Technology and knowledge can either be innovated endogenously or can they be purchased from other countries. Unfortunately, it is not practical in this 'globalizing' world of interdependence. Therefore, it is an ambitious combination (Dhakal and Ueta, 2007).

Combination of 'endogenous' and 'foreign aid' (EnF) is desirable because endogenous approach is aboriginal for recipients. However, it is difficult to attain because aid always brings as Galtung (1979) argues, the structure, social cosmology, and values of the donor countries with technology and institutions. The recipient lacks capacity to deal with multi-layered interest groups in aid delivery chain and lack bargaining power in negotiation table mainly due to asymmetric information and knowledge. Therefore, this combination is difficult. Paris Principles of "Aid effectiveness" for effective

aid management fall within this combination. Unfortunately, lopsided incentives are making it difficult. To make it easy, capacity development of the recipient through organic process could be helpful (Dhakal and Ueta, 2007).

Combination of 'exogenous' and 'local resources' (ExL) is redundant because there is no need to follow the 'exogenous' directions if resources for development are available locally. This combination normally does not occur.

Combination of 'exogenous' and 'foreign aid' (ExF) is commonly found in present day aid relationship. International regimes prescribe the exogenous approach on 'one-size-fits-all' assumptions undermining local capacity and institutions. This approach is costly and unsustainable because of tied and conditional aid. Expenditure standards are set as per donor countries purchasing power and development outcomes achieved with such approach wither away in no time as the outcomes cannot sustain financially and institutionally after donors' withdrawal. Most of the project type funding fall within this combination. Unfortunately, this combination is an unsustainable and 'egocentric' (Dhakal and Ueta, 2007).

Combination of 'Customization' and 'local resources' (CL) is a natural but utopian combination. On one hand it helps meet local needs and aspirations, but on the other hand, a single country cannot offer abundant local resources in this interdependent world. However, it is desirable combination because the process of customization would enhance knowledge and appropriate technology. This is where every recipient country intends to reach but in lack of local resources and capacity, they will have to depend on some role of foreign aid (Dhakal and Ueta, 2007).

Combination of **'Customization' and 'foreign aid'** (CF) could be better for both the donor and the recipient because availability of resources and alignment of incentives could be possible in it. 'Glocalization,' i.e., an admixture of 'globalization' and 'localization' for thinking globally and acting locally, could be the motto in this combination. Identifying both sides' incentives by way of behavioural interaction require capacity and full information.

The 'new views' of development, including 'aid effectiveness' principles can be accommodated in this approach. Instead of building separate rigid model, flexible mixing of two approaches on country to country basis would be pragmatic strategy for effective aid management (Dhakal and Ueta, 2007).

## Concluding Remarks

Having reviewed the literatures and studies carried out in the field of development and aid management, it is evident that the pragmatic development approach rests in-between two extremes- 'exogenous' and 'endogenous' approaches. The mid-way approach can be developed on country by country basis by ways of customization process. Customization involves close review of two-way incentives system, which can motivate the donors, the recipients, and the civil society, including academia and business

community. This is where effective management of aid takes place and can produce development result.

The process of customization involves cost, technology and capacity, which can be attained by help of flexible programmatic aid that can care for local system, institutions, other context and mutually agreeable framework of incentives. Choices offered by this approach help avoid weaknesses and adopt strengths of both the 'exogenous' and 'endogenous' extremes. Ultimately, the choices and flexibility around ownership, leadership, use of country system, and respect to each other's norms, values and structures would ease the customization process moulding with the demand of stakeholders, time, and global and local policy thrusts.

Studies carried out during early 1960s, late 1980s, late 1990s and more recently in 2010 support the argument of 'customized' approach of development. To recapitulate, Riggs (1964) envisages "meso-prismatic" society in between 'endo-prismatic' and 'exo-prismatic' society and hints for the mix up of two extremes. Galtung (1979) pleads for localized approach to avoid negative side effects of foreign technology and prescribes for a right mix of "alpha" and "beta" as appropriate technology. Wight (1997: 390) suggests for participative implementation modality where foreign technology and development model can be tailored to local need in local way of doing business. Case studies carried out by FWP/FNDI (2006), suggests a tailored approach, where blending of 'exogenous' technical support and 'endogenous' idea generates direct benefits to the recipient and minimize the project risks.

Thus, development is a dynamic concept passing through paradox of 'exogenous' and 'endogenous' approaches. It has symbiotic relationship with 'development aid' and its effectiveness. Despite attractive agendas of 'aid effectiveness', the implementation side appears reluctant. 'Exogenous' approach dominates the recipients and distorts their benefits. This approach does not take into account the recipient-incentives. Donor side prefers 'exogenous' approach to 'endogenous' because it is easy to implement, commercially, politically and strategically beneficial, and identifiable. 'Endogenous' approach, on the other hand, is ambitious and does not take into account the donor-incentives. The donors pretend to obey the 'endogenous' approach because of global policy directions. On operational level, donors are reluctant because of inadequate incentives. The new paradigm of development manifested in 'aid effectiveness' is designed exogenously but bears 'endogenous' attributes making it biased to the recipients. Weak capacity at local level further fuels the reluctance of donors. Capacity has causal relationship with aid effectiveness. In lack of capacity and incentives, cooperation may not last long in international relations. Once both sides perceive incentives, they actively participate in implementation. This process may be possible in the 'customized' development approach.

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# 5

## Foreign Aid Politics in Developing Countries

—Bharat Pokharel

*Developed countries give away millions of dollars a year in foreign assistance to aid developing countries, but what are the effects? Foreign aid flows from developed to developing countries have been hailed as the solution to world poverty. However, aid is beneficial to any country no matter the circumstances needs a great deal of introspection. The influx of massive amounts of foreign aid can have deleterious effects on the governments of the receiving countries, and can end up doing more harm than good in several circumstances. However, discrimination by donor countries on the basis of standards of governance creates new complications. The current foreign aid paradigm should be overhauled, and the new system should take a more nuanced view of international development.*

### Background

Traditional development economics has long viewed foreign aid as a tool for overcoming the savings gap in developing countries. Based on the assumption that the Third World is poor because it lacks the capital necessary for making income-generating investments, mainstream economics literature suggests that aid can help developing countries by closing this financing gap that otherwise leaves them stuck in a “poverty trap.” The “big push” argument portrays aid as the necessary catalyst for investment that would, in turn, lead to growth and presumably initialize an upward path to economic development (Schabbel, 2007). This view of aid is perhaps most

famously encapsulated by celebrity economist Jeffrey Sachs' *The End of Poverty*, in which he prescribes a comprehensive package of massive aid transfers and widespread reforms that aim to tackle multiple socioeconomic pathologies quickly and simultaneously. Shock therapy of this sort, Sachs argues, can end extreme poverty for the world's "bottom billion" by 2025 (Sachs, 2005).

When a disaster or famine strikes, people in the West are bombarded by a flurry of appeals, and of course, men and women whose hearts go out to people in distress, do their bits to save the hungry. This is as far as it can go in Western mainstream advertising. They barely talk of the root cause, nor do they bother to talk of who is responsible – and even less of how people can escape clutches of from chronic hunger and recurring natural disasters. In fact, the situation is presented as if there were no solution and nothing could have been done about it but to send charity from the rich countries. But how legitimate is the foreign aid given to the oppressed countries? What are the goals and results of this aid?

### **Foreign aid and corruption**

There is no compelling evidence that donors pay attention to institutional quality or corruption syndrome in their aid allocation decisions. Research has found no systematic evidence that bilateral or multilateral aid goes disproportionately to less corrupt governments (Svensson, 2000; Alesina & Weder, 2002). In fact, one study provides considerable evidence that patterns of aid allocation by bilateral donors are far more robustly dictated by the political and strategic interests of the donors than by concerns over good governance in the recipient nations (Alesina & Dollar, 1998). In more concrete terms, factors such as colonial history and voting patterns in the United Nations tend to explain more of the distribution of aid than do the political institutions or economic policies of the recipient governments. The Alesina and Dollar study illustrates that among the three biggest bilateral donors—the United States, Japan, and France—France in particular gives overwhelmingly to its former colonies, many of which are in Sub-Saharan Africa. A few donors, notably Australia and the Nordic countries, do show a tendency to discriminate in favor of less corrupt governments, presumably because they do not have colonial legacies and are therefore free from specific political pressures, but on the whole these donors remain the exception. Finally, international organizations like the IMF and the World Bank that dispense multilateral aid do not show any discriminatory tendencies against corruption in the recipient country.

High aid dependency often leads to a strong presence of aid agencies and NGOs in recipient countries, which choose to "by-pass" the cumbersome government bureaucracy and consequently "poach" skilled bureaucrats away from civil service. In many cases, foreign aid donors fear that government agencies in recipient countries are ineffective and encumbered by corruption, and that government bureaucrats are unmotivated, underpaid, apathetic, or poorly trained. To maximize the chances that foreign aid will meet its



targets, some donors will therefore choose to “by-pass” the government bureaucracy altogether and set up their own administrative network with better salary incentives (Brautigam, 2000). Empirical data demonstrates that salaries in aid-sponsored projects are usually considerably higher than salaries available through government employment. In Kenya, for example, monthly salaries from a donor-funded agricultural project ranged between \$3,000 and \$6,000. When compared with the average government salary of about \$250, it is easy to see how capable local talent in aid-receiving countries would be attracted to staff the resident offices of aid agencies and NGOs rather than taking up government positions (World Bank, 1998). This erosion of talent leaves the government bureaucracy in the hands of less qualified, untrained, unmotivated, or completely incompetent officials and therefore erodes the quality and effectiveness of government institutions.

### **Foreign aid and renter state**

Aid as a source of government revenue parallels other types of rents. According to Adam Smith’s classic definition, rents are “unearned incomes or profits reaped by those who did not sow.” Economically speaking, rents are “unearned incomes” because they exceed all relevant costs, and are therefore akin to a monopoly’s supernormal profits. In context of the state, rents are incomes generated from external sources—such as foreign aid, or perhaps mineral export revenues—rather than extracted from the surplus production of the population through taxation (Karl, 2004).

Experts warn that if rent windfalls, like foreign aid, coincide with the early stages of state formation, they can distort the institutional development of the state. This happens because aid influxes provide an easy source of government revenue, and thus reduce the need to build an effective bureaucratic mechanism to oversee the extractive and administrative functions of the state. The limited extractive capacity, in turn, tends to deepen the government’s dependence on rents, and consequently creates a “rentier state” effect. This theory is highly pertinent in the case of Sub-Saharan Africa, because the emergence of independent African states in the 1960s and 1970s coincided with high and growing volumes of aid transfers from their former colonizers. Ostensibly, this contributed to undermining the creation of a robust administrative and fiscal bureaucracy and other institutional capacities necessary for the formation of an effective, capacious state. Essentially, the influx of easy money allowed many newborn governments to “substitute aid dollars for state craft.”

The renter state effect not only has serious implications for state capacity, but also for the quality of democratic institutions. This pathology stems from the fact that renter states are less accountable to their populations because they are less dependent on taxation as a source of state revenue. Ross identifies a “taxation effect” commonly associated with the renter state, whereby the government uses its rent revenues to essentially buy acquiescence by relieving social pressures that might otherwise lead to demands for greater accountability and representation. He also finds

a “spending effect” on direct patronage of elites and on the suppression of opposition groups (Ross, 2001). Both of these observed effects have demonstrably negative impacts on government accountability, equity, and civil liberty.

### **Foreign aid delay pressures for reform**

By making corruption more lucrative, aid distorts the incentive structure for public actors, and may therefore delay pressures for institutional reform. Given what we know about the importance of institutional quality for economic performance, institutional reform is the key to development in many poor countries. Yet achieving reform requires solving a complex set of collective action problems. Theory suggests that reforms are akin to public goods in that they benefit the public at large, and it is difficult to preclude anyone from reaping these benefits. Often, the very goal of reforms is to improve governance and reduce corruption levels in the country. However, if aid makes corruption more lucrative by making available large sums of easy money, then the very agents who are supposed to bring about the necessary reforms will lose their incentives to act.

Aid also creates a “moral hazard” problem in the recipient country by serving as a permanent soft budget constraint. The persistent influx of easy foreign aid money creates the impression that the recipient government is always likely to be bailed out when things go wrong. Since recipient governments do not have to worry about answering to taxpayers, and are only bound by relatively loose accountability mechanisms to their donors, there is little incentive in the system for fiscal discipline and sound judgment. Essentially, aid serves as “insurance” for incompetent or corrupt leaders and weakens their incentive to seek alternative revenue sources through wise policies that encourage self-sustaining investments. Furthermore, leaders (who tend to have short-time horizons) will be more likely to make risky or reckless decisions that might yield high short-term results, but may not necessarily have sustainable or desirable long-term effects. The problem is further complicated by the fact that the best long-term policies, like those leading to institutional and economic reform, tend to be less politically desirable because they necessitate significant short-term sacrifices, and require patience and longer time horizons to achieve results.

### **Effects on foreign aid recipients**

New research suggests that foreign aid may not necessarily be harmful and that the existing institutional environment of the recipient country plays a big role in determining the success of aid-led development. An influential study by Burnside and Dollar finds that aid has a positive impact on growth in developing countries with good fiscal, monetary, and trade policies, but has little effect in the presence of poor policies (Burnside & Dollar, 1997). In essence, a positive institutional setting in the recipient country means that the detrimental dynamics of aid flows on governance can be largely

avoided. This adds another nuance to the complicated relationship between foreign aid and governance: while in the absence of good governance aid is most likely to backfire and actually contribute to a further worsening of the recipient's institutional quality, high levels of foreign aid can be well used if the recipient country's institutions are strong. This finding could have enormous normative implications for guiding future policy about foreign aid allocation.

## Policy Implications

There appears to be emerging consensus in the international community that existing institutional quality in developing countries should be factored into donors' future decisions about aid allocation. A growing number of scholars are calling for greater selectivity in allocating aid to poor countries, because evidence seems to suggest that the "big push" theory of foreign aid can only have an impact after countries have already made substantial progress in reforming their policies and institutions. World Bank estimates suggest that a \$10 billion increase in foreign aid flows would lift about 25 million people a year out of poverty if lending favors countries with sound economic management, but the figure drops to only 7 million people a year if lending is indiscriminate on the basis of governance quality.

To be sure, the Burnside and Dollar finding remains far from uncontested. A number of reviews have questioned its significance. One such review by Easterly, Levine, and Roodman suggests that the outcome is not robust to the use of an expanded data set. Additionally, the normative implication of the finding, namely that aid allocation should be predicated on good governance, is strategically thorny because it could potentially compromise the political interests of some of the large bilateral donors. Further, it is also a difficult policy to justify from a moral viewpoint, because it appears to leave poorly governed developing countries on their own.

Ostensibly, selectivity on the basis of governance quality in recipient countries could become a potential policy strategy for bilateral donors. Given the Alesina and Dollar finding that many bilateral donors already rely heavily on strategic and political considerations when making their foreign aid allocations, criteria predicated on issues of good governance seem as good a reason as any to discriminate among potential recipients. In fact, programs like the US Millennium Development Account seem to indicate the emergence of an aid allocation trend that favors good governance. Complications could arise, however, if governance considerations clash with the strategic, political, or security interests of big bilateral donors like the US or France. These concerns will in all likelihood override any consideration of governance. This strategy may be best left to more politically neutral donors, such as the Nordic countries and Australia, who already exhibit strong tendencies to discriminate on the basis of institutional quality.

On the other hand, discrimination on the basis of institutional quality does not seem a feasible strategy for multilateral donors like the IMF or the World Bank. Many multilateral donors are not allowed to discriminate

on this basis. Additionally, the promotion of good governance through aid provision is not generally the primary concern of the aid financing given out by these institutions. For example, the primary focus of the IMF's mandate is to promote macroeconomic and financial stability by fostering international monetary cooperation, exchange rate stability, and helping countries overcome economic difficulties. Although it plays a greater role in channeling global foreign aid flows to developing countries, and thus provides a significant portion of the aid transfers that have proven so problematic for many Sub-Saharan economies, an organization like the IMF cannot withhold its assistance to countries in need on the basis of their poor institutions. Multilateral organizations, therefore, must look for other ways to improve the effectiveness of their lendings.

It must first be made clear that regardless of whether greater selectivity becomes the *modus operandi* of foreign aid lending, the implication of the Burnside and Dollar finding is not to suggest that poor countries with weak institutions cannot be helped at all. The intention is simply to suggest that injecting more money into these countries is often not the answer, because a shortage of capital is frequently not the main problem. In fact, foreign aid aimed at achieving growth and development in these situations more often than not becomes part of the problem. Before any meaningful or sustainable aid-led growth can take place, foreign assistance must aim at catalyzing the institutional reform and cultivating the "social infrastructure" that makes growth possible. As such, in poor governance environments, donor resources are better suited to the transfer of ideas through technical assistance, expertise, and consulting services, rather than the transfer of funds.

However, it is crucial to keep in mind that there is only so much that external actors can do to foster internal institutional reform in the Third World. Given the considerable failures of past attempts to impose Western reform initiatives, such as the Washington Consensus, on developing countries, care must be taken to make foreign assistance as organic and tailored to the local context as possible. Above all, this is necessary as to ensure that foreign involvement does not come to be viewed as an ideological struggle and provoke a local backlash. As such, efforts are best catered to strengthening local civil society, and empowering people by helping them learn how to help themselves.

A lengthening of actors' time horizons will be critical to the success of this shift in thinking about the role of foreign aid. Since institutional reform cannot be achieved overnight, both donors and recipients alike must have the foresight to devise long-term solutions, the diligence to implement them, and the patience to await their slower but more sustainable outcomes. This thinking often appears counterintuitive because people naturally view positive feedback as an indication that their efforts are working, and tend to grow weary when these results do not appear quickly. Precisely because the outcomes of reform are much slower and much less perceptible in the short-run, reform efforts will often appear ineffective and self-defeating,

but the international community must not succumb to the temptation of donor fatigue. If this fact is simply kept in mind, the problem can be largely overcome.

It is also paramount to highlight foreign aid and assistance as a temporary measure. Current expectations that aid funding will always be forthcoming play a significant role in engendering the moral hazard problem that plagues many aid-dependent countries, which in turn leads to poor incentives for self-help, and the selection of unwise or risky policy design. If, however, aid is portrayed as a temporary form of financing that will gradually be phased out according to a known timeframe, there will be built-in incentives to create and nurture productive, self-sustaining investments and adopt constructive policies.

## Conclusions

Sound policies and good economic management matter more than foreign aid for developing countries. As the record shows, without good institutions, aid is likely to have a detrimental impact on the quality of governance in a recipient developing country. In the absence of these strong institutions, assistance efforts should be dedicated to improving the quality of governance before they can be effectively devoted to any economic development effort.

Finally, foreign aid transfers should henceforth pledge to abide by the Hippocratic oath to “do no harm.” Although more progress has been made over the last 50 years or so in alleviating poverty than during any comparable period of time in history, poverty remains a huge global challenge. Over one billion of the world’s people continue to live in conditions of absolute poverty, subsisting on less than \$1 a day. There are aid agencies all over the world whose mission, they say, is “to help the poor in the poorest countries”. Public budgets and private donors in the world’s most powerful countries allocate billions of dollars to these “benevolent operations”. There is rarely a year when some oppressed countries, especially in Asia, Africa and Latin America are not faced with a food crisis due to a natural disaster or war. Globally, between 800 million and a billion people are chronically hungry. Some 25,000 people die every day due to hunger and related causes.

As such, even if development economics have not yet found ways to help them, global actors should at the very least take every effort not to make their condition any worse. If foreign aid is harming rather than helping them, then it is clearly in need of being restructured, such that policy and incentives can be better coordinated to achieve the desired outcomes. In the meantime, research efforts must continue to search for the answers.

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# 6

## **A bottom up aid effectiveness approach:** the case for grassroots level accountability

–Simone Galimberti

### **Synopsis**

*In the last few years, the global discourse on aid effectiveness has been strengthened with tangible actions by the major stakeholders both in the South and in the North of the world. Formal deeds were indeed taken with the signing of the Paris Declaration and followed by the Accra Agenda for Action, one of the boldest attempt to renew and improve the way aid is not only managed but also deliver.*

*While recognizing the urgent need for a comprehensive review of the global aid architecture, this essay is more focused on the links between aid and accountability and how the discussions on aid effectiveness should not only focus on global donors and government but rather start involve the non state actors alias civil society organizations on the ground that are in charge of the delivery of the aid. At the same time, the essay tries to bring into light innovative practices that have the potential to rewrite the role of accountability in the way aid is delivered and in a much better way.*

*The Essay makes the case for a global and national discourse on micro aid effectiveness through enhanced mechanisms at local and national levels. This bottom up approach might lead to the implementation of a Global Compact on Grassroots Aid Effectiveness.*

As the Busan summit on aid effectiveness is approaching, the global attention has once again turned on discussions on how to make the best use of aid, still considered as one of the major tools to lift millions of people out of poverty. In the last years, there has been a great deal of debates on the relevance and impact of aid support to developing countries.

The cause-effect nexus between aid and economic growth, the latter more and more being considered as the real engine to take millions of people away from poverty and misery is being questioned.

Indeed those doubting the positive effects of aid over the overall economic growth of a nation should be reminded at the same time that aid tends to perform better in social rather than economic sphere of development, especially in sector like education and health.

Still wealth creation is the latest jargon on used to demonstrate a tectonic shift in the perceptions of how aid should be designed and delivered. Traditional sector of support like education and health, are no more dictating how aid is being spent in the recipient countries. In few words, aid is being pushed outside its “comfort zone”.

In this scenario, we witness, on one hand, the rise of new form of aid, more focused on social innovation and on other hand, we see attempts to reform the way that traditional aid is managed and spent.

Within the above mentioned second trend, there is the case for a more and better accountability by civil society organizations engaged at grassroots level.

### **Traditional versus new forms of support: towards some form of complementarities**

The agenda of aid reform set by the Paris Declaration is based on ways to improve the existing framework rather than thinking out of the box with some new ways of delivering aid. Far from advocating for a global “*Occupy the Aid System*” movement like the ongoing protests against the financial systems all around the world, there is unfortunately no space to truly speak about different ways for doing aid, although there is an increasing recognition of the need of having smarter ways of doing aid. Actually the new trend is a kind of antithesis of the concept of aid itself: more than aid the focus is on a new wave of mixed approaches that work according to the market but are driven by social missions. In some aspects, we are in a transition time where new actors and players, like foundations, are emerging and a kind of introspection on ways aid is delivered and designed is underway at all the levels. The economic crisis in most of the western countries is also taking its toll in bringing in more efficiency in the sector, especially among the international civil society organizations.

The *Bellagio Initiative*<sup>1</sup>, promoted by several big foundations well reflects the current situation as it attempts to explore the future of global philanthropy

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1. [www.bellagioinitiative.org](http://www.bellagioinitiative.org)



with the overall purpose of setting new scenarios where foundations and charities can be able to perform better. The initiative although neither principally focused on aid effectiveness nor on accountability is important because it lays the ground for innovations in charity sector, setting priority areas of interventions and aid governance and aid delivery will definitely play an important role in defining the most promising ideas.

This kind of soul-searching can positively influence the current debate on aid system restructuring as foundations are already significant players that compliment the official ODA assistance.

While there is strong evidence that new thinking focused on new approaches and triggered by innovation will constitute a truly “lift” towards prosperity for millions of people at the bottom of the society, the traditional ways of aid delivery is still a reality. We need to make the best out of the existing framework and advocate in such a way that smarter ways of helping others might become, in future, the only acceptable modality.

On this line, a recent report from ActionAid, *Real Aid, ending aid dependency* offers a fresh look at the quality of traditional aid that positively can count also on good practices and modalities, defined in the report as key elements that make the “real aid” effective. The findings are encouraging enough to depict a scenario where an increasing number of recipients’ countries have raised their level of ownership on the way aid is managed at country level. The report therefore offers some rationale for proving the positive impact that the aid can have if implemented in the “right way”.

For this reason, the relevance of Busan Meeting that will try to build more consensus for walking the talk in the commitments taken in Accra.

## **Innovations for better results in the traditional aid system**

Indeed, within the aid sector, there are several attempts of moving forward the agenda of the “real aid” with several initiatives to reform the way aid is managed and delivered.

While the nature and scope of these attempts differ from each other, varying from ensuring effective outcomes to increasing the level of accessibility to public information, they are all striving to reform the way aid is delivered through stronger focus on outcomes and transparency.

The *Cash on Delivery* model, a new approach based on awarding successful outcomes of development actions. It has been conceptualized by the *Centre for Global Development*, offering a response to the critics of traditional aid system. This approach tries to link the satisfactory delivery of services not only with the implementation of the planned activities but also with satisfactory utilization of the grants. The idea is simple: donors will pay the grantees once the job is done that means the outcomes have been reached. A formal contract will be signed between the donors and recipient that will set out the working modality of the agreement. The focus is no more on inputs but rather on outcomes and the payments will be done based on the actual performance. Interestingly, several feasibility study have been

conducted in Malawi, Liberia and Ethiopia, offering external development partners guidance on how they can embrace this new model while DFID/UK is piloting a new project based on the Cash on Delivery model in the educational sector for Ethiopia.

Shifting to the vast area of transparency, many innovations are taking place. One of the major initiatives at international level remains the International Aid Transparency Initiative, IATI that strives for creating common reporting and information publishing system to be used by the external development partners in order to make aid data more accessible and comparable. The overall goal of IATI is to make information about aid spending easier to access, use and understand. For this purpose, two set of standards have been set: the activity standard and the organizational standards. The former is designed for reporting the details of programs or projects while the latter is aimed at reporting the future budgets of organizations and forward planning budget. Currently DFID, Hewlett Foundation and WB already subscribed to the IATI initiative and possibly more civil society organizations will be attracted by these standards.

Strictly linked to IATI, *Publish what you Fund Campaign* is pushing an agenda based on 4 basic principles for making aid information more accessible:

- 1) *Information on aid should be published proactively,*
- 2) *Information on aid should be timely, accessible and comparable,*
- 3) *Everyone has the right to request and receive information about aid,*
- 4) *The right of access to information about aid should be promoted.*

The Campaign is clear and straightforward to endorse and practice the principles of the right of information, readopted to the context of aid development.

*AidInfo* is another initiative by *Development Initiatives* in the UK that believes that “*poverty reduction will come about more quickly, when information about aid can be accessed quickly, easily and cheaply*”. This means that aid money can be tracked, adequate project feedback given and that government and donors can be held to account. *AidInfo* therefore tries to understand effective ways on how aid data can be better organized and compiled and how these efforts would lead to better aid.

Lastly, another interesting initiative, although not restricted exclusively to the aid sector, could have positive implications on aid transparency.

The *Open Government Partnership*, recently launched, is the government led initiative promoted by Brazil, Indonesia, Mexico, Norway, the Philippines, the South Africa, the United Kingdom, and the United States. The Partnerships aim at making the state mechanisms more transparent and accessible to the citizenry and it can be considered as a comprehensive response of the North and South governments to the increasing *Right to Information* movement that is spreading all around the world. In the Open Government Declaration, the signatories’ parties “*commit to making policy formulation and decision making more transparent, creating and using channels to solicit public feedback, and*

*deepening public participation in developing, monitoring and evaluating government activities.” Interestingly the Open Government Partnership offers ample venues for engagement and cooperation with the civil society as the members of the Partnership “commit to protecting the ability of not-for-profit and civil society organizations to operate in ways consistent with our commitment to freedom of expression, association, and opinion and commit to creating mechanisms to enable greater collaboration between governments and civil society organizations and businesses”.*

## **Accountability and aid effectiveness**

The above mentioned initiatives if scaled up and implemented up to their full potential, can significantly bring more and better development. A focus on effective outcomes as promoted by the Cash on Delivery model and a greater emphasis on accessibility of aid data can bring more people, especially the beneficiaries, to better understand aid development and the way it is spent. This will bring more oversight, participation and consequently will make aid more participatory and effective.

Indeed, we should not forget that *“Although the Busan meeting is a forum on aid effectiveness, the ultimate aim is effective development”*<sup>2</sup>. Unfortunately, there is probably something missing in the global debate on aid effectiveness: effective aid will be achieved when the accountability agenda will be fully endorsed through a new bottom up process that put the common people in the driver seat of the developing agenda. This citizen centered method could be implemented through practical, no nonsense steps that will bring in much more efficiency and legitimacy to the development efforts.

There are many definitions and literature abound on the significance of accountability. Interestingly, the researches of the Civil Society on Accountability Principles and Practices<sup>3</sup> published by the Commonwealth Foundation, *“found that while the specific ways in which accountability is practiced vary from country to country, the underlying principles are the same”*

We all know about the bottom line when we talk about accountability. It is intrinsically about exercising effectively our responsibilities as development actors. Accountability, in its pure essence, is about common responsibilities to deliver the best service at the best value for money, with highest level of participation of the local beneficiaries. As consequence of the exercise of this primary responsibility, the communities will be empowered and encouraged to get involved in all the phases of the program/project.

Being able to exercise such primary responsibility will make aid more effective and as its consequence, the communities will be empowered and encouraged to get involved in all the phases of the program/project.

2. Homi Kharas, *Noam Hunger, ‘A serious Approach to development: towards success at the high level forum on Aid effectiveness’* Brookings Institute.
3. The Commonwealth Foundation, <http://www.commonwealthfoundation.com/LinkClick.aspx?fileticket=paVn5jldLOQ%3D&tabid=316>

Only going to the core of accountability process, we will be able to achieve sustainable, democratic aid led development.

### **A bottom up approach: grassroots and national level accountability**

While in many countries, an increasing percentage of resources are being directly channeled through the recipients' government in forms of budget support, itself an indicator of major ownership and effectiveness, still considerable resources are being managed by civil society organizations, international, national or locals out of the national budgets.

Weak coordination, even weaker monitoring and evaluation framework are normally the realities in most of developing countries. Regulatory frameworks might be in place but their implementation is still sluggish and patchy.

What is needed here is some sort of self regulating framework that recognizes, at least in certain circumstances, the added value of non state actors in directly serving the population within a clear, transparent set of regulations laid by the government. On other hand, keeping open in mind this ultimate goal, a set of voluntary interventions agreed by non state actors and the state should be pursued.

Therefore the time is ripe for a strong action, something ambitious, a *Global Compact on Grassroots Aid Effectiveness*, a Busan for grassroots quality aid. In order to make this compact a reality, we need to review the roles and responsibilities of civil society organizations, international locals, community based, in their efforts to bring development in the local communities. What might emerge from this new understanding is a set of principles and practices that should be voluntarily followed by those stakeholders involved directly or indirectly in the implementation of aid at grass roots level. The scope of the Compact should be wide and broad and with a certain room for flexibility in its implementation.

A bottom up approach will ensure that the Global Compact will take shape on the foundations of local or national compacts able to capture the different realities in the recipient countries. The local dimension will help setting international benchmarks for the implementation of national levels compacts that are based on the micro dimensions, helping to define standards for the national and global accountability standards

### **The National Compact on grassroots level Aid Effectiveness**

The frameworks at countries level should reflect the domains of the Paris Declaration, nominally *ownership, alignment, harmonization, results, and mutual accountability* although a great level of flexibility and adjustment will be essential in order to reflect the local dimensions.

The efforts at national level should recognize the strategic importance of data and information availability on how a determined activity or project is being implemented. Indeed quality data is a backbone of global aid effectiveness debate but so far not much has been said on which kind of information should be made accessible to the people. The compact should

offer a minimum denominator for sharing and dissemination of information like time frame, progress report and the most essential and relevant financial disclosure, including the budget.

In the case of ownership, the compact should offer guidance on ways to engage local communities and beneficiaries, setting minimum standards for real community level participation and oversight in all the phases of implementation of the project/program. The standards should guide the implementing organizations on how to deal effectively with the beneficiaries beyond the magic “wands” of the *rural or rapid participatory appraisals*.

Community ownership means empowering local beneficiaries in having a considerable say in the way programs and activities are managed, offering them the right but also the opportunity to access to a new platform for participating, monitoring and evaluating the outcomes of the program/projects. How should the implementing civil society organizations get formal feedbacks from the communities in which the program/project is implemented? Should the implementing organizations at least ensure a reasonable number of gatherings to inform and update the beneficiaries on status of implementation?

These practical questions, if properly addressed, will offer a real opportunity to “democratize” the way aid is delivered.

In terms of alignment and harmonization, the compact should prescribe minimum practices and procedures to ensure how a new intervention, regardless of being small or big, will really fit in the local priorities set by the district authorities, ensuring that the new assistance will be directed to geographical areas prioritized by the local authorities. The wisdom and common sense on how avoiding unnecessary duplication and overlapping with other not-for-profit-agencies should also be incorporated in the compact.

At large, the Compact could also work in terms of “check list”, highlighting the necessary steps and good practices on how to select a new project area, indicating the minimum level of necessary information before deciding to start new activities.

Due relevance will be also given on the way to engage local government offices and in case of a partnership framework being used in the country, the compact should spell out best practice on how international non state actors and national and local organization can forge partnership agreements.

In the domain of evaluation, the compact should mention accountability tools like social audits, client/beneficiary satisfaction survey. Social audits should be seen not just as one off event but as a long term process that includes local communities, partner organizations, local and central authorities. Social audits at grassroots level should be accompanied by central level forums and both levels of consultations should be seen deeply complementary to each other. Alignment with national policies on social audit, if in place, should be ensured.

Indeed it is required to think of “silos” mindset as the social audit process

at local level carried out by a national or international non state actor could also contribute and support the overall process of accountability of the local authorities. This is the real meaning of “mutual accountability”.

The compact, in few words, should be intended as a practical tool rather than a regulatory instrument, offering a clear guidance on essential steps to be followed in order to ensure the delivery of the best aid possible, at the best value of money with full involvement of local stakeholders.

### **The role of civil society in the quest of accountability: filling the gap?**

The big question remains if the national civil societies around the world are ready not only to step up their watchdog role for improving the quality of aid but are also keen to play at the best their new status of equal development partners as proclaimed by the Paris Declaration.

As a matter of fact, looking at the level of consciousness and awareness taken by the civil society, the premises are encouraging. One of the aspects in which the Paris Declaration on Aid Effectiveness has been truly innovative is the formal recognition of civil society organizations as equal partners in the development process. Accepting the civil society organizations as development partners represents a new building block in the foundations of a new aid system. Since then, the role of global civil society from north to south and from south to south has been increasingly more and more adamant in channeling its voice in the global stage of aid development effectiveness.

At the same time, there is another dimension that offers tremendous space for civil society to act and not only watch on the implementation of aid effectiveness agenda. Indeed, with the Paris Declaration, the CSOs are now forced out of their comfort zone, from being mere observers in their advocacy efforts for aid effectiveness to being truly considered as equal development partners, therefore equally responsible to perform a better way of aid.

This might mean to go through some self introspection with the required courage to review and re-discuss their working modalities. In this exercise, obviously some might lose out.

In fact, at the end of the day, there is still a high level of inefficiency when we look at the coordination and cooperation mechanisms of the civil society organizations working at the implementation level. Better coordination and division of “labour” will bring less duplication and overlapping and this might bring many actors out of the game.

These constraints should not however be an obstacle to a frank debate on the status of aid at local level: Indeed, there is an urge to come up with a new debate on micro level accountability, something that interpret the principles of higher development forums like Accra and Busan and turn them in practical, actionable, doable actions.

For this reason, a new understanding must emerge on roles and responsibilities of development partners at implementation level. Indeed there is a widening gap between the targets set in the Paris Declaration and

the actual implementation of development aid at local and grassroots level.

Fortunately, the constitution of the *Multi Stakeholders Team on Civil Society Development Effectiveness*, formed in April 2009 within Cluster A (Ownership and Accountability) under the Working Party on Aid Effectiveness of the OECD-DAC, is definitely a giant step ahead.

Here is the real catch: CSOs can keep on demanding increased aid effectiveness but at the same time they have the unique position to lead the way for bottom up accountability that is complementary to the top down approach emerged from the Paris Declaration.

Following up on the Economist's provocation on "*who guards the guardians*", Kumi Naidoo, CEO of Civic Alliance well expressed the dilemma of representation and legitimacy of civil society organizations in a lunch time address at UN Headquarters in 2003<sup>4</sup>

Naidoo points out to the fact that the demand of accountability for CSOs are a sign of maturity of the sector and the time might be ripe for an array of actions that will help CSOs to become more and more accountable like self regulations mechanisms (social audit being one of them) and others standards for actively disclosing information on aid.

The key is that more and better accountability is a precious ingredient to increase and enhance the level of credibility of CSOs. Importantly Naidoo makes a great contribution when he distinguishes between different forms of accountability depending on the size, nature and scope of the CSO" *The way in which a local NGO, working to improve health service delivery within a community, would work towards its accountability would differ greatly from the demands on a transnational human rights association, for example*".

In the same framework, Naidoo affirms that *there can be no universal approach to the issue of CSO*

*Accountability and no magic framework*". Great flexibility is therefore required for civil society organizations from the North and South to live up to the principles and ideas of an accountable aid framework.

Self Accountability, aid effectiveness among non state actors Standards: the international scenario

Around the world, there have been several encouraging attempts that prove the seriousness of the civil society going on the right path when we talk about accountability and aid effectiveness.

The work done by *One World Trust* in partnership with *Commonwealth Foundation*<sup>5</sup> can offer an interesting starting point: Non state actors in several countries and regions (Brazil, India, Uganda and South Pacific region) were engaged in discussing practical ways to enhance their level of accountability, setting a common agenda through the preparation of country wise toolkit aimed at assisting local organizations in putting accountability into practice. This international project identifies common principles of accountability thanks to the identification of existing good governance practices already

4. Civil Society Accountability: "Who Guards the Guardians?", 3 April, 2003

5. <http://www.commonwealthfoundation.com/Areasofwork/Governanceandaccountability>



and providing practical steps to enhance the CSO's level of accountability in their daily work. The toolkits offer a great deal of easy understanding on how to practice and experience accountabilities through high level of country ownership.

Going further, we also have example of self certification of accountability standards. The civil society in Uganda came up with the NGO Quality Standards<sup>6</sup>, a self regulating instrument launched in 2006 that has been devised to promote compliance and adherence of local actors in incorporating and implementing agreed ethical standards and operational norms. This is one of the most advance examples of voluntary framework adopted by the civil society based on 59 standards out of which 32 are considered as minimum. The process leading to a certification process based on three levels provisional certificate, certificate and advanced certificate.

Another incredible self assessment tool is PQASSO<sup>7</sup>, Practical Quality Assurance System for Small Organizations that was designed in 1997, offering three levels of achievement against 12 quality standards areas. All organizations should meet the first level, while organizations that are more developed or have more resources should opt to achieve compliance with levels 2 or 3. The PQASSO standards have been developed in the UK but they have been also adopted in other countries including India and Bangladesh. Currently in UK, the Charities Evaluation Services' is the licensed body that officially certifies the adherence to the standards through a PQASSO Quality Mark. So far 100 British organizations have successfully gained the quality mark!

Interesting also at the policy level, something is happening in the runner up to Busan. The *Open forum for CSO Development Effectiveness* prepared *The Istanbul CSO Development Effectiveness Principles*<sup>8</sup>. This could be an interesting framework although it shies away from any bold and more detailed commitments: only the principle 5 "*CSOs are effective as development actors when they demonstrate a sustained organizational commitment to transparency, multiple accountability, and integrity in their internal operations*"

Following on this first important step the *Open forum for CSO Development Effectiveness* came out with a stronger commitment "*The Siem Reap CSO Consensus on the International Framework for CSO Development Effectiveness*"<sup>9</sup>. The framework is intended to guide the practical implementation of the Istanbul Principles, offering some more specific commitments. Interestingly, the consensus expressed clearly the principle that promoting public accountability and transparency practices "*increase CSOs visibility and credibility*" while at the same time, it focus on "*mutual and multiple accountabilities*" and has strong opening towards provision of

6. [www.ngoforum.or.ug/index.php?option=com\\_docman...](http://www.ngoforum.or.ug/index.php?option=com_docman...)

7. <http://www.pqassoqualitymark.org.uk>

8. [http://www.cso-effectiveness.org/IMG/pdf/final\\_istanbul\\_cso\\_development\\_effectiveness\\_principles\\_footnote.pdf](http://www.cso-effectiveness.org/IMG/pdf/final_istanbul_cso_development_effectiveness_principles_footnote.pdf)

9. [http://www.cso-effectiveness.org/IMG/pdf/final\\_framework\\_for\\_cso\\_dev\\_eff\\_07\\_2011-3.pdf](http://www.cso-effectiveness.org/IMG/pdf/final_framework_for_cso_dev_eff_07_2011-3.pdf)



“timely, accurate and accessible responses to public information requests”. The consensus also defines accountability as maximizing efforts to take into account the views of people living in poverty.

The Siem Reap Consensus strongly refers to the opportunities highlighted by the *Multi Stakeholders Team on Civil Society Development Effectiveness’s Key Message for fourth High Level Forum on Aid Effectiveness*<sup>10</sup> that underlines the importance of having an enabling environment for deepening the aid effectiveness of CSOs. The *Key Message* demands a strong cooperation with the donors that should “encourage” the creation of conducive scenario for a positive change in the way aid is delivered at local level.

All the above mentioned examples show that the process of engaging CSOs in not just talking but also delivering accountability and aid effectiveness has kicked off although much more could be done.

## What’s about Nepal?

### *The Accountability agenda in Nepal*

Nepal is considered a best practice in the international arena for being able to create the conditions for better quality aid being implemented in the Country. This has been possible thanks to a strong commitment by the Government of Nepal towards the agenda of aid effectiveness, embraced also by the external development partners ready to enhance the country system and mechanisms with more and more assistance channeled through direct budget supports like in the educational and health sector. As sign of maturity, the upcoming *Nepal Portfolio Performance Review (NPPR)* of the aid assistance to the country, to be held on 17<sup>th</sup> and 18<sup>th</sup> of November, will raise the important issue of “mutual accountability” that will also look at the joint responsibilities of the external development partners in strengthening the country system and improve the overall quality of aid delivered to Nepal.

This is definitely a milestone for the Nepal and proves the strong willingness of the government to use and mobilize aid at the best interest of the country. Outside the official donor assistance, the scenario is different with most of international non state actors not able to include their financial contributions in the *red book*. Strong voices have been raised against the lack of transparency and effectiveness of international organizations working in the Country. An effective coordination, monitoring and control system is still lacking with deep gaps between central and district levels authorities.

Positively there is also some good news as the Social Welfare Council, the body within the *Ministry of Women, children and social welfare affairs*, is opening up regional offices in order to better monitor and evaluate the work of international and national non state actors. Still coordination problems with line ministries at district and regional level will remain. For this reason the launch of a *National Compact on Grassroots level Aid Effectiveness* can offer a venue to accommodate the demand for better aid effectiveness,

10. [http://www.cso-effectiveness.org/IMG/pdf/final\\_key\\_english\\_c3.pdf](http://www.cso-effectiveness.org/IMG/pdf/final_key_english_c3.pdf)

helping non state actors active in Nepal to pursue some sort of voluntary self regulating framework that will enhance their overall level of accountability, therefore increasing and ensuring more and better effectiveness and efficiency in the development process.

While the focus on supporting an improvement on current legal and regulatory framework should not be reduced, through a Compact, the non state actors in partnership with SWC, the regulatory body for non state sector led development, can encourage the compliance of *minimum standards* on how to improve the delivery of aid at local level.

Below are some examples of standards that could be included in the Nepal Compact:

### **Transparency:**

Minimum practices in the ways programs and activities are reported to local communities and stakeholders, including setting of standard tools (social audit, score cards etc) to be used in order to provide clear oversight on the implementation of the activities; quality and relevancy of information and data provided to local communities/beneficiaries and local stakeholders on program/project, proactively implementing the principles underpinning the Right to Information.

*AidInfo* is also looking with interest at the current situation in Nepal having recently organized a workshop on accountability and transparency in Kathmandu. *AidInfo* with its technical expertise could be instrumental not only for supporting the current process of aid related info dissemination among stakeholders at the highest level but could also supporting the national efforts in favour of the creation of standards on micro level aid data sharing where the local communities will be the first users.

### **Coordination:**

Avoidance of duplication and overlapping with a set of standards for coordination at central and district level in the planning and during the execution of program activities, including division of labor among non state actors

### **Ownership:**

Minimum set of standards regulating the level and quality of participation of local communities/beneficiaries in planning, implementation, monitoring and evaluation. The standards should offer some benchmark on ways to engage and involve the communities and beneficiaries during the different phases of project cycle

### **Partnership:**

Being Nepal a country where international non state actors are working together with local and national organizations, the issue of partnership, key.

Minimum standards for creation of partnership should be ensured, offering benchmarks on ways to engage local partners and local communities in a transparent and effective ways, including their selection and working modalities. (The standards will bring together the existing frameworks within AIN, NGO Federation etc like the different partnership guidelines).

Under this framework, the civil society organizations, both national and international will voluntary decide to adhere to certain standards to be observed and practiced while supporting or implementing the delivery of social-economic activities for the benefit of the beneficiaries. The agreed minimum standards will not only be complementary and respectful of the existing legal provisions but also will help the GoN to better ensure development outcomes according to the national priorities.

### **How to achieve it?**

A National and regional level dialogue could be initiated in order to collect ideas, analyze current concerns and bottleneck. As part of the consultation process, a series of Accountability Forums (at least one at central level and one in each development region) could be held where district level authorities, representatives of non state actors will discuss ways to improve their working relationships. A final central level dissemination meeting would be held, offering the engaged parties and broader stakeholders a forum for discussion. From this point onwards, a working group could be created with the aims of short listing the most important propositions based on the principle of “doability” and practicality.

The selected propositions will be reformulated as a set of standards that will lead to the formulation of the *National Compact on Grass Root Aid Effectiveness* to be officially endorsed by the engaged parties. Are the conditions ripe for such level of initiative in Nepal? Are the national civil society and international aid community, especially international non state actors ready to go the extra mile in order to have better aid implementation and consequentially being able to achieve better outcomes?

Undoubtedly, lots of awareness should be promoted in order to meet the conditions for setting up this process and at the same time the case for better aid at local level should be promoted by external development partners who can push softly the international and national non state actors in embracing the case for aid accountability at local level. As we saw before, the current discussions leading to Busang clearly identify the role of institutional donors in encouraging a more accountability conducive framework. In this way international and national civil society start feeling a certain level of urgency in making their work better and more accountable.

### **Towards a CSO Nepal Aid Effectiveness Forum?**

Given the different nature of actors, national, local, grassroots and international involved in the implementation of aid in Nepal, a new innovative forum could be promoted in order to initiate the national process leading to

the establishment of the National Compact. The Forum should be a loose platform, as informal as possible and as inclusive as the current discussions want aid to be. The representation of National, International, local organizations should be ensured together with institutional stakeholders, starting from the Government of Nepal and external development partners. The issue of representation could be a thorny one but the door should be open to all organizations willing to work on practical and result oriented way. Those interested to work on a better aid framework at local level should be welcome.

The risk to use this Forum for old and present recriminations is real one and a simple code of conduct could be prepared in order to better clarify the purposes of the Forum. Those willing to join the Forum will be compelled to sign up the code of conduct, leaving out any space for bickering on false misunderstandings.

This will not be an easy endeavor as historical differences among stakeholders might impede the kick off of a serious national debate. Self interest might prevail in order to derail the entire process. Not only the external development donors should play an active role but also the Government of Nepal through the Social Welfare Council. The final outcome might be uncertain but it is worthy a try.

## **Towards a Global Compact**

In quest of establishing the national compacts, the *Global Compact on Grassroots Aid Effectiveness* could offer minimum standards for bringing aid effectiveness at local level through a set of principles and benchmarks. The methodology should be clear with a bottom up approach prevailing through discussions for a Global Compact being held among different national civil society platforms that already have come up with a set of national compacts. *The Siem Reap CSO Consensus on the International Framework for CSO Development Effectiveness* could be a good base for discussions although it will need legitimacy at country levels through tangible results in enhancing local accountability framework.

At the same time, once a substantial “*Coalition of the Willing*” will emerge from developing countries, there will be the scope to discuss the global framework that once finalized could offer a global benchmark for the civil societies around the world who are still lagging behind in the quest for a national pact on local aid effectiveness.

The Global Compact should be detailed enough to ensure consistency in the final pursuit of better aid at local level but should not be prescriptive and should offer wide margins of flexibility and re-adaptation for local interpretations. National compacts emerging from the Global Compact will have the flexibility to be shaped and nourished according to their own national features and context.

The existing civil society networks currently involved in the aid debate should take the lead in discussing and framing the Global Compact. Are they really ready to take up this challenge?

Nepal is obviously in a good position to show and lead the way in moving forward the agenda of better and more “real aid” at local level. The conditions are well set for a new approach that builds on the existing will of the Government to improve aid effectiveness. Only if civil society organizations, regardless of their status will agree on working out practical ways to improve their work at local and grassroots level, Nepal will be able to fully take advantage of a new, strengthened “mutual accountability”. The citizen of Nepal will be the real winners of this bold move.

# 7

## Aid Effectiveness and Nepal's road to Busan

-Vidyadhar Mallik

### **The Agenda of Aid Effectiveness – A Global Commitment**

Aid effectiveness is about delivering aid in a way that maximizes its impact on development and achieves value for aid money – progress on effectiveness requires greater accountability on the part of donors and developing countries – towards their own taxpayers and towards each other – for the development commitments they have made. (Aid Effectiveness, 2011)

At the beginning of the 21<sup>st</sup> Century, it became quite clear that aid resources have to be managed better. In 1996, OECD/DAC came up with a report called “Shaping the 21<sup>st</sup> Century: the Role of Development Cooperation” which set out the basic concepts of aid effectiveness. The Millennium Declaration of 2000 endorsed MDG-8 which is on ‘Global Partnership for Development’. In 2002, Monetary Financing for Development Conference agreed on financing targets to achieve MDGs and called for a more effective way of aid disbursement to ensure these resources make the maximum impact on development. In 2003, in Rome High Level Forum (HLF) on harmonization, donors agreed to improve in-country coordination so as to reduce transaction costs for aid recipients. The HLF -2 Paris, in 2005, adopted “Declaration on Aid Effectiveness” whereby donors and developing countries agreed on 56 action-oriented commitments aimed to improve the quality of aid and to monitor the commitments against 12 indicators. Aid effectiveness indicators were monitored in 2005, 2007 and recently in 2010. In 2008, HLF -3 took place in Accra with the adoption of Accra Agenda for

Action (AAA). All development actors – DAC and non-DAC donors, developing countries, CSOs, parliamentarians and global partnerships agreed on actions needed to accelerate achievements of the Paris Commitments.

There has been a change in the behaviors of donors and developing countries since 2005. The norm has come to stay that aid recipients discuss their national development strategies with their parliaments and electorates (ownership); donors support these strategies (alignment) and work to streamline their efforts in-country (harmonization); development policies are directed to clear goals and progress is monitored (managing for development results); and donors and recipients are jointly responsible for achieving these goals (mutual accountability).

The Fourth High Level Forum (HLF-4) on Aid Effectiveness will be held in Busan, Korea in November 2011. It will take stock of what has been achieved, identify areas for concentrating efforts and set aid quality framework for the remaining years to the MDG target date of 2015. Developing countries' list of priorities for HLF-4 is predictability aid flow, use of country systems, removal of policy conditionality, country-driven capacity development, mutual accountability and reduction of transactions costs. HLF-4 will also focus on value for money and raising aid quality. Many countries and institutions want to look at 'development effectiveness' and not only 'aid effectiveness' – a discussion that brings round to all factors that support development – aid, country's own resources, policy coherence for development, the private sector, etc. (Aid Effectiveness, 2011)

Some of the challenges and threats under discussion in view of Busan Forum are: 1) Focus on the essential and get rid of the noise – set the aid quality framework leading to 2015, 2) Donors should focus now on delivering some 'low-hanging fruits' including on aid untying, predictability, removal of policy conditionality and transparency, 3) Keep momentum – do everything you can, 4) Deliver on existing pledges – avoid proliferation of new commitments and 5) Better accountability and communication to win support. (Aid Effectiveness, 2011)

## **Foreign Aid Policy in Nepal**

Nepal's development finance began receiving foreign aid from the 1<sup>st</sup> Five Year Plan, 1956 -61. Since then a substantial portion of development expenditure somewhere about 55% per annum (5-6% of GDP) has been financed from foreign aid. Foreign Aid Policy, 2002 (F A Policy, 2002) came into effect following elaborate consultations with all stakeholders including the development partners (DPs) and adoption during Nepal Development Forum 2002. The guiding principles of the 2002 F A Policy are: 1) Foreign Aid will be directed towards achieving the overarching national goal of poverty reduction. This will involve fostering economic growth by enhancing productive capacity of the economy as well as supporting critical social infrastructure needs. 2) FA will be linked with the sectoral objectives. 3) F A Policy forms an integral part of the overall policy of mobilizing resources. 4) The F A Policy will ensure greater transparency at both the ODA supply

level and user level within and outside the Government system. 5) The Government will try to achieve self-reliance in the longer term by enhancing domestic resource mobilization while increasing quality and quantity of F A during short and medium term. (Foreign Aid Policy, 2002)

FA Policy 2002 lays emphasis on concessional loans and grants, budgetary supports, putting in Nepalese resource persons in the technical assistance provided by donors, one door policy for supports through INGOs and NGOs, emphasis on domestic resource mobilization, leadership and ownership of GON, supportive role of Nepalese civil society, building national capacity and partnership, soliciting an increased level of cooperation from donors, better understanding of donors with respect to sensitivity, selectivity, avoiding trial and error methods, maintaining financial discipline, reflection of financial sources in the Annual Budget and improving donor procedures (harmonization). (Foreign Aid Policy, 2002)

Some strategies have also been discussed in the F A Policy, 2002 for the implementation of policies adopted. Major strategies are: Formulation of Economy-wide and Sectoral Perspective Plans, ensuring transparency and accountability, enhancing the quality of aid, strengthening aid coordination, project/ program identification, selection, design and securing sustainability, creating a foreign aid MIS and promoting institutional effectiveness. (Foreign Aid Policy, 2002)

Harmonization of Donor Assistance was discussed in the Nepal Development Forum, 2004 (NDF, 2004). A draft paper and national action plan on harmonization of donor assistance was presented in the NDF, 2004, based on Rome Declaration, 2003. Need of harmonization of donor assistance at three tiers in Nepal, namely, harmonization at the overall program level, harmonization at the individual program level and harmonization at the financial modality level was felt. Aid integration process was highlighted with focus on support to PRSP and sectoral policies and harmonization in terms of joint programming, common procedures, common monitoring and reporting formats and support to Nepalese financial management procedures. (NDF2004, 2004)

Nepal Donor Consultation Meeting was held in 2008, February (NDCM, 2008) after a gap of four years, that is to say, after NDF 2004. This meeting was also dubbed Mini –NDF, held after Peoples’ movement, to discuss popular aspirations of New Nepal, progress on Paris Declarations and peace dividend. The major issues raised and discussed in the meeting on aid effectiveness were: 1) need of support to relief, rehabilitation and reconstruction (RRR) and peace dividend, 2) rights based approach and community ownership of development efforts, 3) aid transparency, accountability and predictability, 4) national ownership and harmonization, and, 5) a double compact between the GON and Nepali people and between the GON and the donors. (NDCM2008, 2008)

Nepal Portfolio Performance Review was held on November 13-14, 2008, jointly by MOF and some donors with the theme on strengthening country systems for improved portfolio performance. A paper by the GON was



presented drawing heavily from the commitments made on Paris Declaration and Accra Agenda for Action and both the status and challenges were discussed. Basically PEFA assessment in Nepal, Paris declaration Monitoring Survey, 2008, use of country systems in procurement and progress on Public Financial Management were discussed. Practical commitments both from GON and donors were made in this meeting together with an agreed action plan to follow up. (NPPR 2008, 2008)

An effort was made in 2009 to organize Nepal Development Forum (NDF) which eventually fell through. Stakeholders’ consultation meetings were held to lay groundwork for NDF including one on Foreign Aid Policy. A draft Foreign Aid Policy 2009, was prepared and presented in the meeting for discussions. Major highlights on this draft paper included: 1) support of F A Policy to develop Nepal within next 10 to 15 years into a medium – income country, 2) help achieve a high, inclusive and just growth with focus on domestic savings mobilization, 3) prioritize investments in GON’s priority sectors and the sectors with comparative advantage and competitive strengths, 4) help in national capacity building and sustain it through knowledge and technology transfer. The draft incorporated the elements of both Paris Declaration and Accra Agenda of Actions. (Foreign Aid Policy 2009, 2009)

A revised draft named Foreign Aid Policy 2010 reinforced Paris Principles of aid effectiveness as was reaffirmed by the AAA and to be complemented by subsequent resolves (indicating towards HLF 4 at Busan as well) aiming at transparency, accountability, predictability and sustainability by enhancing national capacities, domestic resources mobilization and optimizing the opportunities for trade and investment. (Foreign Aid Policy 2010 - Revised draft for Discussion, 2010)

## 2008 Survey on Monitoring the Paris Declaration

The Key Findings of the Aid Effectiveness Survey, 2008 are as follows:

S. No.	Indicators	Results (%)
1	Aid on budget	74
2	Technical cooperation	34
3	Coordinated technical assistance	14
4	Using country public financial management system	68
5	Using country procurement system	59
6	Parallel project implementation units (number)	106
7	In year predictability	47
8	Program based approaches (budget and other support)	32
9	Program based approaches (budget support)	20
10	Joint missions	36
11	Joint country analytic work	37

The survey, in brief, found that the donor's actual disbursements are considerably less than the amounts pledged, a considerable amount of ODA does not come through the Government financial systems, donors perceive that Nepal has a limited capacity to formulate and implement development programs, leading them to establish separate PIUs and direct budget expenditure and management of procurement of goods and services.

Some suggested next steps were: 1) For Government, needs to create more incentives for donors to channel aid through country systems, performance based funding, E-bidding, PEFA action plan, capacity development plan and advocacy to untie aid, 2) for donors, donor decentralization, commonly pooled technical assistance, common monitoring and evaluation frameworks and all donors participating in NPPR exercise. (Nepal Country Report 2008 Survey on Monitoring the Paris Declaration, 2008)

In 2010, Nepal Country Evaluation, an exercise on a Joint Evaluation of the Implementation of Paris Declaration, was carried out by the Ministry of Finance and the development partners. The following are the main findings and suggestions from that evaluation work:

The efficiencies and effectiveness developed through taking a programme approach can be replicated in other sectors. The lessons from the sector programmes in education and health are applicable more widely.

*Shared learning by GoN, DPs, civil society partners and service users and beneficiaries can be of benefit.*

- A focus on results increases responsiveness.  
*MfDR has changed the way in which programmes are designed and delivered making delivery more responsive to beneficiaries and puts the individual, family and community at the forefront.*
- Just by labelling it as a 'Paris Declaration Principle' does not change what is already being practiced.  
*Through the evaluation many people discovered that what had become common and expected practice was in fact the application of the Paris Declaration principles.*
- Paris Declaration implementation has enhanced results.
- Paris Declaration principles are valid. Though it is too early to identify plausible contributions that relate to the Paris Declaration.
- The Paris Declaration is not being adopted because of perverse incentives within

Nepal and DP systems. (Nepal Country Evaluation for Joint Evaluation of the Implementation of the Paris Declaration, Phase II, 2010)

The key implications of aid effectiveness for future are described as:

Aid effectiveness is not simply about the efficient and effective institutional dynamics of aid management, it relates to the processes through which policy, strategy and service delivery meet the needs of Nepal's citizens. This requires improved institutional capacity, access to information and voice and participation at all levels.

Confidence in Nepal's procurement and other fiduciary systems can ultimately be built only by those who implement those systems. The challenge is to the accountants, managers and administrators within GoN and DP agencies to ensure that the systems are operated as designed and that inappropriate actions are challenged and addressed.

*Nepal cannot ignore climate change and must consider how it reframes the development paradigm.*

*Social diversity has been given prominence as Nepal seeks to reframe its approach to poverty. Similarly, governance and state building take on new meanings in the post conflict environment. All these cross cutting issues need to be integrated into the aid effectiveness discourse.*

*The debate around the structure of the state presents particular challenges in terms of aid effectiveness. Aid effectiveness will need to be reconfigured for the 'new' Nepal as it develops into a different 21st century state.*

*Aid effectiveness in the future will need to engage with and bring into the wider framework including neighbouring countries who still provide considerable support and assistance. (Nepal Country Evaluation for Joint Evaluation of the Implementation of the Paris Declaration, Phase II, 2010)*

## **Nepal's Road to Busan**

An online consultation, involving over 60 developing countries and 163 people, came down in support that Busan should remain focused on the Paris Declaration and AAA commitments, emphasizing the need for accountability and action to implement existing commitments. Alignment, capacity development, managing for results and transparency were highlighted as particularly important areas of the aid effectiveness agenda to date. Developing countries stated the need for their active involvement in preparations for HLF-4. (Aid Effectiveness, 2011)

In this context, the following is recommended as Nepal's road to Busan HLF-4 on Aid Effectiveness:

- 1) Preparation:** Nepal must prepare first its agenda for Busan through wide consultations with different Nepali stakeholders – which should include parliamentarians, political parties, academia, civil society and institution like AAMN which is a leading non-state actor on aid monitoring in Nepal. The delegates to Busan must come up with a single but composite voice of all the stakeholders which should include not only measures to consolidate governments' position as an anchor for development delivery but should also include diverse concerns of community groups, NGOs, local governments and the private sector as agents of change and development in this country, especially during present transition.
- 2) Agenda for Busan:** Agenda that Nepalese delegates should advocate and push at Busan should also be widely discussed with

national partners first and then with also DPs based in Nepal. Broadly that should include aid predictability, medium term support for rehabilitation, reconstruction and economic recovery and high inclusive growth agenda, donor harmonization and alignment, MfDR and country ownership. Specifically, the focus should be lowered on Technical Assistance pooling, support to domestic resource mobilization, aid for trade, capacity building and strengthening of our national systems including that of public financial management and procurement systems. Donors' commitments towards fulfilling their resource obligations to achieve MDGs and beyond should be sought. Mechanisms for incentivizing the donors to effectively implement Paris principles and AAA at local level should be discussed at Busan. A general discourse on 'Development effectiveness' rather than discussions centered on 'Aid Effectiveness' sounds exciting at this stage from both accountability and delivery perspectives. Efforts to satisfy the taxpayers of both donor and recipient countries are needed and Busan HLF-4 should go a long way in this direction.

As the time from now to Busan is very short, the Ministry of Finance and other relevant partners must start working round the clock in preparing and fine-tuning the presentations for the meetings in Busan so as to maximize the outcomes of HLF-4 on Aid Effectiveness for Nepal.

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# 8

## Aid Effectiveness and Gender Responsive Budgeting: Nepal's Experience

-Mina Acharya

**THE** Paris Declaration (2005) laid down five principles to increase aid effectiveness, namely national ownership; alignment of assistance to national priorities; harmonization and coordination of donor support; managing for development with results and transparency; and mutual accountability.

The principle of **ownership** requires engagement of citizens in national planning and priority setting processes in the country as well as ownership of the objectives and plans and programs by the respective country governments. Women are often not included in such processes and their priorities fully not reflected in the development policies and national plans. In Nepal, the grass roots women have had little voice and influence in such processes (MOWCSW\UNDP\MGEP, 2004). Only during the preparation of the Tenth Plan/PRSP (2002-2007) some consultation with women's groups from national to the regional level took place. However, they have had little influence on the budgeting process. Since the introduction of GRB in 2007/08 things are changing somewhat. Women's groups and advocates are being consulted with at least at the national level. Impact of their voice on influencing policies is still few and far between.

**Alignment** requires that donor priorities are set in consultation with the country concerned and that they are in line with the national priorities. There are several mechanisms of achieving such alignment, including Direct Budget Support, which is the support to sectors and programs that

are prioritized in the PRSPs or National Development Plans. However, when gender equality and priorities are not adequately mainstreamed in the national development plans and the budgets, donors own gender equality priority becomes ineffective. In Nepal's case such problems may not be encountered because Nepal's development plans, particularly TYIP (2007-2010) seemed to be several steps ahead of donors in its vision and goals of building a gender equitable, inclusive and just society through structural reforms, and gender and inclusion sensitive policies, strategies and programs. Problems, however, may be encountered in implementation on the part of GON and changing donor agenda and non-fulfillment of commitments made by them.

**Harmonization and coordination** of partnerships between donors and aid recipient governments is supposed to be achieved through structures that enable joint working for improved effectiveness and efficiency in aid delivery. Considering the transaction costs that the diversity of donor approaches and reporting demands places on developing countries, harmonization is a commendable initiative. The issue is to ensure adequate gender mainstreaming in these mechanisms so that gender equality and inclusion remain a priority agenda not only in planning but also in implementation.

**Managing for results requires data** to measure progress and assessment of differential impact of policies, plans, programs and development assistance against the prioritized national goals. It also requires adequate use of this information in formulation of further policies and programs. The Paris Declaration identifies twelve process monitoring indicators for measuring public financial management, accounting and auditing systems, procurement systems, results frameworks, transparency and capacity. However, originally, none of the assessment tools incorporated elements to monitor gender and social equity. The limitation of the system to monitor gender, inclusion or MDGs was acknowledged after intensive lobbying by UNIFEM, the DAC Network, and civil society organizations world over, since 2010 new gender dimension has been added to the monitoring formats.

**Transparency and mutual accountability** demands answers from public authorities on deliverance on commitments. Accountability needs to be seen in a broader frame as the accountability of public authorities, whether donors or developing country governments, not just to each other, but to their own societies.

The Aid Effectiveness Agenda has introduced and assigned increasing role to new modalities for aid – direct budget support, sector wise assistance program (SWAp) joint programs, and NGO funding. However, the declaration mentioned gender only once. The focus was entirely on financial discipline and privatization while development goals stayed only in the background. The GBA and GRB have acquired new importance in this context – as comprehensive measures to ensure adequate financing is in place for mainstreaming gender into the mechanisms and instruments

used in planning and managing general budget support (GBS) and programs with SWAps. The 50th session of the UN Commission on Status of Women adopted "Financing of Gender Equality and Empowerment of Women" as its priority theme for 2008. Nepal is obligated to include financing information in its report to the global body and Nepal has introduced GRB since the FY 2007/08.

Gender Budget Audit (GBA) relates to examination of the budgetary and taxation policies, expenditure patterns, budgetary processes and mechanisms through a gender lens. Gender Responsive Budgeting (GRB) involves ensuring that all these budgetary policies, activities and processes 1) do not impact adversely on women; 2) take into account women's interest; 3) involve women in planning and implementation of budgets and that; 4) adequate resources are allocated for ensuring gender equality goals. GRB is not about formulating a separate budget for women.

Gender Responsive Budget (GRB) exercises are expected to: 1) hold governments accountable for their commitments to gender equality and women's rights, and (2) ensure that progress on gender mainstreaming in the development programs is monitored as part of the regular annual budgeting process. One of the major deficiencies in gender mainstreaming efforts in Nepal has been lack of monitoring mechanisms and regular monitoring on gender aspects of development programs (UNFPA, 2007)

Nepal began Gender Responsive Budgeting (GRB) exercises from fiscal year 2007/08. This was preceded by a series of gender and gender budget audits (GBA) of several sectors. Thereafter a new system of budget classification was introduced, which in principle applies throughout the government, starting with specific focus on 13 ministries.

The GRB concept emerged from women's experience in the 1980s and 1990s, when the resources for social programs were cut widely following the policy dictates of the Washington Consensus (Folbre, 2001). At about this time there was emerging consensus that slow progress for women was in part due to lack of resources for gender equality programs. The Beijing Platform for Action (BPfA) (1995) advocated intensification of gender mainstreaming efforts with particular emphasis on government budgets. But change was slow. Reviews of the Beijing Platform (UNIFEM, 2002 and 2005) showed that commitments to gender equality – including the BPfA, CEDAW and UN Security Council Resolution 1325 – were not matched financially by either national budgets or official development assistance (UNIFEM, 2002 and 2005). A study by the Association of Women's Rights in Development (2005) showed that only 0.6 percent of foreign aid had gender equality as its major objective.

Under Nepal's GRB guidelines, each proposed program has to be scored in accordance with indicators developed by the Gender Responsive Budget Committee (GRBC) which is led by the Ministry of Finance. These indicators of the gender sensitivity of different activities/expenditure lines are: 1) participation in decision making roles and programme planning, 2) capacity

building, 3) benefit sharing, 4) increased access to employment and income earning opportunities and 5) reduction in women's workload. Each aspect has been allocated 20 marks. Programs scoring 50 percent marks or more are classified as “directly responsive”, those scoring 20 to 50 percent “indirectly responsive” and those scoring less than 20 percent as “neutral”. Nepal also requires all programs/projects costing more than NRs. 50 million to have a gender audit report attached.

The allocations to directly and indirectly gender responsive programs have been slowly on rise. The table below (4.1) shows the degree of gender responsiveness of the total expenditure allocations in the budget (donor and government contributions) in 2007/08- 2009/10.

### Gender Responsiveness of Overall Budgetary Allocations

GRB Classification	2007/08	2008/09	2009/10	2010/11
Directly Responsive	11.3	13.9	17.3	17.9
Indirectly Responsive	33.2	35.4	36.4	36.3
Neutral	55.5	50.6	46.3	45.7
Over all	100.0	100.0	100.0	100.0

*Table 4.1: Gender Responsiveness of Overall Budgetary Allocation*

*Sources: GON, budget speeches for respective years*

Along with GRB, the government has introduced specific interventions, such as 20 percent rebate on land registration fees for women, scholarships for girls, 10 percent rebate on income tax for women, etc.

But Nepal's GRB system has encountered difficulties in implementation both blamed at conceptual and practical capacity problems. The scoring system is conceptually sound for income and employment generating programs, but does not capture the key elements needed for gender responsiveness in other sectors. Some of the five dimensions of gender sensitivity like participation in decision-making, benefit sharing and empowerment are relevant across sectors while others such as reduction of workload and capacity building are not. Education or health programs cannot be meaningfully assessed on the basis of reducing workload. The scoring methodology does not mesh with indicators currently used in different sectors and so has not been applied systematically for classification.

In order to be fully fruitful, the GRB encompasses six steps over the different stages of the budget cycle: (a) analyzing the situation of women, men, girls and boys, including those from historically and economically



excluded groups (b) examining the gender responsiveness of the policies, programs/projects (c) assessing budget allocations, (d) identifying the gaps, estimating expenditure required to bridge gaps and reallocating the budget (e) tracking actual spending and how decisions are made, and finally (e) assessing gender disaggregated outcomes and impacts (benefit sharing, empowerment). In Nepal the GRB exercise has not systematically followed these steps and it is done on ad hoc basis. To be effective the GRB system needs to encompass the complete budget cycle and include detailed assessments of each program against the following criteria:

**Transformative:** Policies and programs must address the root causes of gender subordination and not just the symptoms. For example, many of Nepal's development interventions for women's equality were not effective because they did not address structural issues such as unequal inheritance rights, gender based violence, caste/ethnic discrimination, etc. The GRB must take a gender approach to development and improve women's status or bargaining power in gender relations by addressing division of work, resources inequality and power relations.

**Adequacy:** Allocated resources must be assessed to determine their adequacy for achieving not just formal but substantive equality. For example, it is fairly inexpensive to establish formal legal equality, but women need resources to access the legal services, and without that there can be no substantive equality.

**Non-discriminatory:** Programs can be non-discriminatory only when they recognize that women and historically excluded other groups face formal and informal barriers to accessing publicly provisioned services, and make provisions to erase those barriers.

**Monitoring system:** The GRB must have a transparent, participatory and responsive monitoring mechanism with effective indicators to track the expenditure, measure its outputs and outcomes and give feedback to the system.

Nepal's GRB encompasses both benefit and empowerment indicators but the methodology is not systematic: it is essentially a post-allocation classification at the ministry level rather than a pre-allocation exercise. Its focus has been on inputs and project targets rather than on measuring results. The methodology also needs to link GRB indicators for each sector with the institutional outputs and indicators of that sector, leaving out those that are irrelevant and adding those that are relevant to the gender sensitivity of institutional outputs.

Another big challenge in making the GRB operational is training and capacity building of the MWSCW and the Gender Focal Points (GFP)/units in other ministries as well as all planning and budgeting units in government and local self-governance bodies. This is even more important in the context of federalism and decentralization as it can affect planning, budgeting and monitoring. Similarly, capacity building efforts are needed to enable the members of parliament and sister organizations of the political parties, and non-government stakeholders on the GRB process.

So far the focus of GRB has been on the "soft" sectors targeted for integration of gender such as agriculture, education, health, local development, poverty reduction, governance and labor. The focus needs to be broadened to include other relevant sectors, particularly law, home and police, and communications. It is also crucial that all economic policies (e.g. taxation, privatization, reduction in budget deficits, management and regulations of the special economic zones, trade and exchange liberalization, and monetary policy) are filtered through gender and social inclusion lenses.

# 9

## Governing Emissions Reduction: REDD+ and Stakeholder Perceptions of Institutional Legitimacy

– Dr Tim Cadman  
– Dr Tek Maraseni

**PERCEPTIONS** of climate governance quality vary greatly amongst regime participants from the global North and South, and across stakeholder sectors, with implications for the current design and future directions in market-based approaches to climate change management. Given the predicted social and environmental problems as a consequence of climate change, it will become increasingly important to determine whether the policy programmes aimed at reducing greenhouse gas emissions are solving the problem and changing behaviour, or whether they are in fact contributing to perverse outcomes.

This paper presents a framework of principles, criteria and indicators for the evaluation of the governance of a wide range of sustainable development funding mechanisms aimed at tackling climate change. The framework provides a comparative analysis of a range of greenhouse gas emission ‘offset’ mechanisms, including the United Nations Programme for the Reduction of Emissions from Deforestation and Forest Degradation (‘REDD+’), built on a series of surveys of environmental, government and economic stakeholders, conducted between 2009 and 2010. It finds that perceptions of institutional governance quality varies greatly across the specific sectors and regions, but that, curiously, respondents from the global South rate both mechanisms higher than those in the global North, irrespective of their sector. The paper concludes that in the absence of global standards of governance quality it

is difficult to evaluate the credibility of the claims made by proponents of these mechanisms, and the outcomes on the ground. This has important ramifications for the legitimacy of market-based approaches to climate change management and sustainable development generally.

**Keywords:** governance quality, legitimacy, global North, global South, REDD+.

## Introduction

In international relations (IR), the once orthodox perspective, which views global political cooperation being undertaken largely by nation-states via intergovernmental regimes and associated agreements, is now seen as being out of date.<sup>1</sup> Emergent IR 'globalists' emphasise the *structures* of governance.<sup>2</sup> Traditionally, global governance was a matter for individual countries via balance of power politics, but modern global governance is no longer dominated by the nation-state, and extremely disparate interests that are not dependent on organisation along territorial lines have begun to outflank the state.<sup>3</sup> Multilateral institutions in particular have become central, now differentiated between *government* ("control exercised by the nation-state, through formal (usually elected) parties") and *governance* ("control exercised by a variety of public and private institutions that have been established at different spatial scales").<sup>4</sup> The globalisation of politics has led to a commensurate growth of global governance, not solely represented within formal institutions and organisations for intergovernmental cooperation such as the UN. Multinational corporations, transnational social movements and a multitude of non-governmental organisations all pursue global objectives that bear upon systems of trans-national rules and authority, around which the relevant actors converge and through which they pursue international relations.<sup>5</sup> Although there is no formal global government, it is nevertheless true to say that there is still global governance, whereby actors enmeshed in regimes (or more appropriately, less formalised arrangements of norms, rules and procedures) engage in behaviour that is nevertheless regulated and predictable.<sup>6</sup> As it is currently expressed in such intergovernmental institutions as the UN, however, global governance is simply not strong enough as a substitute for the mechanisms of government inherent in the nation-state.<sup>7</sup> This failure of intergovernmental

1. James Rosenau, "Change, Complexity and Governance in a Globalising Space", *Debating Governance: Authority, Steering and Democracy* ed. Jon Pierre (Oxford and New York: Oxford University Press, 2000) pp. 167-200, at pp. 167-168.

2. Mathias Koenig-Archibugi, "Introduction: Institutional Diversity in Global Governance", in *New Modes of Governance in the Global System: Exploring Publicness, Delegation and Inclusiveness* ed. Mathias Koenig-Archibugi and Michael Zürn (Basingstoke: Palgrave Macmillan, 2006), pp. 1-30 at p. 13 and footnote 13.

3. Ruggie, "Taking Embedded Liberalism Global", p. 104

4. Perrons, *Globalization and Social Change*, p. 255.

5. Held et al., *Global Transformations*, pp. 49-51.

6. Ibid.

7. Ruggie, "Taking Embedded Liberalism Global", pp. 94-95.

organisations to institutionalise strong supranational agreements is noted as being particularly evident in relation to the environment.<sup>8</sup> Emergent contemporary social initiatives and movements around the environment are a response to this lack, and are triggering more inclusive forms of global governance to compensate, which are based on the “dynamic interplay between civil society, business and public sector over the issue of corporate social responsibility.”<sup>9</sup>

Without overstating the point, public policy scholars that focus more on governance at the national and supranational levels tend to show a greater interest in its *processes* than more globally oriented theorists. Despite their analytical orientation around the activities of governments within the nation-state they are nevertheless also interested in governance at the international level. This is partly on account of the growth of collectivities such as the European Union (EU), since comparative political studies have been inevitably drawn into discussions regarding multi-level governance.<sup>10</sup> The environment is one policy arena where divergent groups (both state and non-state) are drawn together in a kind of vigorous pluralism.<sup>11</sup> The need to properly address environmental problems has resulted in the replacement of old state/society relations by new forms of public/private interaction.<sup>12</sup> This shift is a consequence of the perception of the lack of effectiveness of purely public regulation in tackling the environmental crisis. Complexity has reduced the ability of governments to act unilaterally, requiring the coordination of inter-dependent players in a way that ensures cooperation instead of the exercise of the power of obstruction, where adversarial and non-cooperative behaviour obstructs economic and environmental outcomes.<sup>13</sup> ‘New’ governance, by contrast to previous approaches, is envisaged as a positive process of learning, where all are involved in the management of structural change and the negotiation and exchange of information between parties results in them learning to trust -- as opposed to mistrust -- each other.<sup>14</sup> The interactions between participants is occurring within democratically self-regulating systems, in which environmental policy is the product of processes of internal reflection. These systems are replacing existing, more legalistic, mechanisms.<sup>15</sup>

Public policy theorists, like their IR/IP counterparts, also question the

8. Sonnenfeld and Mol, “Globalization and the Transformation of Environmental Governance”, p. 1323.

9. Ruggie, “Taking Embedded Liberalism Global”, p. 95.

10. Van Kersbergen and Van Waarden, “‘Governance’ as a Bridge Between Disciplines”, pp. 149-150; Kjaer, *Governance*, p. 6.

11. William M. Lafferty and James Meadowcroft, “Democracy and the Environment: Prospects for Greater Congruence”, *Democracy and the Environment: Problems and Prospects*, ed. William M. Lafferty and James Meadowcroft (Cheltenham and Lyme: Edward Elgar, 1996), pp. 256-272 at p. 257.

12. Daniel J. Fiorino, “Rethinking Environmental Regulation: Perspectives on Law and Governance”, *The Harvard Environmental Law Review* 23(2) (1999) pp. 441-469 at p. 443.

13. Van Vliet, “Environmental Regulation of Business”, pp. 107-110.

14. Van Vliet, “Environmental Regulation of Business” pp. 108-111.

15. Fiorino, “Rethinking Environmental Regulation”, pp. 443-447.

ability of the current modes of governance to provide for genuine democracy. Market-based mechanisms confine democratic decision making to policies for creating low-cost social conditions conducive to economic development. International institutions and regimes aimed at solving problems beyond the nation-state, such as the environment, are built upon highly technocratic and exclusive supranational agencies and agreements, with a very reduced role for the public. Corporate, private governance arrangements for example, despite some modest concessions to demonstrate a degree of accountability and transparency, still exclude major stakeholding interests such as local communities.<sup>16</sup>

## Market-based mechanisms and global finance

Deforestation and forest degradation account for nearly 20% of global greenhouse gas (GHG) emissions, more than the entire global transportation sector and second only to the energy sector.<sup>17</sup> REDD is best understood as an initiative to reduce greenhouse gas (GHG) emissions associated with forest clearing, which allows 'avoided deforestation' in to be included in market-based carbon trading mechanisms. It is effectively a payment in exchange for actively preserving existing forests.<sup>18</sup> The original concept has been accredited to Columbia University MBA graduate and Kevin Conrad. By the time the Kyoto Protocol was formally ratified in 2004 deforestation had effectively dropped off the agenda. Conrad, founder of the Coalition of Rainforest Nations representing the main rainforest regions, successfully lobbied the United Nations Framework Convention on Climate Change (UNFCCC) to consider his proposal as a mechanism for re-integrating action on deforestation back into the climate change talks.<sup>19</sup>

REDD addresses the problem of climate change via a range of state and non-state market-based mechanisms to encourage sustainable management of tropical forests, and thereby reduce greenhouse gas emissions. It is now formally referred to as REDD+ in the wake of the UNFCCC Conference of Parties (COP) 15 in Copenhagen, to reflect the initiative's growing emphasis on conserving and enhancing forests on the basis of their value for carbon sequestration, rather than simply reducing emissions.<sup>20</sup> It is linked to the Kyoto Protocol (KP) and the Protocol-related Clean Development Mechanism (CDM) as it offers developing countries a means of meeting their emissions targets through reducing GHG emissions

16. Paul Hirst, "Democracy and Governance", in *Debating Governance: Authority, Steering and Democracy*, ed. Jon Pierre (New York: Oxford University Press, 2000) pp. 13-35.

17. UN REDD Programme "About REDD+", <http://www.un-redd.org/AboutREDD/tabid/582/language/en-US/Default.aspx> accessed 20/05/2010

18. Carbon Positive, "Glossary" <http://www.carbonpositive.net/viewarticle.aspx?articleID=44> accessed 010/10/2010.

19. Beth Kwon, "Diet for a Warm Planet", *Columbia Magazine*, Spring (2006), pp. 22-27 at pp. 24-25.

20. For more information, see: Charlie Parker, Andrew Mitchell, Mandar Trivedi and Niki Mardas, *The Little REDD+ Book* (Oxford: Global Canopy Programme, 2009), pp. 11- 92.

and increasing GHG sinks (i.e. forests) in developing countries.<sup>21</sup>

There are a number of mechanisms associated with REDD+. The UNFCCC is responsible for the intergovernmental negotiations regarding the content and format of REDD+. The United Nations Collaborative Programme on Reducing Emissions from Deforestation and Forest Degradation in Developing Countries (UN-REDD), manages the technical and financial components of the initiative at the international and national level, with the assistance of the United Nations Development Programme (UNDP) and the Food and Agriculture Organisation (FAO). The Forest Carbon Partnership Facility (FCPF), via the World Bank, provides funding aimed at maintaining standing forests by encouraging biodiversity conservation and sustainable use through a range of country-level projects.<sup>22</sup> The Forest Investment Program (FIP) is part of the World Bank's Strategic Climate Fund (SCF), and provides funds to specific sectors and projects to pilot new activities and build capacity in existing activities aimed at tackling climate change. Funding of more than USD\$500 million has been offered by developed country donors including the US and Australia.<sup>23</sup> The Global Environmental Facility (GEF), created by the World Bank in 1991, is a partnership arrangement made up of 178 countries, NGOs, the private sector and international institutions.<sup>24</sup> The GEF Trust Fund developed a funding programme as part of its fifth four-yearly funding cycle (GEF-5) for REDD and associated sustainable forest management and forest conservation activities as a result of COP 13 in Bali, 2007.<sup>25</sup> The REDD+ Partnership was established in June 2010 as an "action track" to supplement UNFCCC negotiations. It is a country-led initiative of 58 member-states but does include some civil society and Indigenous peoples' organizations (IPOs) as well as the private sector. Developed countries have provided USD\$4 billion for the funding period 2010-2012.<sup>26</sup>

To ensure REDD+ meets expectations as one of the solutions to climate change, it will require a robust, transparent, inclusive and independent monitoring system capable of addressing governance realities on the

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21. CIFOR, *Simply REDD: CIFOR's Guide to Forests, Climate Change and REDD* (Bogor: CIFOR, Undated), p. 9 [www.cifor.cgiar.org/publications/pdf\\_files/.../MediaGuide\\_REDD.pdf](http://www.cifor.cgiar.org/publications/pdf_files/.../MediaGuide_REDD.pdf) accessed 01/10/2010.

22. UN-REDD, "The UN-REDD Programme" <http://www.un-redd.org/UNREDDProgramme/tabid/583/language/en-US/Default.aspx>, accessed 23/03/2010, Forest Carbon Partnership Facility, "Forest Carbon Partnership Facility", undated, pp. 6-10.

23. Climate Funds Update, "Forest Investment program", <http://www.climatefundsupdate.org/listing/forest-investment-program> accessed 01/10/2010.

24. Climate Lab, "Global Environment Facility", [http://climatelab.org/Global\\_Environment\\_Facility](http://climatelab.org/Global_Environment_Facility) accessed 01/10/2010.

25. International Institute for Sustainable Development (IISD) Reporting Services, "GEF STAP Considers REDD, Forest Conservation and Sustainable Forest Management" <http://climate-l.org/news/gef-stap-considers-redd-forest-conservation-and-sustainable-forest-management/> accessed 01/10/2010.

26. Forest Carbon Portal, "Multilateral Interim Redd+ Partnership Established In Oslo" <http://www.forestcarbonportal.com/resource/interim-redd-partnership-established-oslo> accessed 02/10/2010.

ground.<sup>27</sup> Monitoring, reporting and verification (MRV) is essential, otherwise REDD+ will go the way of the CDM with over complex rules for many developing countries and where two countries (China and India) share almost three-quarters of the total projects.<sup>28</sup> The relationship between the CDM and REDD+ remains unclear. If REDD+ is linked with CDM its future is dependent on that of the CDM, which is also uncertain. It has been suggested that additional emissions sources such as REDD+ should be kept separate as it is uncertain how integrating REDD+ will impact on carbon markets.<sup>29</sup> REDD+ requires governance arrangements that can deliver large-scale emissions reductions. Inclusiveness of representation of forest dependent people, civil society organizations, and the private sector, as well as systemic transparency are also necessary.<sup>30</sup>

### Global governance and the North/South divide

Some of these broader governance issues can be seen to be playing themselves out in the various policy regimes tackling climate change. There is an inherent and ongoing tension between sustainable development, and climate governance, for example. Contradictions are evident in the Kyoto Protocol in particular. On the sustainable development side of the equation it promotes specialization and North/South technology transfer, and provides an efficient way of tackling emissions reduction cost effectively. Following the Rio model of engagement, it also allows for multi-stakeholder participation in climate governance, and enhances local capabilities. However, the current realities of climate governance are providing the West with a cheap way to avoid taking action itself, whilst simultaneously privatizing the global commons by ascribing private property rights to nature via the market. These realities reinforce the domination of rich countries over poor, whilst alienating the poor from their land and decision making over common resources.<sup>31</sup> Developing countries argue that developed countries should take the lead in reducing emissions; developed countries in return argue that they were unaware of the impacts of emissions previously and that it is fairer to allocate burden sharing on the basis of current emission levels.<sup>32</sup> The current regulatory carbon-related framework, and its North to South market-based models of capital transfer and carbon finance mechanisms,

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27. Global Witness, *Building Confidence in REDD, Monitoring Beyond Carbon* (London: Global Witness, 2009).

28. Bleaney et al, *Ibid.*

29. *Ibid.*

30. Charlotte Streck, Luis Gomez-Echeverri; Pablo Gutman; Cyril Loisel; Jacob Werksman, *REDD+ Institutional Options Assessment: Developing an Efficient, Effective, and Equitable Institutional Framework for REDD+ under the UNFCCC*, [http://www.redd-oar.org/links/REDD+IOA\\_en.pdf](http://www.redd-oar.org/links/REDD+IOA_en.pdf), accessed 21/05/2010.

31. Okereke, "Climate Justice and the International Regime", p. 470.

32. *Ibid.* p. 465.



“which *necessarily* engenders an uneven distribution of development.”<sup>33</sup> The choice of mechanism also demonstrates considerable variability, such as the preference for climate ‘partnerships’. The Asia Pacific Partnership for example has been characterized as a multilateral governmental model which sits outside the purview of the UN, and which is both elitist and technocratic. Public-private partnerships, might be seen as having higher levels of governance quality since they have institutionalized validation, review and verification through a range of monitoring mechanisms.<sup>34</sup>

Developing-country concerns about institutional or technical capacity are important, but of a second order compared to matters of legitimacy and credibility.<sup>35</sup> Opportunities should be made available to forest sector stakeholders to help ensure REDD+ negotiations deliver progressive and equitable outcomes for people and forests.<sup>36</sup> At present, there is no final and binding REDD+ agreement, nothing can be described as certain. However, negotiators at COPS 15 and 16 did reach consensus on a number of key issues, which are extremely likely to be part of a REDD agreement when it is reached.

## Analytical framework

Studying stakeholders’ attitudes regarding the evolving governance of REDD+ provides insights into the relative influence of specific sectors, and the quality of the initiatives as a whole. This section explores the perceptions of environmental, governmental and economic sector participants from both the global North and South regarding the governance of REDD+. Given its intergovernmental focus, the results relating to REDD+ focus on governmental and environmental non-government participants. Where available, individual comments regarding finance and investment issues pertaining to the mechanisms are also reproduced. The REDD+ survey produces the results of three surveys relating to the UNFCCC REDD+ related negotiations, which were conducted before and after COP 15 in November 2009 and March 2010, and in September 2010, before COP 16 in Cancun, December 2010. The CDM survey was also conducted in October 2010 before COP 16.

The surveys use an analytical model based on a framework of principles, criteria and indicators of governance quality. The framework is based on a review of governance attributes, identified from the fields of international relations, comparative politics, public administration and broader

33. Matthew Paterson and Johannes Stripple, “Singing Climate Change into Existence: On the Territorialization of Climate Policy Making”, in *The Social Construction of Climate Change: Power, Knowledge, Norms, Discourses* ed. Mary Pettinger (Aldershot and Burlington: Ashgate, 2007) pp. 149-172, at p. 543; Emphasis in the original.

34. Ibid. pp. 74-100.

35. Ibid.

36. RECOFT (The Centre for People and Forests) REDD+, “Moving Forward for People and Forests”, [http://www.recoftc.org/site/fileadmin/docs/publications/The\\_Grey\\_Zone/2010/REDD\\_\\_2010\\_MovingFINAL.pdf](http://www.recoftc.org/site/fileadmin/docs/publications/The_Grey_Zone/2010/REDD__2010_MovingFINAL.pdf) accessed 18 /05/2010.

governance theory. These attributes are arranged hierarchically to allow for consistency of measurement. Measurement is by means of indicators, which are aggregated under the relevant criterion, or category. These criteria are in turn used to evaluate compliance at the principle level. A principle is a rule, or value, that requires measurement. See Table 5.1 below.

**Table 5.1: Hierarchical framework for the assessment of governance quality**

<b>Principle</b>	<b>Criterion</b>	<b>Indicator</b>
"Meaningful participation"	<i>Interest representation</i>	<b>Inclusiveness</b>
		<b>Equality</b>
		<b>Resources</b>
	<i>Organisational responsibility</i>	<b>Accountability</b>
		<b>Transparency</b>
"Productive deliberation"	<i>Decision making</i>	<b>Democracy</b>
		<b>Agreement</b>
		<b>Dispute settlement</b>
	<i>Implementation</i>	<b>Behavioural change</b>
		<b>Problem solving</b>
		<b>Durability</b>

**Source:** Cadman 2011: 17

Participants were asked to rate their perceptions using a Likert scale from 'very low' to 'very high' (1-5), rounded to the second decimal point, following the indicators of Table 1 above. The scores of the relevant indicators were added to determine performance at the criterion level. In turn, the relevant criteria were added to determine performance at the principle level; finally, the two principle scores were combined to determine overall performance. Participants were recruited from a range of publicly available lists of representatives from organisations actively involved in REDD+. The invitation to participate in the survey was blind carbon copied to invitation recipients, who were invited to disseminate the survey further. In addition to the qualitative rating scale, respondents were also invited to provide substantive comments. The number and type of respondents are set out in tables 5.2 and 5.3 below:

**Table 5.2 Breakdown of UNFCCC REDD+ environmental and governmental respondents by survey, region and sector**

Survey	Region	Sector		Total number
		Environmental	Government	
1. November 2009	North	19	1	30
	South	5	5	
2. March 2009	North	6	3	36
	South	17	10	
3. September 2010	North	8	9	35
	South	8	10	
Total North/South		63	38	101

## Qualitative survey results

### *Environmental respondents:*

Northern environmental NGOs provided the most comments on the financial and market-based aspects of REDD+. One Northern respondent expressed a concern over the potential impacts of climate change investment could have on other environmental initiatives, since “payments for carbon offsets or use of REDD+ otherwise in international carbon markets will inevitably lead to devaluation of other ecosystem services no matter the level of concern expressed in guiding principles and documents”. They were particularly worried that payments for carbon services would be captured by local elites or private business entities. They also felt that local and indigenous resource users were threatened by further marginalization and inequitable distribution of benefits from REDD+ if this critical issue was not addressed immediately.

Some consideration was given to the representation of interests within the initiative, leading one respondent to comment that it was not “equitable”. They questioned the democratic legitimacy of the negotiations on account of the power of “corporate lobbying and vested interests”, which had a greater impact on decision making than other participants. They felt the whole REDD+ space was overly pre-occupied with “corporate solutions” to climate change. This led one respondent to suggest that REDD+ needed to come to grips with “engaging people from the ethical [Carbon] markets sector”. The corporate emphasis of REDD+ led another respondent to question its “overall policy architecture” and focus on developing carbon trading in the future, as this would, in their opinion, undermine any potential for it to be effective. It was not geared to changing behaviour, but maintaining “business-as-usual”. This view was echoed by another respondent who was concerned that the presence of logging interests in the negotiations would “end up promoting deforestation by subsidising logging”.

Part of the problem, according to a further individual, was that the

initiative seemed “overly dependent on donor funding” from the developed countries. This would impact on the durability of REDD+ because recipient countries lacked genuine motivation. The overall parlous nature of donor funding was also problematic, and referred to by a number of respondents. One respondent felt the situation would only improve if there were more donors on board. At the time of writing, they noted that only Norway and Denmark had made substantive contributions. More were needed. They were also concerned that the support efforts of UN-REDD in channelling funds to recipient countries in the absence of “proper independent expert review of country programmes” meant that money might be approved for countries “without a lot of transparency and oversight”. The situation was very dependent on the UNDP country reps, and it was not clear to what extent “funds are being transferred to country institutions as opposed to being used in the local UNDP offices”. In this context, according to another respondent it was good to have both UN-REDD and FCPF in recipient countries. If they were able to “harmonise” their activities at national level it would improve REDD+ implementation

Southern respondents added two further comments. One echoed concerns about the role of donor countries, and commented that, “money will talk as always, and the big countries will get their way”. This was possibly because, according to another respondent “it seems like politics comes first”. The last respondent was concerned that the rise and fall of different “interim mechanisms” such as the REDD+ Partnership “could blur the quality of the UNFCCC especially in terms of financing, transparency and inclusiveness”.

Northern respondents noted without exception that they received no resources to participate in any of the REDD+ mechanisms. Only respondents from the South answered that they had received support, one commenting that they felt these had been “adequate”.

## **Government respondents**

Governments were mostly concerned about the structures and processes of REDD+. One southern respondent was particularly concerned that “very little effort” had gone into getting scientists actually involved in REDD+ related work to contribute to negotiations. This meant that decision were “too politically based and not factually based”. One northern respondent noted that part of the problem was that the bureaucratic structures at both the intergovernmental and national levels were “a big barrier.” However, by way of mitigation, one Southern respondent noted that what REDD+ was doing was new and that no one had all the answers. What was important were the “collaborative arrangements” (like UN-REDD) that helped collective progress rather than “operating separately”. They saw the value of such collaboration as “tremendous” and they consequently considered their participation in REDD+ to be “highly meaningful”. Finally, in terms of resources, one Northern respondent noted that their government provided all their costs. They did not consider it necessary for the mechanism itself to fund participation.

Quantitative survey results

Table 5.3 Environment and Government sectors' perspectives of REDD+ related UNFCCC negotiations (global North and South)

Principle	1. Meaningful Participation Maximum score: 25; Minimum: 5						2. Productive deliberation Maximum score: 30 Minimum: 6								Total (out of 55)
	1. Interest representation Maximum score: 15 Minimum: 3			2. Organisational responsibility Maximum score: 10 Minimum: 2			3. Decision-making Maximum score: 15 Minimum: 3			4. Implementation Maximum score: 15 Minimum: 3				Principle Score	
Indicator	Inclusiveness	Equity	Resources	Criterion Score	Accountability	Transparency	Criterion Score	Democracy	Agreement	Dispute settlement	Criterion Score	Behavioural change	Problem solving		Durability
Environment North	2.58	1.83	1.59	6.00	2.76	2.76	5.52	2.33	2.29	2.15	6.77	2.83	2.53	3.44	8.80
	2.67	1.83	1.00	5.50	2.60	2.67	5.27	2.20	2.17	2.20	6.57	2.60	2.60	2.67	7.87
	3.63	2.67	1.71	8.01	2.63	2.50	5.13	2.75	2.29	2.50	7.54	3.13	3.13	3.14	9.40
Environment South	2.60	3.00	1.80	7.40	2.00	2.40	4.40	2.25	2.00	2.00	6.25	2.60	3.00	3.00	8.60
	3.25	2.67	2.17	8.09	3.46	3.36	6.82	2.71	2.88	2.54	8.13	3.06	2.94	3.38	9.38
	4.18	3.65	2.29	10.12	3.62	3.93	7.55	3.69	3.06	2.81	9.56	3.82	3.76	3.53	11.11
Government North	5.00	4.00	1.00	10.00	3.00	4.00	7.00	4.00	4.00	4.00	12.00	4.00	4.00	5.00	13.00
	3.33	4.00	1.00	8.33	3.00	3.67	6.67	3.33	2.67	2.33	8.33	3.67	3.67	3.00	10.34
	3.67	2.5	2.5	8.67	3.44	3.43	6.87	4	3.44	3.17	10.61	3.88	3.56	3.63	11.07
Government South	3.20	2.60	2.20	8.00	3.25	3.20	6.45	3.20	3.00	2.50	8.70	2.60	2.40	2.80	7.80
	3.50	3.10	2.33	8.93	3.30	2.80	6.10	2.80	3.40	2.78	8.98	3.70	3.50	3.60	10.80
	3.90	3.70	1.78	9.38	3.10	3.50	6.60	3.50	3.20	3.33	10.03	4.00	3.90	4.30	12.20
															22.23
															27.09
															14.44
															16.94
															14.85
															17.51
															20.67
															25.00
															18.67
															21.68
															16.50
															19.78
															34.81
															38.21

Notes: 1) Results included from Survey 1 (before COP 15 - dark grey), Survey 2 (After COP 15 - medium grey) and Survey 3 (before COP 16 - white).

## Conclusions

The results would appear to confirm some academic concerns regarding the quality of REDD+ governance arrangements. It would also be interesting to determine whether the results generated from this survey would be similar at an individual country level (such as Nepal). With regards to the surveys themselves, it is also worth noting the potential existence of a participation gap between financial 'insiders' (such as government) and 'outsiders' (environmental NGOs) regarding REDD+ governance quality. But the results are from a short-term study, and one with relatively few participants. The surveys nevertheless do provide some insights into the quality of governance but are not definitive in their own right. Longer-term investigation will be necessary to determine if the trends identified here are correct. However it is worth making the point that quality-of-governance standards would make it easier for potential and actual participants in global environmental governance systems like REDD+ to determine whether they should engage in a given initiative or not. Standards would also allow potential and actual investors to determine the 'governance risk' of climate change investments.

# 10

## **Green governance:**

### Development aid, local investment and benefits from community forestry

–B.K. Pokharel

**THIS** paper provides an analysis of forest sector governance, which is facing challenges of contradictions stemming from old fashioned bureaucratic culture of classical forest service and new democratic governance practice of Nepal's community forestry. In addition, it analyses the scale and the volume of development aid, investment of Nepali government and local communities in community forestry sub-sector. Local communities are increasingly seen as the main investors and source of financing, bearing more than two third cost of Nepal's community forestry. The benefit however is not in commensurate with what local communities have invested. So there is a challenge whether local communities can invest on community forestry sustainably for its protection and management if they are not empowered and favoured by government in terms of securing tenure rights and autonomy so as to optimise livelihood opportunities for the people dependent on forests.

#### **Forest governance woes:**

Following restoration of democracy in 1990, forest sector governance has been one of the few sectors in Nepal undergoing massive transformation from conventional technocratic stereo-typed bureaucracy to a pro-poor and democratic public service. On the one hand, forest sector suffers from ill-governance practices, on the other, it is transforming by itself.

On a positive note, through community forestry, re-orientation of people

from the forest service has altered their traditional role of policing to a role of advisors. As a result, the forest service has started to collaborate with civil society organisations. Government staffs are getting aware of equity issues and have begun to realise the need of inclusion of the poor and marginalised groups.

Despite positive change, the forest service still suffers from ill governance. For example, rule of law is not maintained. Law contradicts with policies and its own regulations. Frequent and sudden change in policies without consensus makes the working environment difficult and confusing. Whilst forestry requires long term strategic visions, decisions are taken keeping in mind the short term gains. Forest has several stakeholders but the forest service still suffers from heavy workload and is overburdened with legal, administrative, fiscal and technical loads resulting in low quality service delivery. Legal provisions are normally misinterpreted and not complied with. Tradition of dilly-dally still holds. Necessary documents and procedures for decision making are still held back from public. Officials and functionaries tend to be accountable only to their seniors and not to the general public. Duty-bearers with authority and power often do a disappearing act. Forest sector is yet to learn from its own success and failures. The decision making process is very much influenced by short term political and personal interests, which leads to ill-utilisation and mis-utilization of resources in the forestry sector. Tools of democracy such as public hearing, mass meetings and public poll are rarely used in decision making. Contentious issues and disputes are rarely settled through wider consultation and debates between duty-bearers and rights holders.

### **Development aid in the forestry sector and its effect**

To tackle some of the problems listed above, forestry sector received support from various donors for a period ranging from five years to twenty years, They pumped on an average US\$20 million a year (see table below) into the forest sector development totalling of US\$190.8 million over the last twenty years. Support was provided mainly for institution and capacity building related activities, (i) train forest staff in order to set up community groups through a social mobilization process, (ii) enable groups to prepare appropriate forest management plans, (iii) build capacity of forestry sector stakeholders in order to ensure institutional, ecological and economical sustainability of the community groups, and (iv) for ensuring quality service delivery and technical assistance.

Most of the development aid is spent in kind on facilitation support, government's infrastructure building and capacity building, consultancy services to enhance quality service delivery, social empowerment and technical assistance through expatriates, project and NGO personnel and local human resources, and only 20-30 percent of the total development aid is estimated to have been spent in cash at local user group and household levels.

In the event of royal takeover in February 2005, many donors withdrew



financial support in the forestry sector. Role of donors in forestry has been significant but the impact mixed. Community forestry programme, for example, has been remarkably successful in terms of its tangible impact on environmental conservation; however impact on biodiversity and watershed management has been mixed. There has been limited support in private forestry, non-timber forest products, wood based industries and research sector leaving very little or no impact.

**Table 6.1: Foreign Aid contributions to forestry sector after 1990**

Donor	Duration (approx. years)	Approx. amount in US\$ million	Average budget/yr in US \$ million	Sub sector
UK	> 20 years	53.6	2.68	Community forestry
Switzerland	> 20 years	20.0	1.00	Community forestry
Denmark	> 5 years	20.2	4.05	Community forestry
Australia	> 10 years	17.6	1.76	Community forestry
USA through CARE/N	> 10 years	11.5	1.05	Community forestry
USA through WWF/N	> 20 years	21.2	1.06	Biodiversity
Germany	> 5 years	5.0	1.00	Community forestry
IFAD	> 10 years	13.7	1.37	Leasehold forestry
The Netherlands through SNV	> 5 years	6.0	1.21	Collaborative forestry
EU	> 5 years	18.7	3.75	Watershed
Japan	> 5 years	0.7	0.14	Watershed
UNDP and FAO	> 10 years	2.6	0.26	Biodiversity
<b>Total</b>		190.8	19 .27	

*Source: Adapted from Pokharel et al., 2008*

Swiss government, for example, through its project has spent about NRs 7.5 million per year on regular government (“red book”) activities in three districts. It spent an additional NRs 5.6 million per year on various capacity building and field level activities through direct funding in human resource development (trainings, workshops, long term scholarships MSc, B.Sc, ISc scholarships<sup>1</sup> etc.) to GON staff and community members. This is equivalent to NRs 4.37 million per district, or NRs18600 per community group. It is estimated that 52 percent of this government “red book” activity expenditure is on infrastructure, vehicle running and other recurrent activities.

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 1. Support to pre and post SLC scholarships for community members is also provided but not included in this calculation.

## Local investment is much higher than the development aid

The data from three districts, where Swiss funded Nepal Swiss Community Forestry Project (NSCFP) was launched, show that the cost borne by community forestry user groups was almost 71 percent of the total cost, the donors' and government's share was only 16 percent and 13 percent respectively. Government of Nepal spent, on average, an additional NRs 7.5 million per year per district on salaries and wages of its staff and on some programme activities. A conservative estimate suggests that 50 percent of staff time is put into community forestry in the project districts. That comes to NRs 3.75 million per district or NRs16000 per community group.

Community members, on the other hand, have contributed to community forestry in two ways. Community Forest User Groups, for example, have invested an estimated NRs 76500 per year per group in labour, as opportunity cost in wages attending committee meetings, assemblies and for forest protection<sup>2</sup>. This is equivalent to NRs 850 per hectare of community forest per year<sup>3</sup> and NRs1.8 Crores per district. Community Forest User Group members spent around 25 percent of their cash fund on forest development activities. This is equivalent to an average of NRs 2500 per group per year. Groups spent a further 36 percent of their fund on community development activities like drinking water supply, school buildings, temples and trails. This comes to NRs 5500 investment per group. It is clear from the analysis that if community groups pull out from community forestry, government will have to find about 1.8 Crores NRs per year for one hill district to pay for labour inputs and forest development activities. VDCs and other government service providers will also have to fund other community development activities that are currently being undertaken by community forest user groups.

**Table 6.2: The Costs of Community Forestry (per community forest user group per year)**

Contributor	NRs	%
Development aid from donors	18,600	16
Government of Nepal	16,000	13
Community groups (labour)	76,500	64
Community groups (cash for forest development)	2,500	2
Community groups (cash used for community development)	5,500	5
<b>Total</b>	<b>1,19,100</b>	<b>100</b>

*Adapted from Pokharel et al. 2008*

- Assumptions: shadow wage rate of NRs 100 per day; investment of forest watcher (365 person days per year); assembly meetings (200 person days per year); committee meetings (60 person days per year), tole meetings (40 days per year), tending operations (100 days per year). Person days are calculated on the basis of meetings of 5-6 hours for assemblies and 2-3 hours for committee members. The estimate does not include costs some FUGs incur for forest regeneration (nursery and plantation development).
- There is an average CF of 90 ha per FUG in Dolakha, Ramechhap and Okhaldhunga.

The Table shows that community forestry is managed in the country with an investment of about 1727 million NRs (25 million US\$), of which 17.5 million US \$ is borne by the local communities only.

## **Benefits from community forestry**

Despite huge investment by local communities and the scale of operation throughout the country, the contribution of community forestry to Nepal's economy is not well recognised by the national accounting system. Linkages between the community forestry sub-sector and the poverty indicators of the National Planning Commission are weak; no mechanisms in place to link community forestry impact monitoring data with the national data. This is partly by reason of major share of the nationally unaccounted budget of community forestry is borne voluntarily by local communities and little comes from the government treasury. The national level data tends to look for physical targets against government budget rather than impacts particularly on poverty regardless of the PRSP and government periodic plans that lay emphasis on community participation.

World Bank (1994) estimated that under an intensive forest management regime Nepal's forests could yield products valued at NRs 12.5 billion per year (18.0 million US\$) - taking into account only woody products. Given the present 1.2 million hectare area of community forests, these are clearly significant amounts – the relative financial impact of focusing on 'commercial' i.e. traded products as opposed to subsistence fuelwood and fodder. At present very little of this potential is being realised.

Data from government-controlled forests is not available. However it is roughly estimated that currently Nepal utilises only 8 percent of the mean annual increment from such forests. This supports the World Bank estimate of the loss of NRs 62.5 million (892,000 US\$) per day for not sustainably managing Nepal's existing forests (World Bank 1994). This is a huge figure when compared with foreign aid to the forest sector received by Nepal (approximately 52,000 US \$ per day) over the past 10 years. The total annual income from the sale of forest products from community forests is about NRs 747 million (Kanel, 2004). This stands higher than the annual budget of the Forest Department of about NRs 680 million, and the annual income from government controlled forests of about NRs 550 million in 2002. Since community forests cover only about 22 percent of area that are national forests but generate a much larger income, the implication is that forest management through community forestry is the more efficient in terms of revenue generation (Kanel 2004).

In addition to the economic benefits mentioned above, community forestry contributes to social inclusion, gender equality and rural development. In 15 years, community forestry has become one of the largest initiatives in the country. There are around 14337 CFUG formed, 80 percent of which are federated at village, district and national level federation with an influential role in policy making processes at local, national and, to some extent, at the international level. A total of 23 percent of the country's

forests (1.219 mio ha) is handed over to the groups which covers about 38 percent of the rural population (1.647 mio families). There are about 52,000 grassroots women leaders (1/3rd position in the CFUG committees) and 5000 women leaders in various chapters in CFUG federations (½ of the leadership positions are reserved for women at village, sub district, district and national level federations). As a result of inclusive structure and local democratics processes, Nepal's community forestry programme significantly contribute to social and human development, community infrastructure and addresses, to some extent, poverty and equity issues by mobilizing natural and human resources. It is discovered that many groups are able to deliver 16 various types of services at rural areas which are under the domain of various ministries beyond the mandate of forest ministry and department (see Box below).

### **CFUGs deliver at least 16 types of services to their members**

Local democracy and economy - Local level participatory decision making, election of committees, judiciary, supply of forest products, public auditing; communication and extension, micro- finance, cooperative

Natural Resource Management - forest, agriculture, environment, eco-tourism, and land management

Physical infrastructure, human and social development - community building, community utensils, transport – road, trail and bridge, irrigation channel, pond, electricity, toilet and sanitation, water mill, telephone lines and poles, improved stove, health facilities and humanitarian assistance, temple, drinking water, education – school building, teachers' salary, furniture and women empowerment

**Source:** Pokharel et. al. (2008)

Studies show that quality of community forests has increased as evident from improvement in landscape and biodiversity (Branney and Yadav, 1998; Gautam et. al., 2002; DOF, 2005; Kandel and Neupane, 2007; Nagendra et. al., 2008; Luitel et. al., 2009; Pokharel and Mahat, 2009). Community Forest User groups have become the vehicle to reach to the poorest and disadvantaged households to enhance their livelihoods assets (see Box below).

## Livelihood assets offered by CFUGs to the poorest households

Financial resources – loan, grant, access to group fund, share to enterprise, priority to employment  
Human development – training, self-employment skill, scholarship, information, quota in leadership positions  
Social development – membership, linkage with other organizations, formation of collectives of disadvantaged households  
Physical material support – wood, food, fodder, fuel wood, construction timber, herbs and leaves  
Natural capital – community forest land, right to use water and stream inside community forests for drinking water, fishing and irrigation  
Policy to ensure poor people's right – positive discrimination for equitable benefit, gender equity and inclusion policy  
Mitigating vulnerability – material support to maintain shelter, humanitarian support in cash and kind to the victim of natural disaster and calamities

**Source:** Pokharel and Carter (2010)

Despite all these contributions community forest user groups have made and the dynamics of local institutions in restoring forest resources (Pokharel and Mahat, 2010), the challenge remains on how to institutionalise locally initiated rural development processes; how to make these groups more focused to the wider issues of poverty, equity and access to resources from the part of the poorest and disadvantaged (Yadav et.al., 2008; McDermott et. al., 2009). Many of these issues however are inherited by hierarchical social structure and the top-down nature of wider forest sector governance, and insecure forestland tenure rights (Pokharel and Paudyal, 2010), and not so much because of the weakness of community forestry itself.

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# 11

## Foreign aid and Education in Nepal: Some Critical Issues

– Laxman Acharya  
– Dr. Bidya Nath Koirala

### **Foreign aid: a major means of building relationship with outsiders**

"Nepal is a yam between two boulders" and "Do not allow foreign businessmen to come any closer than Parsha-Gadhi (A border-town with India). If foreign merchants come into the country, they will leave the people destitute" are two famous foreign policies of Late King Prithvi Narayan Shah, the founder of modern Nepal. His first foreign policy of maintaining balanced relations with India and China is still valid in Nepal and no political parties or government of the country have deviated from this. The second policy, isolating Nepal from all other countries prevailed for almost two centuries, and got a break especially during the Janga Bahadur's regime, the first prime minister of Rana regime<sup>1</sup>.

But, a number of events occurred after the Second World War to change Nepal's foreign policy from one of isolationism to a much more open one. Formation of the UNO, India's independence from British rule, the downfall of the Rana regime in Nepal, China's emergence as a communist country, and the cold war politics worked as triggers for the change. Right from the 1950s, successive governments of Nepal have tried to be more open towards the foreign world in order to modernize the country. To fulfill this objective it was necessary to get foreign aid – the financial support, technological know how and development ideas and model. Meanwhile, western countries were also interested to enter into the country because its geopolitical location

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1. Acharya, Laxman (2006)

made it fairly important from a strategic point of view<sup>2</sup>. As a result foreign aid became the major tool to serve the interest of both Nepal's and the western countries. As a result, the number of donors as well as the amount of foreign aid pouring into Nepal increased sharply over successive decades. Being neutral towards superpowers and attracting as much foreign aid as possible, Nepal accepted all and any form of aid, as and when provided. As a result, a wide range of donors from countries capitalist to communist, from sources bilateral to multilateral, and even from missionary organizations to INGOs provided assistance to Nepal. Similarly, there were neither any specific areas, regions, sectors, nor any specific group of people that were targeted specifically by foreign aid.

As a result, foreign aid has been used for any purpose; from physical infrastructure to basic social service development and from entertainment related programmes to the development of culture and religion.

### **Foreign aid: a means of fulfilling donors and recipient's interest**

There is a big debate on the motive of foreign aid. Theoretically, all donors are altruist. The moral and ethical grounds of helping Nepal and its people is the first one that all donors agree upon and state very frankly. But many literatures and experiences claim that donors to Nepal have entered the country with hidden motives riding on foreign aid. The commercial, political and strategic interests are other pervasive motives that they do not like to admit easily. There is no historical evidence to suggest that over longer periods of time donor nations assist others without expecting some corresponding benefits (political, economic, military, etc).<sup>3</sup>

The main objective behind the US's entry in to Nepal during 1950s was to prevent communist incursion by encouraging political and economic stability by helping vulnerable people in the periphery of the communist world<sup>4</sup>. The motive of aid from the then USSR was to counter the American strategy and to spread its own political ideology. India and China started their aid program in Nepal because of their rivalry and their strategic interest in Nepal. Most of other donor countries had one common goal of commercial interest that is to enhance the world capitalist system. Capturing the market in poor countries and making it more favorable for their own trade are the major commercial interests of donors. One can see many examples of conditionalities imposed on aid such as purchase of hardware and appointment of advisors from their own countries in many bilateral donor programmes in Nepal. Japan's growing economic interest in the Asian continent at that time could have been an effort to capture the market through aid.<sup>5</sup>

The motive of giving aid on ethical and moral grounds is also guided by strategic interests of the donor. The resources transferred from rich

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3. Todaro, M P (1985), Development in the Third world,
4. Mihaly, E. B. (1965/2003), Foreign aid and politics in Nepal, Himal Books, Kathmandu
5. ibid



countries to the poor ones help to distribute global resources more equally, which, in the long run, is beneficial and is also a prerequisite for continued welfare and growth of the rich industrial countries. Growing poverty in many underdeveloped countries and the widening gap between the rich and the poor supposedly poses a threat to the security of the rich nations. Thus, this is the general hidden motive of all donors to Nepal behind their assistance to the poor ones: to tackle this possible threat to their own security.

Small European donors, like Denmark, Norway, Finland, Netherlands seem to be the ones providing aid more on humanist grounds and to transfer their own development experiences to Nepal. However, it does not mean that these countries did not have the motives of opening market and global security, a general motive of all developed countries.

Socio-economic development is the global objective behind aid from multilateral institutions such as WB, ADB and UN agencies. Their global interest of helping developing countries and raising the living standards of people is valid in Nepal too. In line with their global agenda, the initiation of these multilateral banks' aid programmes in Nepal is to integrate the country into the global economy – the hidden agenda of western countries. Similarly, the UNDP's interest is to secure security, and to contribute to poverty reduction goals<sup>6</sup>.

Likewise, the ruling party and government of Nepal also have their own hidden agenda with foreign aid inflow. Despite theoretical need of foreign aid to bridge the technological and financial gap, the past experiences show that the foreign aid has remained means to stay on power. The amount of foreign aid inflow into the country and donor's support in the development are considered as a measuring rod of judging the strength of political party or government. Rather than utilizing it, each political party in government counts the amount of foreign aid that could enter in the country during their tenure. Moreover, it is an easy way to collect resources. It needs neither brain storming nor puts any risk of being unpopular by levying tax on people. Further, grant aid is not to be paid back while loan aid will be paid by future generation.

## **Foreign aid: volume, sources, types and priority sectors**

None of the responsible government agencies in Nepal can give the accurate amount of the total inflow of foreign aid to the country. Government has the record of only budgetary support of foreign aid while a huge amount of foreign aid such as some INGO's contribution and support of some missionary organizations are believed to be aid out of record. Even the MoF does not have full record on actual foreign assistance received and its use.

The amount of foreign assistance included in the budget is almost equal to the amount of foreign assistance that is not included in the budget<sup>7</sup>.

6. SECOND COUNTRY COOPERATION FRAMEWORK FOR NEPAL (2002 - 2006), UNDP Nepal

7. Based on the interview with Mr. Bishnu Bahadur KC, Auditor general, *Deshantar Weekly*, 4 March 2000

Economic Survey, a MoF publication, the most reliable source of foreign aid related information, such as gives only the budgetary support of foreign aid that accounts only the half of the foreign aid flow into the country. At present, there are dozens of multilateral and bilateral donors while hundreds of INGOs are also continuously providing development and humanitarian aid to Nepal.

During the 1950s and 60s, there was a limited number of donors, mainly India, China and the USA. These countries contributed to more than 90 percent of the total inflow of aid in the country. As several donors gradually started their aid programmes in Nepal, foreign aid in Nepal increased tremendously over time and more than trebled in each successive decade. Japan has been the largest donor since the 1980s. The multilateral banks increased their assistance sharply after the mid 1980s. Similarly, from the late 1980s, the Netherlands and other small Scandinavian countries like Norway, Finland and Denmark also increased their development assistance. In addition to this, after the restoration of democracy, several INGOs increased their assistance to the country. At present, Japan, UK, the USA, Germany and Denmark remain the largest bilateral donors while the Asian Development Bank and the World Bank are the largest multilateral donors. India and China are also other major donors to Nepal.

Grants, concessional loans and technical assistance are the major three types of aid components in Nepal while bilateral aid, multilateral aid and the contribution of INGOs are the major source of aid. Bilateral donors and multilateral agencies such as UN agencies and the EC mainly provide grants and technical assistances, whereas the WB and the ADB provide some negligible technical assistance along with large chunks of concessional loans. Likewise, INGOs provide both grants and technical assistance. Before 1990, the share of INGO's contribution was very negligible. The technical assistance was not recorded in the government budget while most of the loan and grants were spent through central government channel. But after the 1990s, the disbursement of bilateral assistance (in case of some specific donors), ones not meant to be paid back, has been done outside the government channel (mainly through I/NGOs) and is following an increasing trend. However, the concessional loans provided by the WB and the ADB are still spent almost entirely through government channels.

Technical assistance is one of the major components of foreign aid. It is also one of the most debatable issues as majority part of TA is considered to get back to the donor countries.

Nepal has been receiving technical assistance mainly in terms of foreign experts and technical advisors, feasibility studies to launch programmes, training and scholarship for Nepali citizens and several types of equipments throughout the evolution of foreign aid in Nepal. Since technical assistance as part of aid right from has not been included in the annual budget of Nepal the very beginning, it is difficult to find consistent and actual figures of the foreign aid coming in as technical assistance. According to the OECD review (1985), 'technical cooperation accounts for almost one third of the net

bilateral ODA from DAC members, compared to only 12.9 percent in 1964<sup>8</sup>. Though technical assistance constitutes a large percentage, the amount of aid under technical experts and volunteers costs are not adequately reflected in the aid figures published by the government of Nepal (ibid). The share of technical assistance in total foreign aid further increased in 1990s. Over 40 percent of all aid now is technical assistance and free standing technical assistance, that accounts for the bulk of technical assistance, has increased during the 1990-1999 period at an average annual rate of 17 percent<sup>9</sup>. The use of foreign aid is highly influenced by the donor agency rather than the need of Nepal. International development paradigms, contemporary development theories and their application by the influential donors such as the World Bank, ADB, USA, UK and UN organizations determine the priority of foreign aid. The foreign aid oriented development initiation has adopted the “copy and paste” of the world’s best examples and global leading concepts of development modality rather than identifying the country’s need and addressing it. The fact that more priority was given to infrastructure in 1950s and 60s, basic need in 1970s, the agriculture sector in the 1980s, the continuation in increase in the share of social sector from 1990s, and the sharp decline in priority of the industrial sector from the 1990s and emphasis in good governance and social exclusion 2000 onwards, are examples of this.

### **Impact of foreign aid: less intended and more unintended results**

Foreign aid had provided not only the scarce resources to Nepal but has shaped the entire development model of the country. All development approaches pursued by Nepal at different times such as industrialization to sustainable development, integrated rural development to

poverty reduction, fulfillment of basic needs to structural adjustment, import substitution to export oriented production, and empowerment of women to social inclusion are the result of foreign aid. All these are part of the changing global development strategies over time that were advocated and initiated by donor agencies in Nepal. Thus, all the present outcome of development in the country is the result of foreign aid oriented development process. However, it will be injustice to undermine the role of internal stakeholder of development.

Foreign aid has been unable to achieve its major objectives in Nepal. By principle, foreign aid helps to bridge the resource gaps in short term so that in the long term, the developing countries would be able to mobilize their own resources for sustainable development. But, in reality, Nepal could never mobilize its internal resources to meet the financial requirements of its development activities. Similarly, foreign aid was started in the country in the 1950s with the first and foremost objective of economic and political stability. But, despite a regular inflow of millions of dollars for more than

8. Khadka N (1991), *Foreign Aid, Poverty and Stagnation in Nepal*, Vikash Publishing House, New Delhi

9. *Foreign Aid Policy 2002*, MoF/HMGN

half a century, the Maoist insurgency began and Nepal has now become the most unstable like never before politically as well as economically. The impact of foreign aid in Nepal is found having a paradoxical result.

First, the role of foreign aid is very important for creation of present day socio-economic infrastructure of the country and raising awareness among people. But at the same time, foreign aid has failed to eliminate rampant poverty and deprivation of the people. The credit for the present day physical infrastructure of the country goes entirely to the foreign aid. In 1951, a single airport existed in the country, there was only one bank, only 276 kilometres of roads, a capacity to produce a mere 1.1 megawatts of electricity, just 25 telephone lines and 6,200 hectares of irrigated lines<sup>10</sup>. But today, the present achievements in road and civil aviation, means of communications (newspapers, radio and TV channels) and banking institutions are really impressive. Likewise, the impressive progress in literacy rates and declining infant mortality rates to the emphasis on human rights and democracy, good governance including the concept of social inclusion are all direct or indirect outcomes of foreign aid. But, at present, Nepal is one of the poorest countries of the world with very low per capita income.

Second, the entire development process of the past, where foreign aid had a vital role, has enhanced the wealth and prosperity of the country but the inequality among people is widening and the dependency of the country is increasing. Nepal Living Standard Survey 2003/04 has shown that the inequality between rich and poor has increased, as the value of Gini Coefficient<sup>11</sup> has increased to 41.4 in 2003/04 from 34.2 in 1995/96<sup>12</sup>. It is assumed that the value of Gini has further increased to 47.2 in 2008<sup>13</sup>. According to NLSS 2003/04, the average per capita income of richest 20 percent population is 10 times higher than that of poorest 20 percent population. In addition to this, From individuals to the whole nation itself, an aid-dependency syndrome has increased unmistakably. Today, Nepal is the largest recipient of foreign aid as a percentage of GNP in South Asia and the share of aid in GNP was 8 percent in 2003<sup>14</sup>. There is hardly any government's development programs that do not consist some part of foreign aid. Development activities without foreign aid have now become totally unimaginable in the country. Nepal has taken foreign aid even to make a systematic record of foreign aid inflow in the country. Nepal's historical economic dependency on foreign aid has now transcended into the social and political aspects. Evaluating the worth of every successive government

10. CPWF (1998), A review of foreign aid in Nepal, Citizen's Poverty Watch Forum, Kathmandu

11. The Gini coefficient is a measure of the inequality of a distribution. The Gini coefficient can range from 0 to 1; it is sometimes multiplied by 100 to range between 0 and 100. A low Gini coefficient indicates a more equal distribution, with 0 corresponding to complete equality, while higher Gini coefficients indicate more unequal distribution, with 1 corresponding to complete inequality.

12. Poverty trends in Nepal (1995/96 to 2003/04), (September 2005), CBS, NPC, HMG Nepal

13. [http://www.theodora.com/wfbcurren/nepal/nepal\\_economy.html](http://www.theodora.com/wfbcurren/nepal/nepal_economy.html) down load on Nov 18, 2010

14. World Development Indicators, 2005

in terms of foreign aid inflow is the example of it. Moreover, political parties have used foreign aid and their relation with the donor community as a tool to get into power or to depose the opposition from power. The local level politicians try to bring more foreign aid funded projects into his/her constituencies in order to prove his/her political influence and credibility, and thus, to secure his/her political future. It means foreign aid has been a measuring rod to evaluate the creditability and legitimacy of a government or political party.

Third, foreign aid has emphasized a lot for the democratization of the country and mainstreaming the deprived section of population in development process. Foreign aid has played and donor agencies has played very important role for the political movement for democracy and inclusive development model. But, still a large number of populations are economically, socially and politically excluded from the mainstream of development. They are physically participated in political and development process but neither they are able to put their view nor are their voices heard. Still there is big gap between elite and marginalized and their relationships as ruler and ruled.

### **Role of education: theoretical assumption as well as practical experience**

Education sector is getting increasing attention by the development practitioner and politicians in the developing countries of the world. Education has been recognized as an inevitable component in development from traditional concept of socio economic progress to modern concept of freedom of choice. All economists, from the eighteenth century's economist-

Adam Smith<sup>15</sup> to Nobel Prize winner economist of 1998 - Amartya Sen<sup>16</sup>, see the importance of education in individual's as well as nations' development equally. Additionally, in political context it is equally important as it is one of the strategic tools to shape an individuals mind-setting according to the political system of the country. Likewise, from the functionalists' view of promoting homogeneity in the society and enabling young people for appropriate roles in adult life to liberalists' perspective of self-fulfillment of an individual, education is equally important. Education sector has got equal importance in the Marxists' philosophy as well. They believe that education is a capitalist's tool to serve the interest of ruling

- .....
15. A man's education at the expense of much labor and time to any of those employments, which require extra ordinary dexterity and skill, may be compared to one of those expensive machines. The work which he learns to perform, it must be expected, over and above the usual wages of common labor, will replace to him the whole expense of his education, with at least the ordinary profits of an equally valuable capital--the difference between the wages of skilled labor and those of common labor is founded upon this principle (Adam Smith in *The Wealth of Nation* 1976, as cited in HDR 1998)
  16. The elimination of ignorance, of illiteracy... and of needless inequalities in opportunities is to be seen as objectives that are valued for their own sake. They expand our freedom to live the lives we have reason to value, and these elementary capabilities are of importance on their own (Sen and Derje J ,1999)

class people and to dominate the poor countries by rich one. It reproduces the social inequality, particularly of wealth, power and opportunity. Further they believe that education is an agent of capitalism and prepares student as obedient future workers. So they claim that a nation's investment in education is to maintain the inequality in the society.

The world experiences show that investment in education sector has brought a positive impact on national development. The developing countries such as Japan, South Korea, Hong Kong, Singapore, Taiwan and Thailand were able to turn into developed in second half of the nineteenth century with a significant investment in education sector during their take off stage of development. Japan's investment in the development of human resources during 1940-50 and objectives that are valued for their own sake. They expand our freedom to live the lives we have reason to value, and these elementary capabilities are of importance on their own (Sen and Derje J, 1999) that of during 1960-70 and China's during 1980-90 are the examples (Koirala and Acharya, 2000). Economic miracles in the East Asia are based on the education miracle (HDR, 1998). The development of education increases not only the productivity of labor force but also helps to optimally use other factors of production as well as new inventions and innovations. The tiger economy countries such as Japan, Korea and Thailand had adopted three similar strategies: emphasis in basic education, intensified technical education and made a big investment in education sector<sup>17</sup>. As a result of both theoretical assumption and practical experiences of importance of education, the developing countries have been investing, over the period, more and more in this sector.

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17. Koirala and Acharya, 2000

**Table 7.1: Public investment in education: increasing budget prioritizing primary education**

Year	As a % of Gov. Exp.	As a % of GDP
1950's <sup>a</sup>	4.22	NA
1960's <sup>a</sup>	6.76	NA
1970's <sup>a</sup>	9.53	1.3
1980's <sup>a</sup>	10.18	1.72
1990's <sup>a</sup>	12.53	1.93
2006/07 <sup>b</sup>	19.46	3.09
2007/08 <sup>b</sup>	20.25	3.47
2008/09 <sup>b</sup>	22.10	3.79
2009/10 <sup>b</sup>	21.18	4.19

**Source:** <sup>a</sup>Koirala and Acharya (2000),  
<sup>b</sup>Economic Survey 2009/10

During Rana regime, with very few public schools, education was not government's priority. Altogether there were 321 primary and 11 secondary schools in 1951 (Bhatta, 2009). After the establishment of Ministry of Education in 1951, the government's role regarding education slowly increased. The role accelerated from 1970s, along with New Education Plan (1971), as government took the total responsibility of education system of the country. The government expenditure also proves the increasing involvement of government over the period (see adjoining box). At present years, government is allocating around 16 percent budget in education sector in its national budget. But the data of past years, the actual expenditure in education sector is about one fifth of the total annual government expenditure. The government had allocated 47.53 billion of rupees in education sector.

The distribution of education expenditure in different sectors is the mirror of education policy of a country that shows a country's priority. Looking at the distribution figure of education expenditure over the period, the expenditure pattern is shifting in the same direction.

The share of primary education is continuously increasing over the period while that of higher education is decreasing. The high decrease in primary education in 2009/10 budget is due to the entry of new program – School Sector Reform Project (SSRP). In this FY, 27 percent of the budget is allocated under the educational development heading where most of the budget is for SSRP. So one can consider this budget is also for primary education. It is worth to note that in an average 90 percent of the primary budget goes for teacher salaries. Unlike, primary and higher education, the share of secondary education in total education is somewhat constant.

**Table 7.2: Share of different sub sectors in Education sector Expenditure in Nepal (%)**

Particular	Decade of <sup>a</sup> Panchayat (1970-80)	Decade of Improved Panchayat <sup>a</sup> (1980-90)	Decade of Democracy (1990-98) <sup>a</sup>	FY <sup>b</sup> 02/03	FY <sup>b</sup> 07/08	FY <sup>b</sup> 08/09	FY <sup>b</sup> 09/10*
Mgmt. & Admin.	8.99	4.32	2.68	5.60	4.78	3.37	4.14
Primary & basic Education	23.60	38.60	49.90	59.02	57.00	60.65	36.89
Secondary Education	20.79	15.34	20.46	22.60	25.44	24.24	18.81
Higher Education	36.30	32.80	21.43	10.88	11.09	10.37	10.65
Miscellaneous	10.32	8.94	5.53				
Technical Education.	NA	NA	2.8 <sup>c</sup>	0.85	1.36	1.09	1.65
Educational Development	NA	NA	NA	1.05	0.33	0.28	27.86

**Source:** <sup>a</sup> Koirala and Acharya (2000), <sup>b</sup>: calculated from various Red Book, MoF, <sup>c</sup> : Bajracharya (2003)

The government expenditure in technical education seems very low over the period. In 1990s the average share on technical education was 2.8 percent ranging highest (5.1) in 1993/94 and lowest (1.0) in 1999/00..But in this millennium, the share of technical and vocational education on total education expenditure never crossed 2 percent.

### **Foreign aid in education sector: increasing attention, role and contribution**

Nepal has been receiving foreign aid in education sector from the initiation of planned development in 1950s. The first education plan was formulated by the financial and technical support of American aid. From multilateral donors such as the World Bank, Asian Development Bank European Commission and UN organizations to bilateral donors including INGOs, all have some programs in education sector. Generally, the multilateral financial institution provides loans whereas other donors provide grants. Earlier, only the grant component was used in education sector but Nepal took foreign loan first time in the FY 1982/83 in this sector. The first loan was from the World Bank for Mahakali Rural Integrated Development Program. Since then the share of loan component in total education aid is gradually increasing. The flow of more and more foreign aid gives an idea of increasing intervention of donor



agencies in Nepal's education sector.

The visible trend of up and down in the foreign aid financing in the education sector (see annex 1) gives an idea that foreign aid in education has come in a haphazard way rather than in a planned way. It means various programs are designed and implemented when donors give aid and close down when the donors withdraw.

However, the contribution of foreign aid in total education spending has shown two types of pattern. First, Nepal's education sector is getting more and more dependent on foreign aid. In 1974/75, the share of external financing was almost 10 percent which gradually decreased and reached to about 6 percent in 1990/91. This again started to go up from 1990/91 and reached to almost 25 percent in FY 2008/09. In comparison to overall development sector, education sector is being more dependent in foreign aid. The FY 2009/10 expected Rs. 14.09 billion on foreign aid (almost 30 %) in the total education budget of 47 billion. Second, loan component in education sector is gradually increasing. There was only grant component in education aid in FY 1975/76. In FY 1980/81, there was small share of loan which has gradually increased and it reached to almost 19 percent of total education spending of the country in FY 2007/08. For detail, see the following table.

**Table 7.3: Foreign Aid in Total Government and Educational Expenditure**

Rs. In 10 million

Particular	1975/76	80/81	90/91	00/01	07/08	08/09	09/10*
Total Gov. Exp.	191.3	409.2	2354.98	7983.5	13360.5	16134.9	28593.0
Total Foreign Aid	50.6	156.2	842.2	1879.7	2585.4	2930.1	7851.6
Grant	35.9	86.9	216.5	675.3	1580.1	2032.1	5695.6
Loan	14.6	69.3	625.7	1204.4	1005.4	897.9	2156.1
Total Education Exp.	22.9	38.4	208.2	1104.5	2706.1	3566.2	4752.7
Foreign aid	2.2	3.2	12.2	192.9	688.8	875.2	14,09.0
Grant	2.2	2.8	3.1	136.8	510.3	630.9	NA
Loan	0	0.3	9.1	56.2	178.5	244.3	NA
<b>In Total Government Expenditure</b>							
Foreign Aid (%)	26.43	38.17	35.76	23.55	19.35	18.16	27.46
Foreign Grant (%)	18.80	21.23	9.19	8.46	11.83	12.59	19.92
Foreign Loan (%)	7.63	16.94	26.57	15.09	7.52	5.57	7.54
<b>In Educational Expenditure</b>							
Foreign Aid (%)	9.55	8.20	5.87	17.47	25.45	24.54	NA
Foreign Grant (%)	9.55	7.37	1.48	12.38	18.86	17.69	NA
Foreign Loan (%)	0.00	0.83	4.39	5.09	6.60	6.85	NA

**Source:** Economic Survey 2009/10, Budget Speech 2009/10, MoF,

\* Budget estimate

During 1960s and 70s, donors' support was to help Nepal develop its education planning and basic government mechanism to deliver education services in the country. Then, 1980s experienced an integrated rural development program. But from 1990s policy intervention became the educational aid strategy. Basic and Primary Education Program (BPEP, 1992-2004) Education for all (2004 – 2009) and School Sector Reform Program (SSRP, 2010-2015) are the examples. The World Bank, ADB, FINIDA, NORAD, JICA, and DANIDA are other major donors and the SWAP (sector wide approach) and basket fund modality are being implemented. It is noteworthy that even the foreign aid contributes around one-sixth of total education expenditure of the country, it influences the total education investment of the country. Since 1990s, the target of education aid is to intervene in policy levels. It means, the role of foreign aid has been vital for the development of the education sector of the country. But the question is could we get substantial benefit from the foreign aid in education? Herein below are some of the examples:

1. Nepal invested foreign aid on teacher training. The stocktaking of the research on it shows that teachers are made confident, they knew teaching techniques, and yet they did not apply the learnt skills in the classroom (Subedi et. al., 2009).
2. Foreign aid was invested in university in a hope that its constituent campuses will be autonomous; now University Grants Commission has given the money to the affiliated private campuses meaning that public campuses cannot use the foreign aid properly.
3. Foreign aid was also poured in for the support of technical and vocational education. But the result shows that none of the government owned technical and vocational education centers could be independent. Only the foreign aid based project work have been found "successful"
4. Nepal invested the foreign aid in school/classroom construction. But the experience shows that none of these "fortunate schools" could develop maintenance fund so far: an effort towards institutionalization of the foreign aid.
5. Foreign aid encouraged government to transfer management of the public school to the community. A substantial number of schools have received the "package" to be transferred. But the question is how many schools will be interested to transfer their management to the community without this package. And how many schools could ensure quality education with this "package" and how many of them continued that zeal so far is yet to be known.

### **Philosophy of aid: Incompatibility between culture of donors and recipient**

There is contrasting philosophical difference between donors and

recipient in giving and taking foreign aid. First, according to eastern philosophy, donation is a benevolent action. The donor should not expect even a thanks or greeting for the donation from the recipients. Donors should not show any concern how the recipients use that donated money. But in case of foreign aid, donor agencies are providing the money of taxpayers of their citizen. Hence, donors are always concerned with the use of that money in recipient countries because they are accountable to their taxpayers. Moreover, donors are believed to provide foreign aid with some hidden agendas or their own commercial, political or strategic interests.

Second, foreign aid is a temporary solution that is supposed to be provided for a couple of years, especially during trying times. So that, in long run, the recipient countries recover and become self-dependent. But in reality, in case of Nepal, it never came true. Even, after six decades of continuous flow of foreign aid, Nepal is there where it was in the beginning. Moreover, the dependency syndrome has increased in such a way that even day-to-day activities have been unthinkable to run without foreign aid. Foreign aid has been an easy way for the rulers to stay in power and to suppress dissenting voices. Foreign grants are not to be paid back while future generation pays the foreign loan. So foreign aid has been the "*Ulphatko Dhan Phupuko Shradhha*" means money in aid, the devil send them down the drain for the rulers of Nepal.

### **Motive of aid: Are Marxist nearer to the reality?**

Since the beginning of 1950s, there is a big discourse in the development of third world with the help of foreign aid. The capitalists were in favor that foreign aid is not only helpful but essential for the development of third world. Along with great success of Marshal Plan, neoclassical structural model emphasize the role of capital accumulation in transferring the traditional subsistence economy to self-sustaining growth whereas foreign aid, for them, is the best solution to provide the scarce resources. Even for the modern economic case, foreign aid is the solution for the problem of developing countries.

But, the Marxists think that it is not only impossible to develop a country through foreign aid but it is even counterproductive. For them, the centre (rich countries) is actually inimical to the development of peripheral (poor) countries. The relationship between the centre and the peripheral is necessarily one of exploitation. Similarly, multinational corporations work as the power units of modern imperialism, while the role of state of the imperialist country is supporting them. Further, a small elite ruling class in the developing countries enjoys high income, social status and political power and this group tries their best to perpetuate the international capitalist system of inequality and conformity by which they are rewarded. In addition to this, Third World's underdevelopment is the result of faulty and inappropriate advice provided by well-meaning but often uninformed international experts from developed countries, assistance agencies and multinational donor organizations. These experts offer sophisticated elegant

theoretical structures and complex econometric model of development that often lead to inappropriate or simply incorrect policies. As a result, desirable institutional and structural reforms in the developing countries are neglected or given only cursory attention.

Looking at the result of the development process of foreign aid, Nepal's position is nearer to the Marxists' theoretical assumption.

### **Supporting public school: resulting expansion of private school**

Government is investing both the internal revenue as well as foreign aid for better access to quality education from the public schools. The salary and benefit of public schools are much better than the majority of private schools. Most of the public schools teachers are academically qualified, experienced and trained as well. If one takes the SLC result as the benchmark juxtaposed, the quality of private schools is much impressive. The citizens are compelled to send their children to the public school, just because they cannot afford the private school's expenses. Otherwise, there would be only a few students now in public school. Despite huge amount of government investment including foreign aid, the number of public school is shrinking while the number of private school is expanding with leaps and bounds. Could we think it as an "unintended effect" of this foreign aid against public school system? The answer to this question should be sought out at some point.

### **Investment in education: Making reserve army**

Now government is investing almost one fifth of its budget in education sector. If it is divided equally to the population, each family gets more than Rs. 8000 per annum. This does not account for the money spent by its citizen in private school and other educational investment made by other donor agencies outside budgetary system. But the return of education investment is not only unproductive but also harmful in many ways.

First, there is a culture that once the children come out of formal school education, even just completing primary level, they are not supposed to work in the field and seek the white color job. But the countries' situation is just opposite. New jobs have been the matter of dream in the country, even the opened industries are being closed. Hence, Nepal's present education system is just producing lazy products who neither get back to farm work nor get the white color job.

Second, the educational statistics show that less than 10 percent of population enrolled in grade one completes the high school education. As aforementioned, these dropped out children neither go back to traditional occupation nor get new job. But at the same time, due to the development of communication and other socio political development of the country, these groups of population are fully aware of their rights. Meantime, several political parties rope in these unemployed youth to fulfill their ulterior motives, as this group can be easily swayed by sugary promises. Hence, government investment in education is producing a bunch of thick heads

who can be manipulated by any shrewd institution.

### **Donors' investment in education: Benefiting recipients or donors themselves**

Foreign countries have been the destination for all Nepali youths whether they perform well or worse in education. Gulf countries have been the destination for those who do not get better results in education. At the same time, Europe, Australia, Canada and the USA are the destination for the educational cream of the country. Those who go to the developed countries hardly get back into the country.

In principle, education does not only increase the productivity of the economy but also helps in invention and innovation. But our excellent educational products are working for the developed countries. The country is getting zero from such a huge investment in education while the donor countries investing less than 30 percent of the total education budget of Nepal are getting the cream product of the education system. This bitter truth raises the question that for whom the donor countries are investing in the education sector of poor countries - for the recipient countries or for their own benefit?

### **Unsolved question: Where is the problem?**

Aforementioned discussion gives an idea that the whole development process of the country yielded more unintended and less intended results where foreign aid had a crucial role that had not only provided technical and financial support but also prescribed the development model in the country. Thus, it is worthwhile to find the answer to the questions below for the effective use of foreign aid in education.

- Is the idea of foreign aid itself wrong? If so, can we develop an alternative where a country's development process can be carried out without foreign aid?
- Is it due to the hidden agenda of donors and the ruling group of Nepal? If yes, what should be the mechanism in taking the decisions on foreign aid inflow and its uses?
- Is it due to the inappropriate development models that were copied and pasted from international experience? If so, how should we formulate appropriate development models?
- Is it due to the unsatisfactory role of organic intellectuals of Nepal? If so, how should we mobilize them to utilize the foreign aid?
- Is it the cultural mindset of the people towards foreign aid? If yes, how should we change this mindset?
- Is this the wrong area/priority of investment of the foreign aid? Which are the needy areas that we want to invest foreign aid in education?

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# 12

## Does Food Assistance matter? The Impacts of Food-for-Work in Mugu, Nepal's mid-western district

-Miriam Bishokarma

### Introduction

Food assistance is an issue that often gets into mires of controversy. While its life-saving roles in conflicts or natural disasters are unquestioned, its developmental role together with longer-term impacts on recipients are often questioned (BMZ 2005; Habte Bulgu 2008; OECD 2005). At the root of these doubts lies the assumption that food assistance would create “dependency” of recipients or recipient countries (e.g. BBC 2006; Elliesen 2002; Makenete et al. 1998; Moore/Stanford 2010).

In the Nepalese context this assumption on the dependency-creating aspects of food assistance is prevalent (e.g. Ghale 2009; see also the discussion in Nepali Times 2011a, 2011b). At the same time, the need for food assistance prevails due to high rates of undernourishment, especially in the mid- and far-western mountain regions of the country (WFP 2009c). The main agency of food assistance in Nepal is the United Nations World Food Programme (WFP), which distributed food to 1.6 million people in 2009 (WFP 2010b). The aim of such interventions is not only to save lives in emergencies, but to contribute to longer-term food security of recipients, thereby reflecting the organisation's double mandate of life-saving and developmental role (WFP 2008a). One main concept in this context is so called “food-based social safety nets”, which is part of a broader strategy to fulfil these double roles.

Despite these efforts by the WFP, in Nepal the assumption of the detrimental effects of food assistance seem to prevail, although till today there is a lack of empirically grounded studies that would support or dismiss such critique by analyzing the impacts of food assistance on recipients, and the ways it influences their livelihoods and longer term food security.

The aim of this article is thus to contribute to fill this gap through an empirically grounded study on the impacts of food-for-work (FFW) as distributed by the United Nations World Food Programme (WFP) in the remote Mugu district of mid-western Nepal. Its objective is to assess FFW's positive and negative impacts on recipients' livelihoods and their ability to deal with future shocks. The findings presented in this article are the result of a two months long field research in Mugu. The research was conducted between June and August 2009.

Section 2, introduces the theoretical background on which food security and food assistance was based, including the entitlements framework, research done on vulnerability to food security, and on aid-dependency. Section 3 presents the findings and elaborates on factors that lead to people's vulnerability to food insecurity, and the ways they cope with the permanent food crisis. section 4 outlines some observations on the impact of FFW on this context. The article concludes by presenting some general suggestions for policymakers and food aid agencies.

## **Food Insecurity and Food Assistance**

### **Assessing Food Insecurity**

Food security is defined as “a situation that exists when all people, at all times, have physical, social and economic access to sufficient, safe and nutritious food that meets their dietary needs and food preferences for an active and healthy life” (FAO 2002: 49). Accordingly, food insecurity is characterised as the lack of access to food (FAO 2009; Sen 1981). Amartya Sen (1981, 1984, 1995, 1999) explained food insecurity as being a result of social inequalities and failing entitlements. He defines entitlements as

“the set of alternative commodity bundles that a person can command in a society using the totality of rights and opportunities that he or she faces” (Sen 1984: 497).

Entitlement sets can be acquired through the transformation of a person's endowments, the initial ownership of assets and resources (Sen 1981). Sen distinguished four types of entitlements: production based (growing food), trade based (buying or trading for food), own-labour based (working for food) and inheritance or transfer based (being given food by others, including food aid as “relief”-entitlement) entitlements (Devereux 2001: 246). If the full range of a person's entitlements does not provide them with adequate food (e.g. when drastic food price increases disable people from purchasing food which corresponds to a decline in their trade entitlement) they face starvation. Hunger is thus not (always and only) caused by a decline in food availability but a result of a food entitlement decline.



These entitlements are embedded in the political economy of a society, framed by the ways of distribution of money and productive resources (Watts 2002; Watts/Bohle 1993a), and framed by dynamic formal and informal laws (Leach et al. 1999), as well as by policies and international agreements (Watts 2002).

Research on social vulnerability to food insecurity further embedded the entitlements approach into a longer-term historical perspective, taking into account the consequences of famine and the issue of recovery (Watts/Bohle 1993b). Social vulnerability is a relational concept that not only attempts explaining various factors and processes leading to the exposure to food insecurity but also stresses the ways people cope with it in order to maintain their livelihoods including food security (Bohle 2001). Vulnerability has therefore always an external side of exposure, including various risks, shocks, and stresses to which a person can be subjected; and an internal side referring to people's ability to cope with the situation (Chambers 1989: 1). Those persons are most vulnerable, who are most exposed to perturbations or stresses, who have the most circumscribed capability to cope with these stresses, and a limited potential to recover after the occurrence of a crisis (Watts/Bohle 1993a: 45).

People confronted with shocks often do not obtain the means to cope in a way that would secure their resources, and therefore rely on so called "devastating coping strategies" (Maxwell et al. 2003). These include the selling of assets such as productive resources, cattle or tools, or consumption of seeds, so that their potentiality to recover from shocks does seriously decline and their vulnerability increases.

This discussion suggests that food security, vulnerability, and entitlements are mainly qualitative issues. While quantitative data can provide information on household's income, number of cattle and size of productive resources such as landownership. The question of access to food is very much dependent on power relations. Assessing the reasons behind a certain endowment with resources requires a qualitative approach that not only describes the current situation (as quantitative data do), but that encounters the reasons for the differential distribution of assets and the entitlements. Access to food is not an absolute but a relative issue, as the case study below will demonstrate.

A way to reduce households' or people's vulnerability to food insecurity would be to support their entitlements by increasing/supporting their assets and endowments on which their entitlements are based, or to secure them from selling their assets in times of crisis. This is the idea of so called "productive safety-nets" which will be subject of the next section.

## **Food Assistance and Social Safety Nets**

Food assistance can be regarded as an alternate entitlement for people facing an entitlement decline. It attains the role of an alternative source of food that helps recipients to retain their assets, which they otherwise would have to sell in order to get food. As such it provides a safety net securing

people from falling further into poverty during crises (WFP 1999). It may also supplement already existent social safety nets as for example provided through the extended family, neighbours, or friends.

Such a safety-net approach is applied by the UN-WFP. In its most recent strategic plan for 2008-2013 (WFP 2008b), the WFP announced a “revolution” (WFP 2010a) by changing its approach from food aid to food assistance. While it is hard to determine any huge changes in the *meaning* of these two terms, however, the shift to food assistance entailed a change in strategies of how to tackle food insecurity, including an extended range of programming instruments, such as Cash-for-Work (instead of only food-for-work) (ibid). An important element of food assistance is “safety-nets”, in a working definition described as follows:

“Food-based safety nets provide direct, regular and predictable food assistance, in cash or in kind, to the most vulnerable people, to prevent them from falling below a minimum level of food security as a result of a shock, to increase their resilience to shocks and – in some cases – to promote their food security “ (WFP 2011b: 1).

The basic idea of food-based safety nets is to provide people who face hunger with a sufficient amount of food (or cash to purchase food) in order to help them saving their assets, such as cattle, machines, or land, which they otherwise would have to sell in order to get food. Food-based safety nets are part of WFP strategic objective number two, the prevention of acute hunger and the investment in disaster preparedness and mitigation (WFP 2008b: 16). The safety nets approach is not new to the WFP, and has been outlined already in previous documents of the organization (see e.g. WFP 1999, 2004).

Food-safety-nets are themselves a sub-set of social safety nets (FAO/ GTZ 2005) that are again elements of the broader approach of social protection, referring to transfer programmes that “seek to reduce poverty and vulnerability by redistributing wealth and protecting households against income shocks” (FAO 2006: 22). The FAO stresses that food-based safety nets do not only play a role in providing food during crises (which refers to the life-saving function of food assistance), but also play a role in the protection of, or investment in, assets (FAO 2006: 24). Therefore they combine short-term goals of securing people and their assets during crisis with longer-term goals of building resilience towards shocks and contributing to longer-term food security. The FAO also stressed the role of safety-nets in securing citizens’ right to food.

“assistance should be provided in a regular, reliable, timely and transparent way and must take full account of the needs and priorities of the rights holders” (FAO 2005: 3),

Barrett and Maxwell (2005: 209), however, criticize that safety nets do not work for people who are already in a state of destitution. These would need assistance for the *creation* and not (only) for the preservation of assets. This is the idea of “cargo nets” (ibid.) that aim at “increase[ing] the stock and productivity of chronically poor people’s productive assets so as to enable

them to climb out of chronic poverty and vulnerability” (ibid). If integrated into longer-term developmental programmes and objectives, also food-for-work can be part of such a cargo net (ibid: 131).

## **Possible Effects of Food Assistance**

The influence of food assistance on recipients has been discussed controversially; while some stress on the developmental and life-saving roles of food assistance, others blame food assistance for creating dependency, even resulting in a longer-term decline of recipients’ ability to cope with shocks and crises. The literature on food aid-dependency (Barrett 2006; FAO 2006; Harvey/Lind 2005; Lentz et al. 2005) offers a valuable entrance point to discuss these issues.

In these debates, the impacts of food assistance are differentiated into insurance- and transfer-effects. Both effects are resulting from food assistance induced incentives and disincentives that translate into livelihood decisions and actions. While insurance effects appear prior to the possible distribution of aid, transfer-effects happen only after the start of programmes. Both classes of effects might have positive or negative longer-term impacts on recipients’ food security.

### **Insurance-effects**

Insurance effects are resulting from recipients’ expectations regarding future assistance. They are a function of expectation, information and transparency of the (potential) distribution of aid (Lentz et al. 2005; Little 2008). Only when people can rely on the distribution of assistance they can readily depend on it (ibid).

Food assistance in this context can supplement already existing social safety nets (as provided in networks of mutual help, such as family, friends, or neighbours), and provide an insurance for those without access to alternative support during crisis. It can thereby enable people to take more risks in their livelihood decisions. On the other hand, the expectation of food assistance might simultaneously result in the “crowding out” of existing safety nets among neighbours and family, or induce a risk-taking behaviour that exceeds responsible levels. It might also make people producing less as they expect external food to be delivered (Barrett 2006; FAO 2006; Lentz et al. 2005). These effects can then result in the decreased capacity to deal with shocks independently from external assistance.

### **Transfer-effects**

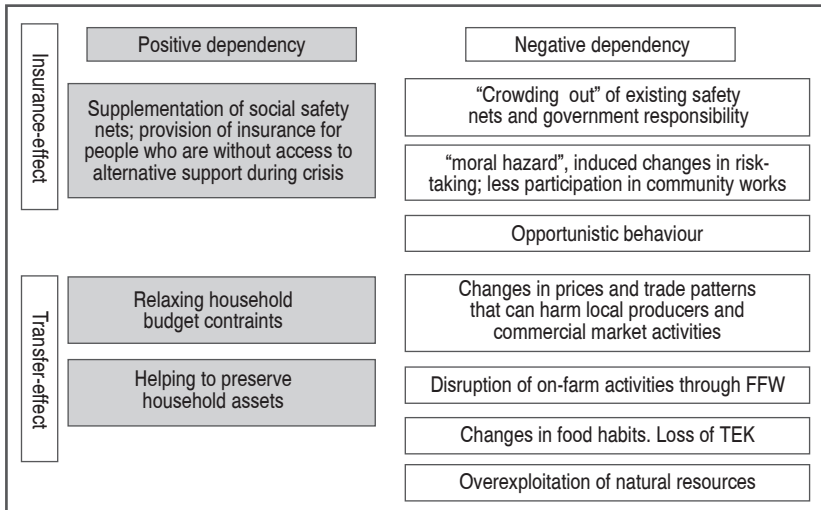
Transfer-effects emerge after the distribution of aid and reflect the function of food assistance as an additional transfer of assets to households (Barrett/Maxwell 2005: 131; FAO 2006: 28).

Food assistance in this context can be conceptualized as an additional entitlement. The basic idea of FFW thereby is to transform human capital or

labour into food, by providing participants a prescribed amount of food in exchange for their work in a community project. This way they are hindered from employing ‘devastating coping-strategies’ (OECD 2005), such as eating less, eating seeds, or selling productive assets in order to obtain food (Maxwell et al. 2003). As such, food assistance can attain the role of safety-net, preventing households from slipping further into poverty (OECD 2005), while at the same time aiming at the generation of assets to help recipients to increase their capacity to cope with shocks in future.

However, while FFW’s positive contribution is the relaxing of household assets constraints, and helping households to preserve assets, it might simultaneously lead to a decline of on-farm activities in favour of food-for-work, or the loss of traditional ecological knowledge, reducing the longer-term coping capacity of recipients, adding up to a “dependency-syndrome” (Barrett 2006; Harvey/Lind 2005; Lentz et al. 2005).

These positive and negative effects of food assistance are reflected in the definitions of “positive” and “negative” dependency. Positive dependency thereby refers to the intended life-saving functions of food assistance. “[D]ependence on external assistance enhances welfare, the alternative is destitution” (Lentz et al. 2005: 12). It helps recipients to meet basic needs when they otherwise could not. Yet, “when meeting current needs is achieved at the cost of reducing recipients’ capacity to meet their own basic needs in the future without external assistance” (ibid.) this is referred to as “negative dependency”. Figure 1 summarizes some of the possible effects of food assistance.



**Figure 1:** Possible effects of food assistance, adapted from Adhikari 2008; Barrett 2006; Harvey/Lind 2005; Lentz et al. 2005. TEK refers to Traditional Ecological Knowledge. Source: Bishokarma 2011

In this context, it is important to distinguish different types of food

assistance. While the bulk of food assistance is today provided in the form of emergency aid (FAIS 2011), a smaller part is distributed in the form of project or programme food aid (ibid). Further, there are several different ways of distributing food assistance, ranging from unconditional emergency aid, over school-feeding programmes, to conditional transfers in form of cash or food in exchange for work (for a discussion see: Barrett/Maxwell 2005). Among these, food-for-work (FFW) is still a famous and wide-spread tool for distribution of aid, although more and more cash-transfers are entering the field of food assistance (WFP 2010a). The present study focuses on the impact of FFW.

Before turning to this aspect however, a general overview about people's vulnerability to food insecurity and their food entitlements is due.

### **Living at the Edge – Food Security in Mugu**

The Karnali zone<sup>1</sup> in north-west Nepal belongs to the most food insecure area of the country (WFP 2010b). According to a sub-regional hunger index, it ranges into extremely alarming categories, with rates of undernourishment among adults of about 54 percent (WFP 2009c). Among the reasons for this high food insecurity are the rather low agricultural productivity due to low technization standards, small plot sizes, and adverse weather situations including droughts and hailstorms, the lack of access to regular employment opportunities, lack of roads and transportation facilities, resulting in higher commodity prices on the few markets, and the problematic health situation (UMN 2004, 2008; WFP 2009c: 21). The general lack of development is also reflected in the low Human Development Index, which ranks the region least in whole Nepal (UNDP 2004). Especially worse is the situation in Mugu district (ibid).

According to data of UNDP (2004), 68.5 percent of the children under five are undernourished and the share of population with a life-expectancy below 40 years is 40.3 percent. About 45 percent of the population does not have access to safe drinking water (ibid). Also in educational terms Mugu ranks far below other districts: only 5.2 percent of women are literate, compared to 41.6 percent of men (ibid). Other problems are the lack of electricity (despite some houses with solar-panels generating electricity), sanitation, and health facilities.

Although subsistence agriculture and animal husbandry form the main base of livelihoods in Mugu, they do not provide sufficient food due to low agricultural productivity. As the access to food is not guaranteed through these production entitlements, people have to rely on other sources of food.

People engage in various activities including labour migration or sale of Non-Timber-Forest-Products to fulfil their basic needs (Adhikari 2008). Yet, the combination of high food prices due to the lack of transportation facilities on the one hand, and the irregular and low incomes (UMN 2004, 2008) on

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1. The Karnali zone includes the districts of Mugu, Humla, Dopla, Jumla and Kalikot in the mid-western mountain-region of Nepal.

the other compromise people's exchange entitlements. Applied strategies are not sufficient to cover basic needs. Further, the decline of traditional coping strategies, including cross-border trade with Tibet, contributes to the populations' food insecurity (Adhikari 2008).

As a result large parts of the population (about 45 percent in summer 2009, WFP 2009b) face food insecurity in Mugu. Women often carry the greatest burden of coping as they are the ones who eat less or skip meals in order to feed their children and husbands (UMN 2004).

Although most recent reports have shown an improvement of the food security situation in the Karnali zone and Mugu (WFP 2011a), food insecurity in Mugu may not be regarded as a transitory problem, resulting from short-time declines in entitlements due to shocks. Rather, it must be regarded as a chronic phenomenon which is rooted in the century-old history of exploitation and marginalization of the region, and today prevails as a connection of poverty, powerlessness, and exclusion. The food crisis in Mugu is of a chronic nature and must be regarded as a prolonged phenomenon characterised by high exposure of large parts of the population towards various risks and low ability to cope with these mainly due to structural constraints and widespread underdevelopment. The "desperate search for coping options" (Shrestha 1993: 140) and the high dependence on the Indian labour market put livelihood security and food security even more at risk (Thieme 2006: 192 pp).

### **Food Security in a local Context**

The village where the case study was conducted is located near Gamgadi, Mugu's district head quarters. Data collection took place in August and September 2009, combining quantitative and qualitative research methods. Quantitative data were collected through a sample survey, conducted in 28 percent of the villages 117 households, based on a stratified random sampling (Singh 2007: 104) according to three wealth categories. It served mainly to derive a better overview about the basic characteristics of households such as family size, land ownership, sources of food, and health indicators. The core of research formed a qualitative assessment of the reasons for food insecurity, and of the impact of food assistance. The qualitative data were collected through various participatory tools, including social mapping, wealth ranking, seasonal calendar, and trend-analysis (Kumar 2002).

It must be stressed, that the findings only present observations from one village, which were however compared with a second village at a later stage of research; nevertheless, their applicability on other contexts in Nepal should be tested by further research.

The village consisted of 117 households, comprising three castes. 70 percent of households are Dalits (Lawad and Nepali), 30 percent Thapa (Rawad). In order to analyse the food security of different groups of the village, households were divided into three wealth categories, using a wealth-ranking-tool. Nearly 70 percent of the villagers were thereby classified as having huge problems maintaining their livelihoods; only three percent were

classified as being capable of maintaining their livelihoods without huge problems. Main distinction criteria for the categories were household size, number of children, amount and regularity of income, skill and educational level. Interestingly, food production indicators such as field size or amount of production did not serve as initial distinction criteria. Rather, participants of the discussion stressed that the endowment with land within the village was relatively equal, an observation which was also supported by the quantitative data of the sample survey. The wealth ranking partly reflected differences between castes with a higher share of Dalit households in the middle-and worse off categories, and a relatively higher share of Rawad households in the better-off one.

According to the three wealth categories, an analysis of households' vulnerability to food insecurity was undertaken.

### **Differential access to various sources of food**

The village's households are characterised by chronic food insecurity which stems from a combination of low production entitlements, and unreliable exchange entitlements. However, households preserve different entitlement sets which are based on their endowment with certain assets and also reflect their social position within the broader political economy.

Production entitlements are generally low and not only resulting from small plot sizes (0.4 ha in average, without huge differences between the interviewees) but also from the low standard of technization and the total lack of any irrigation facilities which exposes agriculture to the vagaries of weather, such as droughts. Although villagers stressed their equal endowment with agricultural land, there were differences between households regarding the sufficiency of food production. These differences could only partly be explained through differing household sizes, suggesting that there might be huge differences regarding plot size than told by the villagers. Although the own production sufficed for only 3 (in the worse-off) to 6 months (in the better-off group) of the year, all wealth groups stressed that their domestically produced food was their main and most important source of food. Further, it was regarded as the source which was easiest to access, in comparison to other sources such as the market, or relatives. Yet, as production entitlements are low, villagers engage in a range of other livelihood activities that combine their production entitlements with exchange and work-entitlements. These, however, displayed some clearer differences between the three wealth-groups.

Due to their employment in Government or NGOs many better-off households preserve more and relatively secure income so that it is easier for them to purchase the expensive food from the market. Those employed with the government usually hold higher degrees of education, suggesting that education is one determinant for attaining such jobs. Furthermore, through their linking social capital (Bohle 2005: 68), their access to the state subsidised rice (provided through Nepal Food Corporation, NFC) is higher, whereas other villagers often find it difficult to receive the amount of 10



kg rice per month. In addition, the NFC supplies subsidised rice to state- and NGO-employees through a quota system, allowing for more reliable distribution of this source of food for those working in these institutions. Other villagers – in comparison – often have to wait for days in order to be given some rice by the NFC under the ward system.

In comparison to those working in NGOs or governmental jobs, worse-off households often engage in irregular unskilled daily wage labour and thus earn less. This includes skilled or unskilled labour such as house construction, carpeting, portering, livestock farming or sale of herbs. A common form of employment is the so called *baure kaam*, a socially less valued work on other people's fields. This also includes the carrying and breaking of stones or sand and was regarded as an unpopular strategy by the villagers. As these income sources are rather unreliable, members of the worse-off wealth group depend more on networks of mutual help with other villages, the extended family or friends. Among such networks is the *lagi-lagitya* system, a traditional patron-client relationship where the *lagitya* (a member of the Lawad caste) provides services, mostly in terms of handicrafts – to one or more *lagis*, higher-caste members from different villages that provide a small amount of food in exchange. This system – however – was not regarded as an important source of food due to the small amounts provided. Another form of traditional exchange is *besaya*. This includes the purchase and exchange of food in lower places of the region (e.g. Jumla, Sinja), or from other villages, meaning that villagers have to leave their home for several days in order to bring (and carry) food. However, this source of food was not regarded as important because the food obtained was only sufficient for about two weeks of a year. Further, it was regarded as difficult to organize food from places as far away because one has to carry it. Some elder members of the Chhetri group also mentioned that going for *besaya* was regarded as a strategy which only lower-caste members of the village employed, suggesting its low social value. However, members of the two worse-off wealth groups spend about 10 percent of their income on food purchased through *besaya* in the month previous to the interviews.

Interestingly, a huge amount of money (about 40 percent of food expenditure of the worse-off group) was spent on the purchase of WFP rice, which had been intended for distribution to other more remote villages. Due to a lack of transportation in the summer months (when mules are on the high pastures), however, these recipients decide to sell their rice for a lower rate compared to the market price, instead of transporting it home, so that those villagers of the study village, which is closer to the airport, could profit from food assistance, although they had not directly been targeted by the programme in that time.

Another important source of food for the worse-off group is wild crops, reflecting the need to depend on freely available sources of food. The importance assigned to wild crops increased from the better- to the worse-off wealth group.

A common strategy among the two worse-off wealth groups is also



seasonal migration of men to India; sometimes even the whole family migrates. Only members of the middle- and worse-off wealth groups ever migrated to India, while those better-off stayed in the village.

To cope with acute lack of food mainly poorer households apply a range of devastating strategies such as selling of assets or eating less/skip meals. In many cases women bear the full brunt of coping with food and cash shortages, because they forgo their food consumption in favour of men and children. Among the strategies which villagers regarded as worst were the skipping of meals, sending children to others for food, and taking children out of school for work. These three strategies were only employed by members of the worse-off group during the study-period suggesting their higher food insecurity compared to the better-off groups. This observation was supported by the relatively higher numbers of children under five malnourished<sup>2</sup> and the alarming 31 percent of children that had died before reaching the age of five within the worse-off wealth group.

Summarizing, it can be stated, that wealth groups in the village correlate to different degrees of vulnerability to food insecurity, determined by broader social, political, economical, and cultural aspects. The most vulnerable households are those with low domestic food production per person, who do not have sufficient and regular income to purchase food at the market, who lack physical ability to purchase cheaper food from places further away, who lack social networks to migrate, who lack education to obtain more earnings through migration or local government/NGO work and who lack the linking social capital to NFC or parties.

The important question now is, whether food assistance influences these nets of dependence and inter-dependence (Harvey/Lind 2005: 35). The influence of food assistance in this context can only be understood *relative* to other sources of food and the access to them.

## The Impact of Food Assistance

In order to address the critical food security situation in Mugu, the UN World Food Programme (WFP) started its interventions in 2003, first through a Quick-Impact-Programm as a direct response to the armed conflict between Maoists and state forces. This and two other emergency operations were followed by various Protracted Relief and Recovery Operations (PRROs) starting in 2008 (WFP 2009a). While emergency operations are a direct response to declining food security of populations and have the main task to save lives, PRROs are situated to bridge the gap between rather short-term and longer-term developmental programmes (WFP 2008a). Their main objectives are relief and recovery (WFP 1998, 2008a). The initial aims of the PRROs in Mugu were to provide support to drought- and conflict-affected populations in order to (i) safeguard livelihoods and lives, and to create assets, and (ii) to support the return and rehabilitation of former

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2. Malnourishment among children under 5 was measured using the Middle-Upper-Arm-Circumference (MUAC) (see ACF 2008).

Maoist combatants (WFP 2009b). WFP describes the PRRO as follows: “Its three priority areas are: critical infrastructure development, return and reintegration, and non-formal education” (WFP 2009a). While the return and rehabilitation package was part of the overall UN peace mission to Nepal which started after the end of the civil war in December 2008, the livelihood support package is still ongoing. The aim of the livelihood support package is to reduce vulnerability and provide immediate food security while enabling people to create assets to improve their longer-term food security through FFW-activities (also referred to as: Food for Assets or Food for Enterprise). The basic idea of this activity is to provide food to needy communities during times of severe food insecurity. In exchange for the food assistance households work for communal asset-creation and -rehabilitation, e.g. the building of irrigation channels, schools, health posts or wells. These assets are expected to contribute to development and increase food security in the longer-term. FFW is therefore – according to its description – part of a social safety- and cargo-net in so far as it helps people to retain their assets, while at the same time contributing to the creation of assets (WFP/NDRI 2008: 7). It utilizes households’ labour endowment and transforms this into food resources on the one hand, and community assets on the other. Besides these activities FFW also includes supplementary feeding for children under five, and non-formal education for all participants. The PRRO from October 2009 to June 2010 covered 13 Village Development Committees (VDC) and reached 29,333 beneficiaries in Mugu. The total amount of food distributed was 1040 metric tons (WFP 2009a).

The study village had first received food assistance in 2003, and since then four more times (till 2008) under the FFW programming. In exchange for 40 days work (including 8 days of non-formal education) one person is provided 4 kg rice a day, summing up to 160 kg rice per working period. Sometimes also seeds or lentils are distributed. The distribution of rice and implementation of the program was carried out by local NGOs. The rice is transported by WFP helicopters and private airlines to the nearest airport (in Talcha) and must be picked up by the villagers. More remote villages are provided with money for transportation. The targeting of VDC wards is carried out based on a three-monthly Food Security Assessment carried out by local NGOs, government stakeholders, and the WFP field monitor, together comprising the so called food-security-network. Within the selected villages one member of each household is entitled to participate in the FFW-program. The decision of what will be constructed is taken by the villagers in a participatory way, a local user committee comprising different groups of the village, organises the work and food distribution at the village level.

During the time of data collection the study village did not participate in any FFW programmes so that the above described food security situation reflects the situation *without* food assistance, and the description of effects is therefore based on accounts of the interviewees.

## Insurance-effects

The study revealed that the insurance effects of food assistance were minimal. Although during WFP food provision, the assistance was regarded as an important addition to other sources of food, thereby increasing the overall well-being and feeling of security (see also discussion on transfer-effects), its role as an insurance prior to the distribution was minimal. This is mainly due to the fact, that potential recipients lack basic and timely information on the future provision of food assistance. Food assistance is therefore perceived as difficult to access. This lack of transparency was also reflected in the villagers' assumption that the selection of VDCs for the distribution of support was determined by powerful political leaders, their village fell from political grace, which served as an explanation for the current exclusion of the village from FFW. Due to the lack of information, food assistance becomes unreliable. As villagers do not know when food assistance might be distributed in future, they do also not adjust their livelihood strategies prior to the distribution, including migration to India, and engagement in domestic works.

Once, food assistance-programming had started, however, the provision is regarded as relatively timely and according to the schedule. General hindrances are the instable political situation in the Terai, recurrent *bandhs*, and adverse weather situations, hindering the transportation of rice.

Nevertheless, although people do not have information on the provision of food assistance, they have very high expectations regarding the future provision. This became especially prevalent in the worse-off wealth group indicating where food assistance plays a more important role.

To summarise, these findings put a question mark on the role of food assistance as a safety-net. The concept of safety-nets suggests that they must be regular, reliable, timely, and transparent (see FAO/GTZ 2005) to enable people to rely on it also prior to the concrete distribution of aid. Lack of transparency, and longer-term planning on side of the WFP, which is itself dependent on donors' funding decisions, hinder the proper application of food assistance as a full-fledged safety-net on which people can readily rely in times of crises.

## Transfer-Effects

Once the distribution of food assistance has started, it provides an additional source of food for the recipients in form of a transfer.

The findings of the study revealed that the food assistance's transfer effects were mainly positive. Households replied that through food assistance they were enabled to preserve their assets during crisis, and that all household members were able to consume sufficient food. Further, the reliance on less-privileged coping mechanisms such as migration to India, or doing *baure kaam*, declined during food assistance. Further, recipients reported a general improvement of their well-being, and an enhanced feeling of security. Also the need to exploit natural resources, such as the (illegal)

sell of firewood, declined. These findings were also supported by the sample survey, which stated that food assistance provided food for additional 1.4 months (in average). However, in one household the additional food was only sufficient for 0.4 months, suggesting, that the need for food aid changes according to household characteristics such as family size and amount of own production. Further, these findings reveal that the additionality to regular sources of food is rather low, and only relaxes household constraints immediately during and after the provision, but not in the longer term. Some villagers even described the food assistance as a “snack” not being sufficient to feed a whole family over a longer period of time. Nevertheless, the additional food supply seems to affect intra-household distribution, as some women stressed that due to WFP they could eat enough. Women of the worse-off wealth-group expressed their gratitude by comparing WFP with a king.

The findings further reveal that food assistance was not only an important factor for household’s assets-preservation, but also contribution to assets-creation. This includes the creation of human capital through informal education lessons, or the construction of infrastructures such as trails or buildings. Also social capital was positively affected, as during FFW implementation all members of the village regardless of their caste of economic wealth were working (and eating) together. Also the ability to support neighbours and friends increased due to food assistance as households had more resources to share, although the need for such help declined during food assistance provision.

However, despite the positive changes through the transfer of food, respondents mentioned several negative impacts. 45 percent of respondents mentioned time-constraints as a problem, as participation in FFW prevented them from engaging in domestic field work or employment. Although all interviewed households regarded domestic production as the most important source of food, the expected higher pay-offs and reliability of food assistance led to their participation in FFW. Yet, respondents stressed that they would never totally give up their domestic field work; rather, even during programme implementation they held down their jobs in free time besides FFW. This finding very much opposes perceptions of food aid-recipients becoming lazy due to food assistance. Rather, the engagement in food-for-work must be regarded as an additional strategy being combined with other activities. Other effects of time-constraints are the employment of children for domestic household works, instead of sending them to school, and conflicts among family members, reducing the overall feeling of enhanced security through food assistance. Furthermore, food assistance seems to create disincentives for participation in VDC community works because the payment by the VDC is comparable lower.

Another negative effect is the rising rates of air-cargo to Mugu; due to food assistance the demand for air-transportation increases, which translates into higher rates per kilo air cargo, making it difficult for local traders to bring goods at an achievable rate to the market. This also resulted in increased

commodity prices, therefore decreasing the affordability of goods for local consumers.

Food assistance in the form of rice is often believed to be responsible for changing recipients' food habits and decreasing their traditional ecological knowledge about wild crops, increasing their dependence on generally non-affordable items (Upreti 2008; Wahlberg 2008: 7). Indeed, food habits in the study village seem to have changed. The traditional staple food millet is now being replaced by rice, if available, consumed in the evening. It is however difficult to blame food assistance for changing food habits; rather, rice is also provided at the market in Gamgadi, and distributed by the Nepal Food Corporation (NFC). Locally grown millet is hardly available at markets, as producers usually do not sell it in order to consume it themselves. Further, food habits should be distinguished from food *preferences*. The preference for rice should be understood as a combination of cultural, practical and historical reasons. In Hindu culture doing *puja* using millet is simply not possible – rice is necessary. Also the previous presence of the Gorkhali state representatives<sup>3</sup> and their demand for rice (see Adhikari 2008) during travelling in Mugu should be regarded as factor contributing to the perceived social value of rice. Further, especially elders prefer to eat rice instead of millet because it is easier to digest. Women mentioned an ease in work load for food preparation as the preparation of millet bread was more time consuming. In this context the distribution of rice rather attains a wealth-enhancing importance. The consumption of rice has also not led to a decline of knowledge about the preparation and consumption of wild crops. On average, 78 percent of respondents answered that they taught their children about the use and preparation of wild crops. Therefore, it seems unlikely that FFW activities have any substantial long term impacts on food habits when rice is not provided.

.....  
3. This practice dates back to 1789 when the then Kingdom of Jumla was annexed into the rising Gorkha Kingdom, and the local peasantry had to provide extra services to state representatives including the free provision of rice, and carrying of heavy loads. This practice continued under the Rana-regime, so that elder people still remember this system of free rice-provision.

**Figure 2** summarises the perceived effects of food aid based on a trend-analysis.

	without FFW	with FFW
food sufficiency	00	0000
well-being	00	0000
sale of assets	0000	00
exploitation of natural resources	0000	00
time spend for employment	0000	00
need for mutual help in village	0000	00
confillcts in society	000	000
participation in community works*	00	00000
migration	0000	00
education (children)	000	00

**Figure 2:** Trend analysis presenting the results of a community discussion.

Summarising, the findings of the study suggests, that food assistance through FFW does help people securing their assets during crises, and increase their overall feeling of well-being and security. Contrary to the assumption that food assistance would result in the decline of recipients’ ability to deal with shocks, the findings show that food assistance does not replace other mechanisms of food acquirement but that it rather is an *additional* source of food on which people can rely in the short-term. It therefore does not replace but combine traditional sources of food. However, these positive effects of food assistance only prevail in the short-term. Neither prior nor after the distribution of food assistance does it provide additional security to potential recipients. This is mainly due to two reasons: on the one hand, FFW is not reliable and transparent enough to enable people to readily rely on it and adapt their livelihood strategies; on the other hand, its developmental contributions, e.g. through the construction of small-scale infrastructures, are not regarded as long-lasting and sustainable by the villagers. Instead of building the village path, or improving the school building, villagers would prefer to be given skills-training and other employment generating activities. Additionally, the VDC secretary criticised the lack of coordination between his office and the WFP. Finally, what villagers needed most was a water pipe, which could not be constructed due to limited resources for non-food items on side of the WFP. Therefore, instead of contributing to a longer-term improvement of the situation in the village, food assistance rather helped to sustain the status-quo, preventing villagers from slipping further into

poverty, but yet not helping them to build resilience for longer-term food security.

## Improving the longer-term Effectiveness of Food Aid

In ‘Hunger and Public Action’ (1989) Drèze and Sen describe the goal of public action as “mak[ing] it possible for all to have the capability to avoid undernourishment and escape deprivations associated with hunger” (Drèze/Sen 1989: 13).

So understood, famine prevention includes not only the protection of entitlements, but also their promotion (ibid: 65), including the access to health, to education or sanitation (ibid: 14). The ultimate goal of food assistance can therefore be described as entitlements protection, and the reduction of vulnerability to food insecurity through an active entitlements *promotion*, including fostering people’s ability to cope with shocks and crises on their own.

Safety-nets must be regarded as a valuable first step towards this goal. However, research findings suggest, that in order to cover the entitlements promotion aspect safety-nets should be complemented by cargo-nets, which actively support people in climbing out of poverty through assets-creation (see discussion in section 2.2). Such an approach, however, can only succeed, if the broader socio-political context, as being constructed by beliefs and values, and determined by power-relations, in which entitlements are embedded, is addressed by an integrated policy. Only by changing these very *structures* entitlements protection and promotion can be successful – the provision of food to recipients on the local level can only be part of such a broader strategy. The differential vulnerability to food insecurity among the three wealth-groups of the case study suggests that among these structures is not only the access to education, which allows for better and regular employment, but also health infrastructures, access to roads in order to stabilise market prices, and the ways of distribution of subsidised rice through the NFC to name but a few. Most important seems to be a shift in attitude on the side of the Government of Nepal, from an attitude of neglect to an attitude of support towards Mugu and the Karnali region.

There is a need for understanding and addressing the power relations that determine people’s access to various sources of food. More in-depth studies that address these aspects grounded in a qualitative methodology are needed in order to better understand the working of entitlements and to find possible ways to promote them in the longer-term. Only qualitative research can complement the mere descriptions of food security indicators by an understanding of the factors *behind* such numbers.

Obviously, food assistance can always only be a part of the solution and must be embedded into broader developmental programmes, designed in cooperation with the Government, other donors and civil society. Such a strategy must be based on the needs of food insecure populations. Food assistance has a huge potential also to address the longer-term needs of

recipients, as it covers geographically huge areas, and connects these over a network of NGOs and local implementing partners. However, standing alone it might not be more than a drop in a bucket. Only embedded into a broader joint approach the longer-term developmental effectiveness of food assistance can be increased. This includes the closer cooperation with Government offices at the district and local levels.

The recent WFP country-strategy already takes many of these points into account, thereby stressing the role of WFP in providing a productive safety-net:

“This approach will address immediate hunger and under-nutrition in the face of shocks while helping households and communities become more food and nutrition resilient in the medium to long term” (WFP 2010b: 2).

One of the means to attain this goal is the building of assets and knowledge to improve agricultural production, access to market and the development of alternative livelihoods (ibid: 25) through food/cash-for-work modalities. This might include support for micro irrigation, green house construction, cultivation of high value cash crops, or the support of farmer cooperatives, to name but a few (ibid). Other priority objectives in this context are measures to increase access of vulnerable populations to government and non government services such as health care and education, and capacity building on the Government level (ibid: 24, 26).

These outlined activities reflect WFP’s attempts to work towards more sustainable solutions of hunger and food insecurity, but do only partly reflect the underlying causes of people’s vulnerability. Although the general approach of WFP towards a more developmental role in this context should be welcomed, it lacks a clear strategy of implementation which shows what concrete role food assistance could play embedded into broader developmental programmes that tackle underlying reasons of food insecurity and poverty.

### **Based on this short discussion, following policy recommendations are derived:**

- Work towards the design and implementation of a joint strategy for the eradication of hunger in Nepal.
- Define the role of WFP and food assistance as part of a broader developmental strategy that aims at reducing people’s vulnerability to food insecurity.
- Conduct an in-depth study on the *underlying reasons* of food insecurity and entitlements-decline, in order to understand hunger as determined by broader political, economic and social structures, and to define ways to foster food security in such contexts.
- Think about accomplishing the concept of safety-nets by the concept of cargo-nets, helping vulnerable people out of poverty, instead of preserving a status-quo.
- The implementation of these suggestions might be first steps towards



a situation, where people can lead a healthy and happy life free from the fear of hunger and starvation in future – without food assistance.

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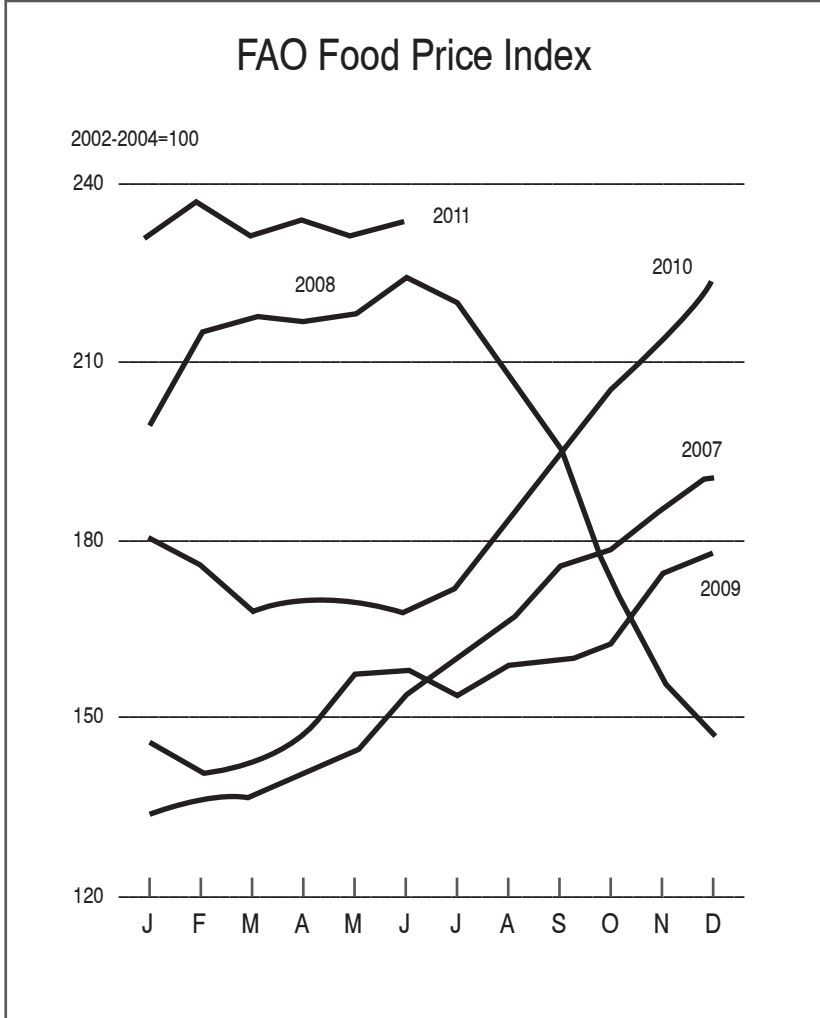
## Food prices, food security and aid

–Chandan Sapkota

The global food prices have been rising rapidly and have exceeded all levels recorded in the past. Recently, the Food and Agriculture Organization's (FAO) Food Price Index surpassed the upper bound reached during the peak of the food crisis in 2008 (see Figure 1). The World Bank says global food crisis has reached "dangerous levels". In Nepal, the World Food Programme (WFP) argues that about 3.7 million people are at risk of food insecurity (Sapkota, 2011a) even though the government maintains that the nation as a whole will have food surplus of about 110,000 tonnes in fiscal year 2010/11 (TKP, 2011). Sadly, the increase in output is not reflected on rising food prices, which have reached the second highest level since 1990.<sup>1</sup> Yet still 38 districts in Nepal are having deficit food production.

1. See 'Update on food security in Nepal (2010-11 is surplus year) at <http://sapkotac.blogspot.com/2011/06/update-on-food-security-in-nepal-2010.html>

**Figure 1: FAO Food Price Index (2002-2004=100)**



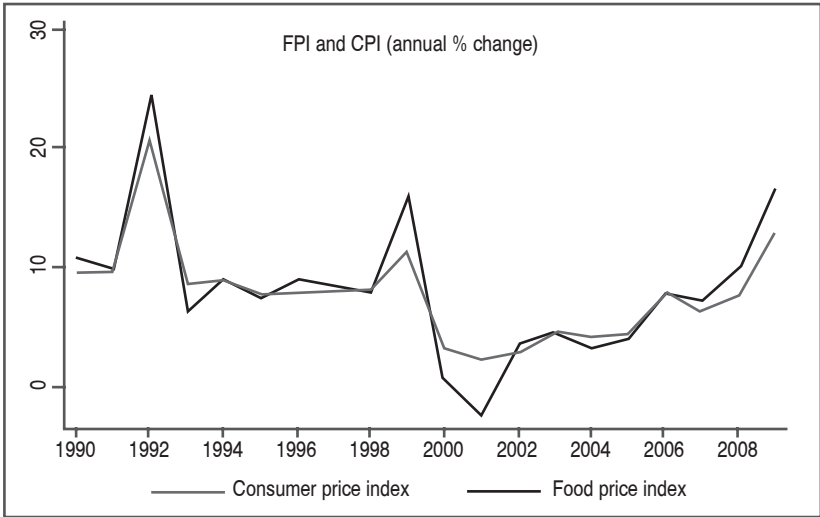
Source: FAO 2011<sup>2</sup>

2. FAO Food Price Index <http://www.fao.org/worldfoodsituation/wfs-home/foodpricesindex/en/>

## Rising food prices

The consistent upward trend in food prices might push more people below the absolute poverty line.<sup>3</sup> This could undo the recent astonishing achievement in reducing absolute poverty to 13 percent of population in the past six years as revealed by the forthcoming Nepal Living Standard Survey III report (Khanal, 2011). It is estimated that a 10 percentage increase in food prices will increase the number of poor people living below US\$1.25-a-day by 0.6 million in Nepal (ADB, 2011).

**Figure 2: Nepal's food price index and consumer price index (annual percent change)**

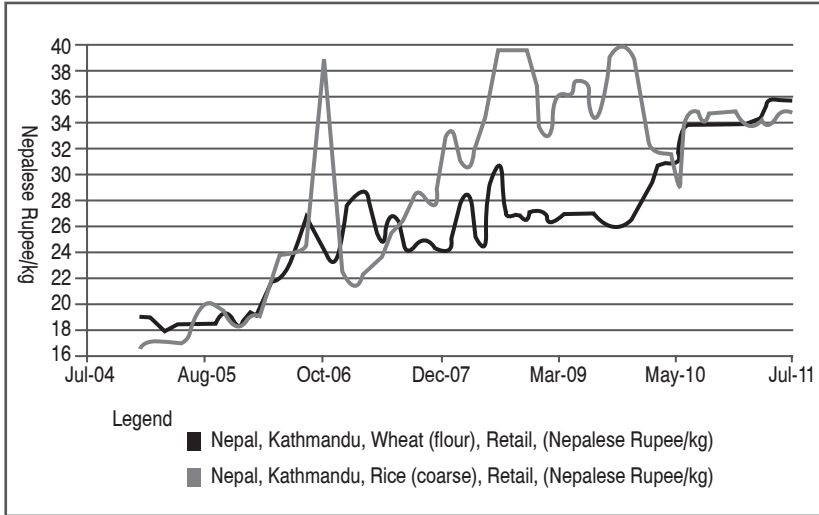


Source: *Key Indicators for Asia and the Pacific 2010*

Domestically, food prices are fast outstripping overall general prices. The Food Price Index (FPI) has been continuously dragging up Consumer Price Index (CPI), whose annual percentage change is a popular measure of inflation (see Figure 2). Note that higher inflation means more erosion of purchasing power of people. Production deficit is one of the major reasons for the spike in food prices. Figure 3 shows that retail prices of wheat and rice in Kathmandu are fluctuating and rising especially after 2006. Since rice and wheat are two major daily food items consumed by most of the households, rising prices and high price volatility adversely affect food consumption, and food accessibility and availability.

3. The World Bank economists argue that about 44 million people fell below the poverty line of US\$1.25-a-day due to high food prices between June and December 2010. See Ivanic, M., W. Martin, and H. Zaman. (2011).

**Figure 3: Retail price of wheat and rice in Kathmandu (nominal NRs per kg)**



Source: FAO<sup>4</sup>

Since Nepal does not produce anything like enough food to meet domestic food requirement it has to import food equal to domestic production deficit. So, shocks in production, supply and prices of agricultural goods at the global level affect food prices in our local market as well. In 2009, agricultural trade deficit was US\$270 million, up from US\$157 million in 2003.<sup>5</sup> Since the demand for food doesn't go down at price surge, Nepal will be importing at least the same amount of food even if prices skyrocket. That means it has to spend substantially more to import the same quantity of food. This will negatively impact the already high trade deficit and government expenditure available for other development activities. Meanwhile, donors will have to redirect funds to address rising food prices instead of implementing already planned development activities.

Globally, rising temperatures, shifting season pattern, more frequent and extreme weather events, flooding, wildfire, and drought in Russia, Canada, Australia, Pakistan, China, Argentina, and Kazakhstan, among others countries result in production shocks. Meanwhile, supply shocks occur when major exporting nations take preemptive measures to curb exports or put embargos on certain agricultural products – so much so that their own domestic demand is met and prices remain below a stipulated threshold for their citizens. For instance, supply shock occurred recently when India, Russia and Vietnam, among other nations imposed food grains embargo. Additionally, speculation by brokers and investment firms, who bet on the future price of major agricultural items based on account of production,

4. Data extracted from FAO's GIEWS food price data and analysis tool (<http://www.fao.org/giews/pricetool2>)

5. Author's computation using UN Comtrade database (<http://www.comtrade.un.org/>)

inventory, and future expected production level, have also contributed to price shocks (HLPE, 2011).

All of these events have not only affected demand, supply, and prices of agricultural goods at the global level, but also, to some extent, our own economy. A Nepalese citizen spends, on average, 59 percent of his income on food. Of this about 58 percent and 15 percent are spent on breads and cereals, and fruits and vegetables, respectively.<sup>2</sup> Since food prices are already high in the domestic market, any further price rise will force more people to scale down discretionary expenditures and savings, which will directly affect savings, investment and economic growth.

## **Donors' role**

The failure to address the impact of rising food prices will have adverse effect on the progress made in achieving Millennium Development Goals (MDGs) on poverty and malnourishment. As mentioned earlier, rising food prices might undo the astonishing achievement in reducing absolute poverty. Worse still, it might worsen malnutrition, which is at “alarming” level since 1990 (Sapkota, 2011b). Achieving the MDGs is one of the top priorities of donors. The multidimensional impact of rising food prices and deficit food production will have an impact on the progress on MDGs and warrant increased donor focus and intervention.

Since aid money is limited, it has to be spent efficiently in the most targeted projects and programs. There is no central estimation of how much food aid Nepal receives each year. However, multilateral and bilateral donors such as WFP, USAID, DFID, ADB, and WB among others donors are launching projects and implanting interventions to address food insecurity in Nepal. While WFP is focused on addressing the emergency needs, the others are primarily assisting in increasing production and productivity in the agriculture sector, which has not received much attention from the government except for the customary budgetary allocation for subsidies and irrigation projects in various districts.

Aid intervention should primarily focus on increasing production and productivity in the 38 food- deficit districts. Some of these districts bear such geographical terrain that it is unfeasible to produce goods that are consumed daily by households. In such cases, both the government and donors should focus on facilitating supply of essential food items. This might mean subsidizing transportation costs and building roads network. The right kind of intervention depends on the remoteness of food deficit districts. Meanwhile, donors could also assist in funding temporary conditional and unconditional transfers and safety net programs depending on local context. Providing in-kind assistance (food and other necessary household items) in return for manual agriculture works in villages could also help to tackle both rural unemployment and food insecurity problems.<sup>3</sup>

As always, the first priority should be to dampen rising food prices in food deficit districts. This should be followed by interventions aimed at increasing production and productivity.<sup>4</sup>



## Way forward: Tackling rising food prices & insecurity

Apart from specific interventions in food deficit districts, the following recommendations will help address the effects of rising food prices and low food production in Nepal.

First, there should be higher investment geared towards increasing agricultural production and productivity so that production deficit can at least be narrowed down. Meanwhile, domestic production of climate resilient varieties of food grains should be encouraged. Equally important are state subsidies on appropriate varieties of seeds and fertilizers, plus some sort of guarantee to facilitate transport of surplus production of each household to the market. The government and development agencies should provide sufficient infrastructure and policy structure to facilitate this process.

Second, to facilitate unhindered access of agricultural items to the market, food cartels should be reined back. The agricultural traders, who are mostly affiliated to one party or the other, get dirt cheap food items (especially veggies) from farmers and sell them in the market with a wide margin. If prices start to come down, then they slow down the supply to hike up prices. This sends deceptive, undervalued price signals to farmers, who are neither encouraged to produce more nor are motivated to seek innovative methods to produce improved varieties of food items crucial for food security and for putting downward pressure on prices. The supply-side bottlenecks have to be tackled in favour of encouraging farmers to produce more and motivate them to seek innovative farming methods as well as to curb price manipulation and hoarding of agricultural goods. The market monitoring and successful cases of good governance intervention conducted by donors might help if they are put to good use in this case.

Third, smooth regional agricultural trade is crucial to meet Nepal's food demand. Since agricultural imports from India constitute over 40 percent of total agricultural goods imported by Nepal, it is in Nepal's interest to convince India—a net exporter of agricultural goods—to make an exception, or at least to ensure quota that is enough to meet its domestic needs even if India puts an embargo on food export to other countries. Since Nepalese and Indian population consume pretty much the same kind of food items and the two countries share an open border with free flow of pretty much all goods and services, it is in both countries' interest to smoothen trade. Or else, the negative political and economic spillovers and black marketing will further plague the region, on both sides of the border. Moreover, greater cooperation on agricultural trade among South Asian countries could also help to ease food deficit.

Fourth, a fully functional regional food bank is needed for contingency arrangements in South Asia. The 14<sup>th</sup> SAARC Summit held in New Delhi in 2007 agreed to establish SAARC Food Bank, which is expected to serve as a regional food security reserve for SAARC member countries facing recurring food shortage and emergencies. The food bank was authorized to start off with a total reserve of 0.24 million tons of food grains. Since this amount is not enough to ensure regional food security, Bangladesh recently proposed

to raise the strategic reserve to 4 million tons. Sadly, the whole concept of SAARC Food Bank is yet to become materialize. There is a need to address the issue of price incentive and access threshold to enable the release of grains from the reserve. The donors that are running projects on enhancing regional integration should look into this aspect as well.

Fifth, and most importantly, it is high time political leaders, and officials at National Planning Commission, Ministry of Finance, Ministry of Agriculture & Cooperatives, and Ministry of Commerce & Supplies woke up and acknowledged the fact that rising food prices and a potential food crisis pose a real economic threat and could engender political instability. They have to plan and work in tandem to eschew intensification of food crisis and its spillover on the economy and political fronts. Furthermore, donors and government have to look at short term and long term options to tackle food insecurity. The short term measures include providing immediate assistance, targeted subsidies, and implementing safety net programs. The long term measures include programs to increase production, productivity, availability and accessibility.

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# 14

## Food Insecurity in Nepal: A Poverty and Social Exclusion Nexus

—Ganga Dutta Acharya

*Over the past decade, food security has emerged as one of the prominent policy issues in development debates in Nepal. A number of events have brought the question into sharp focus in later years. Reports of more than one fourth of the population forced to go to bed hungry every day, the media's spotlight on food shortages, starvation and malnourishment in various districts of the country, growing activism of NGOs against the plight of the hungry, visible impacts of globalization on agriculture and farmers—all make this issue prominent in policy discourses.*

*This paper briefly examines the food security situation of the country and reviews the obligations and initiatives by the government and external development partners to ensure food security. This paper mainly argues that food insecurity problems in Nepal largely bear the structural causes while almost all interventions seek technical fix grossly ignoring the fundamental issues of structural transformation. As a result mainstream interventions are less relevant, poorly targeted and ineffective for the poor and excluded.*

**Key words:** Food security, Right to Food, Chronic and Transitory Food Insecurity, Food Aid, Poverty, Exclusion

## Background

Food security and freedom from hunger is considered as a fundamental human right in international human rights treaties including the Universal Declaration of Human Rights (1948), the International Covenant on Economic Social and Cultural Rights (1966) and the Convention on the Rights of the Child (1989). Feeding the hungry that are unable to feed themselves is almost universally regarded as a compelling moral obligation. International community has well recognized this issue as one of the most important goals of the Millennium Declaration is to halve proportion of people who suffer from hunger by 2015<sup>1</sup>. Since then food security has become one of the key issues in policy debates particularly in developing countries.

The World Food Summit held in 1996 precisely defined the concept of food security as a situation *when all people, at all times, have physical, social and economic access to sufficient, safe and nutritious food to meet their dietary needs and food preferences for an active and healthy life*<sup>2</sup>. Thus, food security is a multidimensional socio-economic phenomenon that integrates at least following four interrelated components

- **availability** of food,
- physical and economic **access** to food,
- biological **utilization** of the food and
- **stability** of food supply.

For a long time, food security meant ensured availability of food (through production, imports or food aid). After Amartya Sen's seminal work, *Poverty and famines* (1981), it has increasingly been understood that the availability of sufficient food in the right place and at the right time is a necessary condition, but it is not sufficient to avoid hunger. A well-stocked food market is irrelevant to those who do not have enough income to purchase food. Similarly, enough income may also matter less if insufficient food is available in the market. Households and individuals must always have physical and economic access to food through their own production, purchases in the marketplace or transfers via social safety nets.

Recent thinking has added to the concept of utilization as a dimension of food security. Adequate access to food matters little, if people have poor physiological ability to utilize the food they intake due to their poor health and sanitation status. Thus non-food inputs such as education, clean drinking water, sanitation and health care are considered equally important for food security. Finally, stability is also an essential element of food security because even temporary interruptions of food availability, access or utilization can have serious long-term consequences. Household food security is meant to apply these concepts to the family level, with individuals within households as the focus of concern.

Food insecurity is a situation opposite to the above where people lack

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1. United Nations Millennium Development Goals ([www.un.org/millenniumgoals](http://www.un.org/millenniumgoals)).  
2. WFS (1996). Declaration of the World Food Summit 1996 (Para. 1)

secure access to sufficient amounts of safe and nutritious food required for normal, active and healthy life. If a household or individual faces deficiency in minimum food requirements only for a short-period of time generally arising from natural and human induced catastrophes such as natural disasters, wars and conflict, it is regarded as the **short-term or transitory food** insecurity. A situation emerged as a long-term or persistent inability of individuals or households to meet minimum food consumption requirements is regarded as **chronic food** insecurity.

A chronically food insecure household is generally deprived in multiple dimensions- combinations of capability deprivation, low levels of material assets, and socio-political marginality making them unable to secure minimum food consumption requirements over long periods. Such a situation is generally associated with the structural factors which frame the availability, access, utilization and stability dimensions of food security. It is important to note here that the natural and human-induced catastrophes are normally responsible for around 10 percent only of all hungry and malnourished people in the world; while 90 percent of the hungry suffer from chronic food insecurity<sup>3</sup>.

## Food Security Situation of Nepal

Over the past decade, food security has emerged as one of the prominent policy issues in development debates in Nepal. A number of reasons have brought the question into sharp focus in later years. The media's spotlight on food shortages, starvation and malnourishment in various districts of the country, growing activism of NGOs against the plight of the hungry, visible impacts of globalization on agriculture and farmers—all make this issue prominent in policy discourses.

Food and nutrition security situation of Nepal is grim as the country is persistently failing to adequately feed more than a quarter of total population. It is estimated that nearly 7 million out of about 27 million populations of Nepal go to bed hungry every day in 2010<sup>4</sup>. Nearly 40 percent of children below the age of five suffer from protein-energy malnourishment<sup>5</sup>.

As nearly 96 percent of hungry poor live and work in rural areas<sup>6</sup>, it is predominantly a rural phenomenon in Nepal. Substantial disparities exist by caste, ethnicity, gender and geographic regions also. Generally, *dalits*, ethnic minorities and women are more vulnerable to hunger than other groups. Due to prevalence of caste and gender-based discrimination these groups are deprived of resources, opportunities in virtually all aspects of daily life resulting with lower levels of human and productive capital.

3. FAO (2006). The State of Food and Agriculture. Food Aid for Food Security? Rome: Food and Agriculture Organization of the United Nations
4. WFP (2009). A Sub-regional Hunger Index for Nepal.
5. National Planning Commission (2010). Nepal Millennium Development Goals Progress Report.
6. Central Bureau of Statistics (2009). Report on the Nepal Labour Force Survey.

Some 40 percent of the population does not have access to minimum calorie requirement, with a higher proportion in the Mountain regions (45%) followed by Hills (42%) and *Terai* region (37%)<sup>7</sup>. People in the high mountains and western hills are more vulnerable and experience higher frequency of food shortages than the *Terai* and eastern parts of the country<sup>8</sup>. In most remote mid- and far- western hill and mountain districts, local food production sometimes covers just three months of annual household needs, affecting almost two third of the population<sup>9</sup>.

### **Causes of Food Insecurity: Social Exclusion and Poverty Nexus**

Globally, food insecurity is largely a situation created not by lack of food but by poverty and exclusion which deny people access to food. This is true for Nepal as well. Nepal when achieved self-sufficiency in food production, still failed to avoid hunger and malnutrition at household and individual level. Even in the current year national statistics show that domestic production of edible cereal grains is more than adequate to feed every Nepalese<sup>10</sup>. Still, more than a quarter of total population of the country goes to bed hungry every day. Therefore, food security challenge is not to just produce enough food but ensure required level of food energy intake at household level.

Food insecurity is a question of mal-distribution of resources and inequality. The resource-poor are hungry and malnourished not because there is no food but because they cannot afford the food. Therefore, it is not the matter that sufficient food is produced, but who produces it and for the benefit of whom.

Hunger and poverty are closely interlinked and interdependent phenomena. Inadequate access to productive resources such as land, irrigation, seeds, inputs, credits and markets or other sustained means of incomes is the root cause of hunger and malnutrition. Poor have denied access to such resources and services. Social exclusion is one of the main causes of poverty. Hunger is the obvious manifestation of poverty and poverty itself is an outcome of systemic exclusion. Social exclusion primarily driven by institutions and processes on the basis of gender, ethnicity, caste and geography uphold or exacerbate income- and capacity-poverty. The ethnic, indigenous, tribal and occupational caste groups and women have continuously been excluded from socio-cultural and economic mainstream of the country. As a result, ability of these excluded communities to access and control over productive resources and opportunities is extremely limited in Nepal resulting into persistent poverty and hunger.

Land is the principal source of livelihoods in rural Nepal. Unfortunately,

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7. NPC (2007). Three Year Interim Plan (2006/7-2009/10 ). National Planning Commission, Singhadurbar, Kathmandu, Nepal.
  8. National Planning Commission (2010). Nepal Millennium Development Goals Progress Report
  9. *ibid*
  10. Preliminary estimate of MoAC as of October 2011 (Personal Communication with MoAC authorities)

the distribution of this valuable productive resource is highly skewed. More than fifty five percent of the farm families are either landless or hold less than 0.5 ha of cultivable land in Nepal (table 1). Over 70 % of peasants operate on less than one hectare of land<sup>11</sup>. A majority of the fertile land in the country is held by absentee landlords who principally derive their means of living other than farming.

**Table 8.1: Distribution of land in Nepal<sup>12</sup>**

Farm families types	Number	Land holding size/family	percentage
Landless	287100	0-0.1 ha	10.13
Marginal cultivators	6,70,000	0.1-0.3 ha	23.63
Small farmers	6,48,000	0.3-0.5 ha	22.86
Medium farmers	1131560	0.5-3.0ha	39.92
Big farmers	93700	3.0-10.0ha	3.33
Very Big farmers	3800	>10 ha of land holding	0.13

Nepali society is highly diversified in terms of caste, class, gender, ethnicity, language and cultural patterns. Gender-bias against women is a well established historical and socio-cultural legacy of Nepalese society governed by patriarchal Hindu ideology that largely limits their access to land, income and employment opportunities making them more vulnerable to food insecurity<sup>13</sup>. Extreme forms of discrimination are found against women at household and community level though the law has given equal opportunity.

Nepali society is comprised of 37% of the indigenous population belonging to 59 different nationalities with more than 100 different dialects<sup>14</sup>. Unfortunately, majority of the indigenous people of Nepal were systematically discriminated in national unification process. The so-called high caste Hindus hailed from Nepal's western hills controlled the state politics since the 18<sup>th</sup> century and gradually *Hinduized* the entire indigenous population (who are not the Hindus by origin) of the country. In more than 238 years long rule of Gorkha kings, the indigenous communities were forced not only to lose their identity but also the traditional means of livelihoods and were pushed into the margins.

Indigenous people's food system cannot be understood outside the context of their cultural practices. For them the means of livelihoods such as land traditionally tend to have a collective dimension with the ownership rights largely vested on the community as such, for example *Kipat* system among *Limbus* of eastern Nepal. This traditional system of land ownership

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 11. Central Bureau of Statistics (2009). Report on the Nepal Labour Force Survey  
 12. Report of the High Level Commission of Scientific Land Reforms, Nepal (2010).  
 13. Pandey, Devendra Raj (2000) Nepal's Failed Development: Reflections on the Mission and the Maladies. Kathmandu: Nepal South Asia Centre.  
 14. <http://nefin.org.np>

and possession came under strain with the introduction of private land ownership system and systemic attempts made to break collective control of land to allow for privatization. Due to this state intervention, indigenous communities like *Limbus* and *Tharus* have become poor and food insecure today.

Besides, some other indigenous communities such as *Bote*, *Majhi*, *Chepangs*, *Raute*, *Raji* etc traditionally dependent upon forest and other natural resources are also systematically denied to access their traditional means of livelihoods making them poor and more vulnerable to food insecurity. In fact, indigenous people's food system cannot be understood outside the context of their cultural practices.

Similarly *Dalits* represent about 20 % of Nepalese population. The Hindu hierarchical system discriminated entire *Dalit* communities characterizing them as so called 'untouchables' alienating them as servant class of the society, thus systematically denying their access to land and other productive resources. Although untouchability was abolished in the revised Civil Code (*Muluki Ain*) of 1963, discriminatory practices continue even today barring them to access wider livelihoods options.

Due to the persistent exclusionary value system and practices, all types of productive resources-land, forest and water- as well as other livelihood opportunities available in the societies have virtually been captured by the high-caste male elite classes. In an agrarian economy, the landed elites at local power structure are always dominant to influence all sorts of decision. Without breaking this unequal and unjust social relation of power at local level it is hard to realize the food security goal of poor and excluded in Nepal.

In addition to the above, globalization and integration of national economies to the international markets and corporate world has widened inequality. With the adoption of Structural Adjustment Programs (SAP) in mid 1980s, nearly 30 years of rampant hegemony of the market-led model of economic growth has been in practice in Nepal that has clearly demonstrated the increased privileges for the few, increased concentration of wealth in hands of few elites and increased inequality resulting into persistent problem of chronic poverty and food insecurity. Besides, recurrent floods, landslides, drought and other nature induced catastrophes and associated crop losses also contribute to some extent to the food insecurity and hunger problems of Nepal. However, most of such incidences induce short-term crisis.

## **Tackling Food Insecurity**

From the foregone discussion, it is obvious that food insecurity is the prominent development challenge of Nepal. The Government of Nepal and the external development partners seem to be aware of the gravity of this issue and have launched several schemes to address the problem. The mainstream interventions of food security- carried out by both the state and non-state actors can broadly be divided into two categories Production promotional interventions- such as income generating activities Subsidized food provisioning The food insecurity problem of Nepal largely bears



structural features, but the dominant mode of interventions is technical in nature. The Ministry of Agriculture and Cooperatives is considered to be responsible for ensuring food security of people, which is however mandated for food production only. Other actors particularly I/NGOs and donor agencies like WFP also have food security interventions. However nearly all interventions are exclusively production focused. As discussed earlier, food production is necessary condition but not sufficient for food security. Moreover the centrally designed production focused interventions are obviously less relevant or useless for resource poor people, particularly landless or marginal cultivators who live in complex, diverse and risk prone niches adopting multiple livelihoods portfolios.

The provision of subsidized food for the hungry masses should be a temporary measure to tackle food crisis arising out of sudden shocks such as flood emergencies that affect the households temporarily and must be ended as soon as the crisis is over. However, in our case, food aid has become a standard and institutionalized response to chronic food insecurity problems with increasing flow of subsidized foods.

Nepal Food Corporation a semi-autonomous government institution and World Food Program of the United Nations have been involved in providing subsidized food particularly rice targeting to food insecure households of the hills and mountain regions of Nepal for more than four decades. The implications of such a provisioning are multidimensional as it creates dependency among recipient communities and sidelines the priority of state authorities to create sustainable foundation of food security. By discouraging policies and programs that would contribute to build a foundation of sustainable livelihoods of people in highly vulnerable areas, food aid in no way has benefitted communities in the longer term. Neither has it become a reliable means of food safety for the rural poor. The recurrent and increasing flow of food from outside has not supported the vulnerable people's desire of secured livelihoods rather it has continuously been undermining them. It is largely not contributory to food security rather deepening the problem by sidetracking the attention of policy makers, donor agencies as well as development workers from pertinent issues of structural transformation.

## **Conclusion:**

Food insecurity is a perennial problem of poor and excluded communities and households passing through one generation to other. Denied access to productive resources and thus the food due to socio-cultural and economic exclusion is basic cause of persistent problem of food insecurity. The mainstream intervention schemes ignore this fundamental reality and search for a 'quick fix' either through provisioning of subsidized food or introducing production-focused technology packages which are less relevant and ineffective for the poor and excluded. Robust schemes of promoting structural transformation to ensure access to productive resources and opportunities for the poor and excluded only could bring lasting solutions of this perennial problem.

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## A critical assessment of Third Global Review of Aid for Trade

–Paras Kharel

### Introduction

The Aid for Trade (AfT) initiative was launched under the aegis of the World Trade Organization (WTO) in 2005 in response to the inability of developing countries in general and least-developed countries (LDCs) in particular to take advantage of increased market access opportunities on account of their supply-side constraints and the ineffectiveness of previous trade-related technical assistance and capacity building programmes at the multilateral level in helping address the core trade-related supply-side constraints facing these countries.

Six years into the implementation of the AfT initiative, a robust and comprehensive monitoring and evaluation mechanism is yet to be in place. Three major multilateral (official) platforms/ mechanisms are being used for the monitoring and evaluation of AfT. First, the Organisation for Economic Co-operation and Development (OECD) and the WTO jointly publish an annual report titled *Aid for Trade at a Glance*, which analyses AfT flows based on the OECD's Creditor Reporting System (CRS) database and broad qualitative trends in AfT based on questionnaires filled out by recipient countries, and unveil the report for wider discussions at periodic intervals. Second, on a pilot basis, both donors and partners are including a section on AfT in their respective trade policy review documents. Third, periodic discussions on AfT issues take place at the regular sessions on Aid for Trade within the Trade and Development Committee of the WTO. Following criticism of the largely

top-down Geneva- and Paris-based monitoring and evaluation exercise and growing calls for country-based assessments, the OECD and the WTO have included 269 "case stories" in the *Aid for Trade at a Glance* report for 2011, unveiled at the Third Global Review of AfT in Geneva in July 2011.

Realizing the shortcomings of the present monitoring and evaluation systems, South Asia Watch on Trade, Economics and Environment (SAWTEE), Kathmandu and the International Centre for Trade and Sustainable Development (ICTSD), Geneva prepared a methodology<sup>1</sup> for assessing the effectiveness of AfT, based on which country case studies are being conducted in six developing countries: Cambodia and Nepal in Asia, Malawi and Mauritius in Africa, and Jamaica and Peru in the Americas.

The aspects of AfT considered in the Nepal study<sup>2</sup> are largely based on the recommendations made by the Task Force on AfT constituted by the WTO Director General as mandated by the Hong Kong WTO Ministerial Declaration in 2005. The aspects can be grouped under four pillars. Additionality, predictability and sustainability constitute the fundamental issues. Under the effectiveness pillar, ownership, alignment, donor coordination and impact are considered. The third pillar is coherence, where South-South AfT and the coherence of AfT and climate funding are considered. Under the fourth pillar, three additional aspects are considered: grant versus loan, demand-supply gap, and absorptive capacity.

Besides the OECD's CRS database, the Nepal study used national-level data where available and conducted in-depth interviews with a wide range of relevant stakeholders (50), including government officials, academics and trade experts, civil society, the private sector, the media, and donors.

This article critically assesses the evaluation approach adopted by the *Aid for Trade at a Glance 2011: Showing Results*<sup>3</sup> (henceforth the Report) mainly in the light of the findings of the Nepal study conducted by SAWTEE and the methodology that underpins it. While all the findings of a country study cannot be generalized, the methodology employed and the issues/aspects covered in the study, but ignored or not adequately dealt with in the Report, provide for a more comprehensive evaluation that can be adopted in other countries too. The focus of this article<sup>4</sup> is on the fundamental issues (additionality, predictability and sustainability, plus definitional issue), ownership, alignment and impact.

1. Adhikari, Ratnakar. 2011. "A Methodological Framework for Conducting Independent Evaluation of the Effectiveness of Aid for Trade", ICTSD Programme on Competitiveness and Sustainable Development (ICTSD), Issue Paper No. 18. Geneva: International Centre for Trade and Sustainable Development.
2. Adhikari, Ratnakar, Paras Kharel and Chandan Sapkota. 2011. "Evaluating Development Effectiveness of Aid for Trade in Nepal". July. Report prepared for the International Centre for Trade and Sustainable Development (ICTSD) and South Asia Watch on Trade, Economics and Environment (SAWTEE).
3. OECD and WTO. 2011. *Aid for Trade at a Glance: Showing Results*. Paris and Geneva: Organisation for Economic Co-operation and Development and World Trade Organization.
4. This is an extended version of Kharel, Paras. 2011. "Critical assessment of Third Global Review of Aid for Trade", *Trade Insight* 7(2). Kathmandu: South Asia Watch on Trade, Economics and Environment.

## Fundamental issues

Based on the CRS database, the Report shows that in 2009 AfT commitments reached approximately US\$40 billion (in 2009 constant prices), a 60 percent increase from the 2002-2005 baseline period. Likewise, disbursements have been increasing at a constant growth rate of between 11-12 percent for each year since 2006, reaching US\$29 billion in 2009.

The Report concludes that the increase in AfT commitments in the post-2005 period has been additional, i.e., not at the expense of aid to other sectors, on the ground that the average share of AfT in total sector allocable official development assistance (ODA) since the 2002-2005 baseline period has remained stable at 33 percent. There are a number of problems with this approach. The Report assesses additionality in commitments but not in disbursements, and does not assess additionality at the country level. The Nepal study finds additionality in commitments but not in disbursements. Moreover, the basis for determining additionality used in the Report may not yield meaningful results in all cases. For example, even if the share of AfT in total sector allocable ODA had increased, there could still be additionality, provided that the growth of non-AfT ODA had not declined compared to the baseline period. The Nepal study assesses additionality in both commitments and disbursements by taking into account whether i) AfT has increased over the base period; ii) non-AfT ODA has also increased over the base period; and iii) the growth rate of non-AfT ODA has not declined over the base period.

The distribution of AfT flows across recipient countries is highly unequal, slightly more so than the distribution of overall ODA. According to the Report, although low-income countries got almost 50 percent AfT commitments in 2009, up from 39.5 percent in 2008 and the LDCs' share rose from 26.5 percent to 30.4 percent, the top 10 recipients got 45 percent of country-specific AfT commitments during 2002-2009. The presence of countries like Iraq (ranked second), Afghanistan (fourth) and Egypt (tenth) in the top 10 list—attracting AfT in volumes disproportionate to their economic and population size, and, more importantly, the trade-related constraints they face—strongly points to strategic considerations reigning supreme in the allocation of AfT resources by donor countries.

Another issue related to the volume of AfT flows is that while the Report compares AfT commitments made in the years 2006-2009 with the average commitments made in the baseline period 2002-2005—globally as well as for individual countries—it does not do the same for disbursements. That it is important to look at changes in average disbursements is demonstrated by the finding of the Nepal study that disbursements to Nepal have actually *fallen* in the period 2006-2009 compared to the baseline period.

Most of the analyses in the Report are based on commitments rather than disbursements. The ratio of disbursements to commitments at the global level was 72.5 percent in 2009. The Report argues that commitments are forward looking and show the amounts that donors will spend on certain development activities and are often multiyear (e.g., infrastructure) with

subsequent disbursements spread over several years, with the result that disbursements always trail commitments. These arguments are valid, but other factors that may explain the divergence between disbursements and commitments—such as the absorptive capacity of recipients and donors' onerous procedural requirements—are not analysed. The Nepal study finds the gap between AfT disbursements and commitments (taken as the ratio of *average* disbursements to *average* commitments) to have worsened sharply in the period 2006-2009 compared to the baseline period (from 98 percent to 59 percent). In contrast, the gap is not so severe in the case of non-AfT ODA. Apart from technical reasons (e.g., mismatch between the reporting periods of donors and the recipient), which are only a part of the problem, the study finds human resource-related constraints at the domestic level as well as systemic factors both at the domestic level (e.g., lack of project banks, political instability) and the donor level (e.g., donor bureaucracy and its onerous procedural requirements) as critical factors behind the variation between commitments and disbursements. The Report does not discuss the predictability issue in the light of the commitment-disbursement gap, although it identifies inadequacy and unreliability of external funding as "a recurring brake on project success" when presenting case-story findings.

In what is one of its major limitations, the report does not assess the sustainability aspect of AfT despite it having been emphasized in the WTO's AfT Task Force Report. Sustainability, here, means sustaining the achievements made through AfT even after donor support ceases. The Nepal study assesses sustainability in terms of financial, institutional and human resource sustainability. Financial sustainability calls for mobilization of funds for the continuity of AfT programmes/projects even after donor funding dries up. However, financial sustainability alone is not enough to ensure effective sustainability. An institutional home for the AfT programmes/projects to carry on is of utmost importance. The human resource aspect of sustainability basically refers to efficient human resource planning to ensure effective designing and implementation of AfT programmes/projects: frequent transfer of staff and weak implementation of a performance-based reward system in the bureaucracy are found to be adversely affecting sustainability in Nepal. The Nepal study finds that AfT donors are in general not building the capacity/expertise of local institutions and individuals such that AfT projects could continue even when donor support cease to exist. The tied nature of aid is found to have adverse implications for sustainability. When equipment have to be sourced from a particular donor, the replacement of parts and components could become extremely difficult after the foreign assistance is terminated, as was the case in a project in west Nepal.

## **Definitional issue**

The broadness of definition of AfT on the basis of which AfT is monitored and evaluated by the WTO has been a major criticism of the AfT initiative. The WTO's Task Force on AfT divided AfT into six categories: i) trade-

related infrastructure (e.g., road, telecommunication, electricity); ii) building productive capacity (e.g., enhancing productivity of agriculture, industry, fishery); iii) trade development (e.g., investment promotion, trade promotion, business services); iv) trade-related adjustment (e.g., retraining of workers, compensation for retrenched workers); v) trade policy and regulations (e.g., training of officials and stakeholders, help in designing policies and compliance with trade rules); and vi) other areas (e.g., other needs of the recipient countries that are not included elsewhere).

The OECD's CRS database on AfT flows basically follows the Task Force's definition, but clubs building productive capacity and trade development together, and places trade-related adjustment under the category of trade policy and regulations. This database has remained the principal source of data on AfT provided by members of the Development Assistance Committee.

The first two categories—infrastructure and building productive capacity—are so broad that a lot of aid activities remotely related to trade can be included in them. This problem takes on additional significance when one notes that the main objective of the AfT initiative is to address trade-related supply-side constraints and that these categories represent the most important areas for addressing such constraints. Since the launch of the AfT initiative, aid to economic infrastructure and building productivity capacity has dominated AfT flows (about 97 percent of total AfT commitments during 2006-2009). Taking it at face value would mean that AfT is mostly going towards addressing trade-related supply-side constraints. But the broadness of definition coupled with the fact that the database relies on self-reporting by donors evokes skepticism. The inclusion of aid for the construction of an urban transport system in Istanbul and a mass transit system in Bangkok is an example of how the broadness of definition distorts the AfT picture.

The broadness of definition emerged as a major issue in the interviews with stakeholders carried out for the Nepal study. Serious doubts were expressed over the entire US\$986 million (in 2008 constant prices) Nepal received in AfT commitments during 2006-2009 being really AfT *proper*, with some going so far as to dub AfT "old wine in a new bottle". According to a government official handling trade matters, aid for the construction of a road with little or no significance for Nepal's international trade was counted as AfT by donors.

The Report does admit that definition remains an issue and that the OECD's AfT categories are at best proxies to keep track of aid flows geared towards "supporting" trade. It quotes Nepal's dissatisfaction with the broadness of definition. It also cites the case of India, which, despite being the largest recipient of AfT commitments since 2002, takes the position that except for a single project it has received no AfT! The Report attributes this to India's narrow definition of AfT. Possible ways to address this problem are not explored, however. Because the definitional issue is fundamental to any reliable assessment of AfT, the WTO and the OECD should seriously engage in sorting it out, although determining the precise "trade" component of aid

is impossible, as pointed out in the Report.

The broadness of definition would not have been such a critical issue if there were a robust mechanism at the local level through which both donors and recipients could monitor AfT flows. One way to partly address the issue could be the channelizing of AfT through a single dedicated AfT fund in which donors pool their AfT resources. While Cambodia has already successfully adopted a sector-wide approach to mobilizing AfT, Nepal's Ministry of Commerce and Supplies is taking steps for the creation of a Trade Trust Fund. Channelizing AfT through a dedicated fund will not only help in making the definitional issue less crucial (as the recipient country will have to agree that any particular aid project/programme is indeed AfT) but, even more importantly, also contribute to sustainability, ownership, alignment, transparency and, hence, overall effectiveness.

Despite evidence of pooled funding showing relatively positive results in the social sector (e.g., in Nepal) as well as in the trade sector (e.g., in Cambodia), the Report is dismissive of the idea of a dedicated AfT fund. It argues that "if AfT were implemented through earmarked funds rather than as part of broader development programmes, it would risk *undermining the principles of ownership and alignment*. This is particularly important considering that donors provide over a quarter of their ODA to aid for trade" (emphasis added).

## Ownership

Trade mainstreaming is regarded as a precondition for national ownership. It means the integration of trade into national development and poverty reduction strategies, including through the integration of trade into sectoral policies, strategies and actions. It entails coordination, formulation and implementation of trade-supporting plans and policies by all concerned ministries.

The 2011 Report finds that almost 60 percent of the partner countries that changed their trade-related objectives and priorities since 2008 mainstreamed these changes in their development strategies. In 2008, more than half the partner countries had fully mainstreamed trade and another almost 40 percent had partially mainstreamed trade. However, the 2009 Report used a narrow definition of mainstreaming and the 2011 Report continues with it. In the 2009 Report, those who ticked the box "Trade is a key priority and the plan includes well developed trade-related priorities and implementation actions" were considered to have "fully" mainstreamed trade in their national development plans. The AfT Global Review, therefore, does not consider the quality or substance of mainstreaming—for example, whether trade has been incorporated into sectoral policies like agricultural policy, industrial policy and forestry policy.

The Nepal study makes a distinction between mainstreaming in the formal sense (as adopted by the Global Review) and mainstreaming at the substantive level. It finds that while trade has been mainstreamed in the national development plan—trade is one of the six strategies of the current

three-year plan—mainstreaming at the sectoral level is yet to take place. For example, the Inter-Ministerial Technical Committees, chaired by the secretary of the relevant ministries and created as part of the National Implementation Arrangements of the Enhanced Integrated Framework, are yet to be fully activated. Likewise, the roles and responsibilities of the sectoral ministries for trade policy/strategy implementation are yet to be clearly defined.

In a departure from the norm of looking at mainstreaming only at the partner country level, the Nepal study also assesses whether donors have mainstreamed trade in their country strategies. The report only considers the global-level strategies of donors. The Nepal study finds that most donors are yet to mainstream trade in the planning and implementation of their aid strategy in Nepal. "Peace-building" activities have become donor darlings. According to government officials, there is inadequate sensitization and awareness about AfT among donors at the country level. Staff at the World Bank's Nepal country office, while being interviewed for the study, expressed ignorance about the AfT initiative. All this suggests that mainstreaming by donors at the global level may not be mirrored at local-level donor strategies.

## **Alignment**

Two major components of alignment are donor alignment with country strategies (including policies and priorities) and donor alignment with country systems (including public financial management and procurement systems). The Report finds that alignment is improving albeit unevenly, but its assessment of alignment is almost exclusively centred on the first aspect of alignment. Question No. 15 in the questionnaire for partner countries, which is supposed to deal with the issue of alignment in its entirety, only asks whether donors are better aligning their support around partner country's trade-related priorities.

The issue of strengthening partner country systems and aligning aid with them is hardly discussed in the Report. The tendency of some donors to bypass the national systems and deliver aid through parallel implementation units emerged as a serious issue in the Nepal study, as did the excessively "bureaucratic" national Procurement Act. An assessment of this aspect of alignment in Report would have been illuminating.

## **Impact**

The Report finds that AfT's main achievements so far relate to raising awareness about trade's role in development and to improving the delivery of AfT. This finding is based on the responses of partner countries. Partner countries report having achieved less in terms of improved economic and trade performance, with positive answers for "increased trade" and "increased exports" below 50 percent.

The Report points to the measurement problem in assessing trade-related outcomes—importantly, the problem of attribution—as a possible



reason why positive economic and trade results may be underreported. It also cites a time-lag effect to explain the gap between partner countries' objectives (improved economic and trade performance) and the results achieved. It does not, however, investigate the role of the broadness of AfT definition in the difficulty in establishing strong links between AfT and positive trade and economic performance.

The purpose of collecting "case stories" for the 2011 Report was "to probe more deeply into the objectives, challenges, and processes of trade-related assistance so as to better understand the results of such assistance". A "great majority" of the programmes and projects in the case stories reported "at least some elements of success". The Report candidly admits that the case stories are not a scientific approach to evaluation: the sample reflects selection bias (mostly written by governments, donors or consultants working in the project), and generalizations should be "taken with a grain of salt" (because of omitted variables and attribution problems). Further, most case stories suffer from a dearth of quantitative information.

Based on the case stories, the Report identifies some essential conditions for successful AfT: ownership at the highest political level built upon the active engagement of all stakeholders; adequate and reliable funding; leveraging partnerships (including with providers of South–South cooperation); and combining public and private investment with technical assistance. It also notes that complementary policies—especially stable fiscal and monetary policies—and flexible labour market policies, together with good governance, can greatly enhance the chances of success.

## **Conclusion**

The inclusion of case stories for the Third Global Review of AfT marks a welcome and refreshing departure, even if on a small scale, from the hitherto completely top-down approach to AfT monitoring and evaluation. However, given the limitations of such stories, the OECD and the WTO must now go for independent monitoring and evaluation at the local level so that the "positive and vibrant picture of aid for trade in action" that they paint stands up to scrutiny on the ground.

# 16

## Aid for land reform or land grabbing?

-Jagat Basnet

Today, in Nepal, foreign aid and development projects are synonymous, so are the elites and development. One cannot exist and function without the other (Shrestha, 1998 p. 71). This sentence gives a quick sketch of why and how aid is channeled into Nepal and how it has been feeding on the interest of elite and rulers. The fact of the matter is that the aid doesn't come without a sting in the tail - the agenda and interest of donors. Perhaps, that is how it is made to work! For example, one of the first aid providers to Nepal, the United States, was interested in agriculture and rural development. At the center of the US interest was the apprehension that this messy sector, plagued with unequal distribution of landholdings, was vulnerable to communist influence (Mihaly, 2003).

Another aid provider is India. The southern neighbour has been providing grant to Nepal on security-related issue. The root of it is the apprehension of china's influence in Nepal. India's aid to Nepal was shaped largely by its security concern *vis-à-vis* China, but it was also motivated by the need to counterbalance the growing influence of the US in what it regarded as its own backyard (ibid). These two references are mirrors of how and why aid flows into Nepal. Nepal had, in fact, brought into being the Development Board Act in 1956, in order to allow the government to accept loans for its development needs. This facilitated the passage for multilateral lending agencies although it was only from the early 1970s onwards that these organizations began their activities in a significant manner in the country (Shrestha, 1998).

This paper broadly deals with aid for land reform in Nepal.

The aid for land reform, as is evident from sources, channeled indirectly with agendas and interest of donors and mostly the International Financial Institutions (IFIs). Tracking down the history of aid for land reform in Nepal, it is Ford Foundation, an American organization, showed interest in land reform and subsequently sent consultants to study the process for support to Nepal after the land reform of Japan, Taiwan and South Korea. The consultant met with King Mahendra and gave memorandum to him requesting land reform in Nepal. Nepali elite (ruling class) didn't accord priority to land reform and the donors' priority was dovetailed with that of ruling elites in a way that went on to save the power and property of ruling class. The upper social classes reaped benefits from foreign aided development. As a result, foreign aid strengthened the position of the upper social classes, who benefited from the existing political and economic order. The need to legitimize such a power gave foreign aided development the halo of a 'people-oriented development' while at the same time increasing the dependence of the lower classes (Sharma 2008). In this way, the aid channeled to Nepal was to save the property and power of elite and ruling class and bolster up power nexus between donor and ruling class of Nepal. A good example is donors' interest in agriculture, irrigation and road which directly benefits the landlords, though they were ostensibly meant for poverty alleviation of the poor people.

In the context of Nepal, those who till the land do not have land certificate and those who do not till the land have the land certificate. That will mean whatever money goes on land, the landlords reap the benefit. The support to irrigation and road directly give benefits to the landlord as it gives them an opportunity to raise the price and rent of land. The facts notwithstanding, bi-lateral and IFIs have been consistently supporting Nepal's irrigation, agriculture and road extension in the name of poverty alleviation and poor people. As far as the rights of poor people over land are concerned, they save their skin on the issue of land reform calling it political and contentious. They are not interested to support the land reform agenda. Intriguingly, the aid disbursement is made by the IFIs like World Bank, Asian Development Bank meant for land reform, especially to promote the market assisted land reform called willing buyer and willing seller.

In 2004, Government of Nepal was asked to introduce the 'land bank' concept by the World Bank. The whole concept was that World Bank (WB) provides the loan to the Government of Nepal to establish the land bank. In line with the World Bank strategy, the concept of land bank, the Government of Nepal developed, was willing buyer and willing seller that, in turn, meant resource (money) to landlord and loan to landless farmers which is a failure model in the world. Civil Society Organizations stood up to the concept, especially CSRC and its collaborating organizations. A mission of World Bank visited Nepal in the wake of opposition to the concept from the Civil Society Organizations. They promised that they would mutually work together with the Civil Society Organizations. The Civil Society stuck to its gun arguing that they were in favour of comprehensive land reform and that the concept

floated by WB didn't fit for Nepal. For decades, the WB has been promoting market-based approaches to land management through its lending practices and policy advocacy. This apparently means privatization of land rights, both through the conversion of customary rights into marketable titles as well as disengagement of the state, and legal reforms necessary for western style land markets to function (Grain 2010).

Another case in point is aids provided by Asian Development Bank (ADB). In June 2007 Asian Development Bank sent a mission to Nepal to study the land governance and land reform of Nepal. The team developed the proposal on 'Nepal: Strengthening Land Administration Services' Project Number: 40544 September 2007<sup>1</sup> (first report and proposal, it was revised after scathing comment from the CSRC)<sup>2</sup>, as a piloting project in Nepal. Although the amount involved was small in size, the proposal ignored the expertise of Nepalese and the main agenda of land reform. The first proposal was developed costing US \$ 350,000, the Government of Nepal's share was US\$ 50,000. The proposal was designed to suit the pockets of international consultants. Of US\$ 300,000, some \$262,000 was set side for fees, salary, transportation and per diem of international consultants (see table below). The objection raised against draining of resources channeled in the name of poor was brushed aside as baseless. When like-minded international organizations, individuals and network, stood up to it, the Country Director of ADB Nepal Office consulted Civil Society Organizations on Land Rights over the issue. Nepalese Civil Society expressed their reservation about the issue of land right arguing that it was not a mathematical thing, and that the computerization of Kathmandu based Land Offices wouldn't help reduce poverty. It was a political issue and there was a clear provision in the interim constitution of it, and an agreement in Comprehensive Peace Accord favouring scientific land reform and there had been the commitment from the political leaders on this.

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1. ADB: Technical Assistance Report, Project Number: 40544 September 2007, Nepal: Strengthening Land Administration Service
2. Community Self-reliance Centre (CSRC) working in land and agrarian rights issue

## ADB's proposal to strengthen the land administration in Nepal

	Total
Item	Cost
<b>A. Asian Development Bank Financing<sup>a</sup></b>	
1. Consultants	
a. Remuneration and Per Diem	
i. International Consultants	220.00
ii. National Consultants	10.00
b. International and Local Travel	31.00
c. Reports and Communications	5.00
2. Equipment: Computers	5.00
3. Pilot testing	
Data entry	7.00
b. Software	6.00
c. Computers	5.00
4. Miscellaneous Administration and Support Costs	6.00
5. Contingencies	5.00
Subtotal (A)	300.00
<b>B. Government of Nepal Financing</b>	
1. Office Accommodation and Transport	30.00
2. Staff and Office Support	17.00
3. Translation Services	3.00
Subtotal (B)	50.00
<b>Total</b>	<b>350.00</b>

The other issue was about maintaining balance of Nepali and international consultant to do the work. The cost earmarked for local consultant was injustice, hence unacceptable for the Nepalese. The ADB Director agreed to revise the proposal, and subsequently, added US\$ 50,000, increasing the budget from US\$ 350, 000 to US\$ 400,000. The only change made was in remuneration and per diem of Nepali consultants' budget that went up from US\$ 10,000 to 40,000, which still stopped short of doing justice to Nepalese consultants. The above proposal shows how aid is disbursed to Nepal and how they are spent and who are the real beneficiaries.

So far, in my study, there has been no direct support from bi-lateral organization for land reform, yet still several organizations have invested in the study of land reform in Nepal. Recently DFID hired one international and two national consultants to conduct a study and published the study report on 'Land Reform in Nepal, *where is it coming from and where is it going?*' in English language and Nepali as well.

WWF is extending support to Nepal government but its interest is to

protect wild life and their habitat and not the land reform of Nepal.

Danida, ActionAid, CARE, Lutheran World Federation, Oxfam have been supporting the CSOs for the advocacy on land reform and peace process.

The table below shows that there has been no direct foreign aid for land reform in between 2001 and 2005 in Nepal.

**Table 9.1: Actual Aid Disbursements in the Subsectors of Economic Services (in Million Rs)**

<b>Economic Services</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>	<b>2002</b>	<b>2001</b>
Agriculture & Cooperatives	686.5	546.2	1,014.3	1,194.7	1,380.7
Civil Aviation		0	80.1	362.2	655.2
Commerce	34.3	17.2	59.0	122.1	232.4
Forestry & Soil Conservation	889.3	223.5	162.2	93.9	84.4
Hydropower & Alternative Energy	4,234.70	648.4	1,584.5	3,330.8	4,928.5
Industry	77.6	68.7	105.1	119.6	99.6
Information & Communications	494.5	272.8	57.1	332.0	0
Irrigation	174.3	784.4	1,478.4	2,106.3	2,398.7
Labor	139.9	192.0	146.1	84.7	51.9
<b>Land Reform &amp; Survey</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
Natural Resources Management	130.1	91.5	109.7	84.1	84.3
Roads & Transportation	1,385.30	1,356.3	1,721.5	2,644.7	1,876.4
Science & Technology		0	0.3	2.0	0
Tourism		44.3	129.9	195.0	236.8
Other Economic Programs	3,079.20	6,105.4	3,201.0	1,331.9	1,718.8
<b>Total</b>	<b>11325.6</b>	<b>10350.7</b>	<b>9,849.2</b>	<b>12,004.0</b>	<b>13,747.7</b>

*Source: Adapted from the Development Cooperation Report 2005, Ministry of Finance, GON*

## **Aid for land grabbing in Nepal**

The debate in Nepal revolves around whether foreign aid was meant for land reform or land grabbing! The civil society and the tillers of land are demanding aid for genuine land reform, increase productivity and food security while the IFIs are providing aid to grab the land in different countries, promoting market-led, willing buyer and willing seller model of World Bank. Although Nepal has no multinational companies doing business but national elites have been grabbing the rural land in the name of land plotting and commercialization of farming. The commercial banks have been financing real estate and commercialization of farming.

Land has been a major commodity of business, a profit making venture in Nepal. As of May 2010, the commercial banks have invested 445 billion

Nepali Rupees in land transactions (The Himalayan Times, 10 May 2010). This has resulted in the surge of interest rates from 8% to 16%. It is estimated that urban cooperatives have made about 93% of their investments in land and real state. Moreover, more than 80% of remittances have been invested in land and household consumptions (Nagarik Daily, 14 April 2009). Likewise, financial companies have also found land transactions as a major area of investment (Kantipur Daily, 16 June 2011). The instable political situation in Nepal has heightened risk in business investments blamed at insecurity, power shortages, extortions and donations, which have increasingly made investments in land less risky, more than 50 industrialists in the eastern region of Nepal have siphoned off their investments from business to land (Annapurna Post, 17 May 2011). The trend of land grabbing has not only been an increasing phenomenon in the capital city, but it is on the rise in the rural areas too. Recent media reports show a trend of price rise of land, incredibly high in the headquarters of the remote district like Argakhachi. For example, the price for 1 square metre of land is approximately 1.5 million in Chutrabesi, Argakhachi (Kantipur 3 March 2011).

### **The aid for land grab at International level**

A report by Oxfam, published September 2011, identified 227m hectares (561m acres) of land – an area the size of north-west Europe – as having been sold, leased or licensed, largely in Africa and mostly to international investors in thousands of secretive deals since 2001. In another case, 56m hectares identified by the World Bank earlier this year, again predominantly in Africa (Retrieved from <http://www.guardian.co.uk/global-development/2011/oct/06/un-land-deals-governance-talks?intcmp=122>, UN expert calls for guidelines to protect vulnerable people against 'land grabs', on 7th October 2011).

Foreign land acquisitions worldwide now cover 218 million hectares (almost 10 times higher the World Bank's 2008 estimates), with 67 million hectares as more or less "verified". Some 71% of these are in Africa, 19% in Asia<sup>3</sup>. Independent panels of MDBs (Multilateral Development Banks) since 1995 have established independent panels to receive complaints by citizens (non-state actors) affected by the impact of development projects funded by them. Perhaps the most recent one was the World Bank's Land Titling Project in Cambodia, where 20,000 families near Phnom Penh were displaced when denied titling to the land and later evicted by government that sold the land to a private developer. But the question about these panels remain paramount: many are not truly "independent" from Bank staff or management; they only involve Bank projects with regards to their compliance with internal policies (eg "involuntary resettlement"); to them, Bank policies are "givens", these Panels are not mandated to engage in discussions about Bank policies themselves (Ibid- Tony Quizon). The burgeoning evidence for the last several

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3. Tony Quizon, presented paper Land Asia Forum 2011, organized by ILC, CSRC and ANGOC from 20-21 October 2011, Kathmandu, Nepal

years (approximately last couple of decades) shows a remarkable increase in the transnational hunt for land by economically powerful international and national players (e.g. multinational corporations (both agribusiness as well as others), national governments, equity funds, and banks, etc.) and relatively less powerful entities (e.g. association of farmers with active support from their domestic governments) for a variety of purposes including cultivation of biofuels and a range of cash crops<sup>4</sup>.

These cases serve as a reminder that how multinational companies have been grabbing the land with the support of IFIs and government. A further study on how the multinational aid and national elites are grabbing the land with the support of banks or government is absolutely imperative. The IFIs and bilateral organizations have been providing fund to big projects for land acquisition but the compensation is received by landlords not the tillers. In Nepal, the real tillers largely have no land certificate to claim the compensation.

Political changes notwithstanding, foreign aid continues to make up a very large share of the development budget. Despite the significant inflow of aid, the people at large feel that aid channeled through government line ministries has done little to poverty reduction, and that much of the aid money as been drained. Even the seemingly large aid for agriculture has not resulted in acceptable growth in agricultural production (Sharma 2008).

Agriculture land has been treated as a profitable commodity. In this context, the question is who is providing foreign aid and for whom? If it is for the cause of social justice and poverty alleviation as claimed, it leaves much to be desired. So far the aid has been able to fulfill the agendas and interest of elites and ruling class.

It makes one wonder if foreign aid is meant for eradicating poverty or eradicating the poor!

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4. Praveen Jha, presented the slide in Land Asia Forum 2011 organised by ILC, CSRC and ANGOC in Kathmandu, Nepal from 20-21st October 2011



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**Dr. Meena Acharya** is a renowned economist and feminist scholar. She is presently General Secretary of Tanka Prasad Acharya Memorial Foundation.

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