CHAPTER I
NEPALESE ECONOMY AND GLOBALIZATION

1.1 GENERAL

The present study is carried on the basis of the terms of reference provided by the International Labour Office (ILO), Geneva to the study team of the Nepal Society for Applied Economics. The list of the team members is presented in annex. The study was initiated in March 2003 and completed by January 2004.

1.1.1 Methodology Adopted for the Study

As per the format requirements and the methodology developed by the ILO expert team of the study, the country team adopted the process of conducting the study. The study was carried at two phases. In the first phase, a statistical report was prepared based on the format provided by ILO expert team and the report was reviewed by the expert team and the analytical and monographic reports were prepared and the draft reports were submitted in September 2003 to the ILO team. The ILO team has reviewed in details both reports and provided the comments in December 2003. The country team prepared the second draft report incorporating comments and suggestions provided by ILO expert team. The second draft prepared by the team was given for review to the reputed national experts to get their inputs for further improvements. A national dissemination workshop with the participation of policy makers, academia and representatives of private sector and non-governmental organizations was organized on March 18, 2004. Two national experts were requested to review the general report mainly from the perspective of: a) Openness and Employment and b) Openness, Income Distribution and Poverty. Third national expert on Agriculture was requested to review the monograph on Globalization and its Implication on Agricultural Development in Nepal. The suggestions of the national external experts and the ideas provided by the participants in the national dissemination workshop were also thoroughly analyzed and included in the chapters where they are found relevant. The message given by Prof. Macro Viverelli to the dissemination workshop also provided inputs for discussion and for the improvement of the reports. The list of the participants with program is presented in Annex II. As a result of these processes, the country team prepared the following two reports to accomplish the work:

a. General Country Report
b. Globalization and Its Implication on Agricultural Development in Nepal

1.1.2 The Research Design

The research design was pre-designed by the ILO Expert Team and it was tested in the Nepalese context. The assessment of the consequences of globalization can be done if adequate quantities of the required data are available. But in a developing country like Nepal, there is always paucity of specific data because only few primary data are collected regularly. The information and data collected regularly through survey and sample studies carried at different periods are used to conduct the study. The information collected from some micro studies is also used to substantiate the facts. In addition, some qualitative analysis has also been made to substantiate the
consequences of globalization on different aspects of Nepalese life. In order to translate the design into reality, the following activities were carried:

On March 6 and 7, 2003 an interactive workshop was organized in Kathmandu where the team members of the study and the members of the ILO expert team Prof. Marco Vivarelli and Mr. Jean Baptiste Gros participated. The workshop helped the study team to understand the TOR and methodology of the study and the ILO Team could assess the availability of data sources for accomplishing the study.

Prof. Vivarelli presented the theoretical foundation of the trend of the process of globalization and the approach adopted for the study. It helped in providing theoretical inputs and direction to the study team and the approach to be taken for the country study.

Five members of the country study team provided an overview on the status of data sources in Nepal, particularly with regard to macroeconomic situation, trade and FDI, employment, income distribution and poverty. Both of these presentations helped in developing an appropriate interface between the country study team and the ILO expert team. These two presentations clarified the issues and the way of approaching the issues.

In order to assess the consequences of globalization in a deeper way, a specific area relevant to the context of Nepal was identified for the monographic study. Agriculture was taken as the area for the deeper study for assessing the consequences of globalization in Nepal and the framework for monographic study was formulated.

1.1.3 Limitations of the Study

The process of liberalization was initiated in Nepal broadly in the mid 1980s when the Structural Adjustment Program (SAP) was initiated. This process was further accelerated with the restoration of multiparty system of governance in 1990. Therefore information covering the period from 1990/91 to 2000/01 is taken for analysis. In addition, the available data and information have been used to approach correctly to the issues of poverty. In some cases, where the quantitative information is not available, qualitative analysis has been made on ground of the observations and experiences of the members of the study team and in some cases, it is substantiated by the studies made by other institutions and individuals.

1.1.4 Organization of the Study

The main report of the study is organized in seven chapters, as given in the TOR of the study, consisting of: an overview of Globalization, Macroeconomic overview, Trade and FDI, Employment, Income Distribution and Poverty, Openness and Employment and Openness, Income Distribution and Poverty. It is having an Executive Summary and the general lessons learnt from the case of Nepal. The monographic study is presented in a separate report.

1.2 BACKGROUND

Nepal is a small, landlocked country with an area of 147,141 sq. km situated between two large countries, India and China. The nearest port is Calcutta, India, which is about 500 miles away from the nearest border point of Nepal. The population of Nepal is about 23.2 million and its economy highly depends on agriculture, which employs more than 78.1% of the total workforce.
and account for about 39% of GDP. The manufacturing sector is still small but growing rapidly. It contributes about 10% to the GDP.

Table 1.1: Comparative Status of Nepal with other South Asian and Low Income Countries

<table>
<thead>
<tr>
<th>Countries</th>
<th>Per Capita GDP US $</th>
<th>PPP Per Capita GDP US$</th>
<th>GDP Growth Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nepal</td>
<td>220</td>
<td>250</td>
<td>230</td>
</tr>
<tr>
<td>Bangladesh</td>
<td>380</td>
<td>370</td>
<td>360</td>
</tr>
<tr>
<td>India</td>
<td>460</td>
<td>460</td>
<td>480</td>
</tr>
<tr>
<td>Pakistan</td>
<td>470</td>
<td>420</td>
<td>410</td>
</tr>
<tr>
<td>Low Income Countries</td>
<td>420</td>
<td>430</td>
<td>430</td>
</tr>
</tbody>
</table>


Information given in Table 1.1 shows that Nepal is having very low per capita income as compared to the countries of South Asia. In 2002, her per capita income was US$ 230, while her neighboring country India was having US$ 480 and the group of low-income countries was also having per capita income of US$ 430. In the case of per capita purchasing power parity also, Nepal is at the lowest rung. In 2002, Nepal had per capita purchasing power parity income of PPP US$ 1350, whereas India was having PPP US$ 2570 and the PPP US$ for the group of low-income countries was US$ 2040. The GDP growth rate in the countries of South Asia was 3.1 to 3.9% in the year 1999-2000, while in the year 2001-2002 it varied from –0.6 to 4.4 %. The average growth rate in other countries of South Asia was 4.1%, while in Nepal it was - 0.6%. The Nepalese economy is at shambles due to the armed conflict in the country. So the investment climate is not favorable in the current situation of Nepal.

1.2.1 Structure of the Economy

Structure of the Nepalese economy is dualistic. Both the monetized modern economy and non-monetized traditional economy exist in the country. On one hand, there are urban areas where physical facilities like roads, electricity, health and educational institutions, means of modern communication and other infrastructure are available due to which the development of industry, trade, transportation etc. are taking place rapidly. The economy of this sector is therefore monetized and somewhat modern. On the other hand, there are vast rural areas where 85.8% of the total population of the country live. The development of infrastructure like road, communication, electricity etc. is negligible in these areas, where people are largely dependent on agriculture. The technology used is traditional and the investment is very low. Large number of the people of these areas are poor and illiterate. The economy of this rural sector is, therefore, less-monetized and traditional.

The influence of macro-economic instruments like money, foreign exchange, capital market, government finance etc. lies mostly upon the monetized modern economy, and less upon the less-monetized traditional economy of the rural areas. With the adoption of open policy for grain trade, the cheap import of rice from India, has pressurized the farmers to sell their products at lower price. In the same way the farmers have to pay high price for the imported fertilizer, which is no more subsidized by the government. In this way, the rural areas are affected. The rural areas,
where roads are constructed, are influenced with the supply of manufactured products from the urban areas. No attempt has been made in the area of investment for the improvement of the agriculture of hills and mountains. If something is done, it is not sufficient for the development of the rural areas. The macro economic policy measures could not bring substantial improvement in the socio-economic life of the people of such areas. The rural sector is still having more closed economy.

During the last one and half decade, the economic activities in Nepal are influenced by the changes in the international and regional situation and by the changes occurring in the domestic socio-political situation. The liberal economic ideas in the form of globalization have influenced the Nepalese policy makers to adopt the liberal economic policy.

1.2.2 Topography

On the basis of topography, Nepal can be divided into two major regions: Mountain-Hill region and Terai region. The Mountain-Hill region includes a complex of high Himalayas, Hills, valleys, basins and a network of speedily flowing streams and rivers. The area of land covered by this region is about 83% of the total land area of the country. The Terai region is a plain low land and includes some major rivers of the country. This region covers about 17% of the total area of the country. The land is fertile and partially irrigated. The topographical feature of the Mountain-Hill region makes it very difficult to develop basic infrastructure like road, electricity, irrigation, communication etc. as it requires huge amount of capital and modern technology. Therefore it is more difficult for a least developed country like Nepal to make an investment in infrastructure development in the difficult terrain. As a result, the status of infrastructure development in this region is in initial stage compared to the Terai region. This situation has led Mountain and Hill region to the poor economic condition as compared to the Terai region where development is taking place in modern way, though slowly, due to the development of basic infrastructure. The diversified mountainous terrain with its natural beauty has provided ample of potentialities for the development of tourism in Nepal, and it is an important source of earning for meeting her balance of payments.

1.2.3 Actors of Economic Activities

Government, private sector and community are the prime actors of economic activities in Nepal and they largely influence macro-economic policy of the country.

1. Government: The government sector in Nepal plays a dominant role in the Nepalese economy. Though it has been engaged mainly in the infrastructure development, it has also been engaged in production, distribution, and marketing activities through various public enterprises. During the Panchayat era (1961-1990), the economy was more or less government regulated. After the restoration of democracy in 1990, the elected government adopted liberal and open economic policies and began to disown public entities giving greater emphasis on privatization.

On sectoral basis, the government has been giving greater attention to the agriculture sector by making direct investment in agriculture extension programs like irrigation, financial and technical assistance to farmers. In regard to industrial sector, the government had taken protectionist policy during Panchayat era, but the democratic government, established after the people's movement adopted an open market economic policy giving more emphasis on the export promotion and industrial development.
2. **Private sector:** Private sector in Nepal is small and weak but it is in a developing stage. The private investors in Nepal can be grouped for simplicity as Domestic Investors (native investors), Guest Investors (Indian investors) and Overseas Investors (Investors from the third countries). The size of domestic investors in the country is smaller because large portion of the population is engaged in the traditional occupation like agriculture, civil service etc. and the investments made by them are concentrated mainly to those areas that can have quick return, such as, trade, means of transport, real estate, other services etc. rather than on industries, infrastructure development, and innovative practices in agriculture. As there is open border, no passport system exists between Nepal and India, nor there is any restriction provision for Indian citizens to work in Nepal. So many Indians are attracted to invest in Nepal. As a result, a large portion of private investment in Nepal comes from guest investors. These investors are mainly engaged in trade and a few in industries.

The history of foreign investment in Nepal is not a long one. It flourished with the establishment of some commercial banks and financial institution in joint venture with foreign partners in 1980s. After the restoration of democracy, the government has adopted an open and liberal economic policy and has given greater emphasis on foreign investment. But in reality, the country has not been able to attract effective foreign investment yet. So the portion of foreign investment in Nepal is very small.

3. **Community:** As a large number of population of Nepal are illiterate, the community sector in the country is also weak; but it is at developing stage. The political, administrative and financial powers are more concentrated in the hands of the central government. Though there are provisions for governing bodies at village, town and district level, they enjoy relatively little power. Therefore they are mostly dependent on the decision of the central government. After the restoration of democracy, many Non-Governmental Organizations (NGOs) and International NGOs (INGOs) have come into existence in the country working in various social and economic sectors like poverty alleviation, education, environment, health, human right etc. But their impact is at a limited scale.

1.3 **Review of Literature on the Performance of Nepalese Economy**

In this section, the review of the current Nepalese economic scenarios has been presented on the basis of the review made by various institutions. In Nepal, in addition to the annual economic survey made by the government, comprehensive periodic reviews on the performances of the Nepalese Economy are mostly made by Asian Development Bank, UNDP and the World Bank. Therefore the recent report of some important organizations and the studies done by prominent economists in Nepal are reviewed here to provide information on the performances of the Nepalese economy and its governance that influence very much on the globalization process.

1.3.1 **Institutional Studies**

1.3.1.1 **Asian Development Bank’s Studies**

Asian Development Bank (ADB) in its Country Report of 2001 has identified several structural factors hindering the development effort of Nepal like the difficult terrains of a mountainous, landlocked country, heavy dependence on subsistence agriculture, low level of physical infrastructure and human capital, low domestic resource mobilization, and continued dependence on foreign assistance, inadequate institutional capacity for development management and poor governance, along with political instability.
The report identifies some positive aspects like rising GDP growth, increasing saving rate with manageable inflation rate during the year 2001. But despite these positive signs, limited growth in private sector investment, growing security expenditures and weak governance are identified as key issues to be addressed to accelerate economic growth. The report also projects a stagnant private as well as public investment in the medium term. Uncertainty in the domestic and global markets is considered to be prevailing in the near future, and it will affect private investment. The increasing expenditure for security operations is going to affect public investment.

ADB reports continue to highlight the significance of financial reforms along with effective law and order situation to achieve the level of growth necessary to reduce poverty. The report emphasizes the need of improvement in the performance of the agriculture sector within the broad framework of the Agriculture Perspective Plan (APP). It also focuses on improved governance in the public sector to maximize development effectiveness.

1.3.1.2 UNDP’S Report on Nepal Human Development 2001

The Nepal Human development Report 2001 is the recent version of Human Development Report on Nepal. The progress achieved in the field of poverty reduction during 1990s is highlighted in the Nepal Human Development Report 2001. During this period, Nepal has embarked upon a program of reforms that has covered almost all sectors of socio-economic activities. Almost two fifth of the Nepalese population still lie below poverty line. The root causes of the disappointment in development are weak governance, and the absence of people’s participation in the decision making process. The Report examines the relationship between vast disparities in the ownership of productive assets with lack of broad policy and participation of people in allocating public resources. It explores the relationship of transparency and accountability in governance to such issues as misuse and waste of public resources.

It is clearly shown in the report that the people of Nepal are largely discriminated, their voices are not heard, the government do not protect their basic rights and their state institutions are neither transparent nor accountable. The people in the grass-root level have only limited opportunities to accelerate development and they have very little influence in the delivery of basic services.

The governmental programmes on land policies directed to poverty reduction have suffered mainly from weak implementation of the programmes. Ownership, equality, accountability and efficiency are the four dimensions on which the whole analysis is based. The study proposes that if human development and poverty reduction are to be realized, policies and programmes should focus on broad-based growth and should be monitored closely to ensure that action follows intention towards the goals of poverty reduction, good governance, decentralization, empowering people through social mobilization and human development. But the current armed conflict in the country is considered as a major obstacle to achieve the goals of poverty reduction, quality education, and good governance.

Nepal has been pursuing planned development for nearly half century. However, its human development status remains among the lowest in the world. Despite the progress made on this sector, human capital formation and human resource development remain inadequate and gender, caste/ethnicity, and geographic regions locate great disparities. The report shows that good governance, and effective and efficient management of resources in response to the needs of all
members of society are essential to achieve both the poverty reduction and human development. Indeed, good governance is the “missing link” in Nepal’s poverty reduction strategy.

The Human Development Report (of the world), 2003 has shown the fact that from the point of view of HDI, Nepal’s level is low (0.499) as compared to other South Asian Countries namely Bhutan (0.511), Bangladesh (0.502), India (0.590), Pakistan (0.499) in 2001. Nepal Human Development Report shows lower HDI in rural areas (0.466) as compared to urban areas (0.616) that indicate urban biased development. The GDI of the country is low (0.452) which follows the same pattern of HDI higher in urban areas (0.605) than in the rural areas (0.426) where gender inequality is significantly higher. The ratio of GDI to HDI provides a better picture of the deprivation of women in relation to men as compared to GDI alone. The analysis of HDI made in Nepal Human Development Report 2001 has shown the ratio of GDI to HDI in whole Nepal, including rural and urban areas as reported respectively 96.9, 95.7 and 98.2 in Table 1.2. Similarly women are far less empowered than men as reflected by the computation of Gender Empowerment Measures (GEM). Different indicators and ratios vary not only by rural urban residence but also by development regions, ecological zones and caste/ethnic groups.

Table 1.2: Some Selected Indicators of HDI

<table>
<thead>
<tr>
<th>Description</th>
<th>Nepal</th>
<th>Urban</th>
<th>Rural</th>
</tr>
</thead>
<tbody>
<tr>
<td>HDI (2000)</td>
<td>0.480</td>
<td>0.616</td>
<td>0.466</td>
</tr>
<tr>
<td>% Change in HDI (1996-2000)</td>
<td>15.6</td>
<td>8.6</td>
<td>16.1</td>
</tr>
<tr>
<td>GDI (2000)</td>
<td>0.452</td>
<td>0.605</td>
<td>0.426</td>
</tr>
<tr>
<td>GDI to HDI Ratio (2000)</td>
<td>96.9</td>
<td>95.7</td>
<td>98.2</td>
</tr>
<tr>
<td>GEM (2000)</td>
<td>0.385</td>
<td>0.443</td>
<td>0.333</td>
</tr>
</tbody>
</table>


Poverty is measured in different ways by different studies. Thus the population below the poverty line differs in each study carried out in different periods of time. The recent estimates of the government based on "one US dollar a day" definition show that 37.7% Nepalese people are below the poverty line, and poverty is far more rampant, deeper and more severe in rural areas. Poverty not only varies from the place of residence but also varies greatly with the different castes and ethnic groups. On the basis of HPI, Nepal ranks 70th out of 94 developing countries; and it also indicates that the situation of Nepal is worse as compared to all other South Asian Countries.

Human and income poverty persists largely because of the weak governance. Poverty reduction policies and programmes have often fallen short of their aims. Basic social services remain inaccessible to large segments of the poor, and the quality of these services is low. Public investments have yet to be more effective in addressing poor peoples’ needs.

Over the last 15 years, Nepal’s annual economic growth rate has averaged about 5%. Although this is not spectacular, especially in comparison to the growth of East Asian countries, it is not very low either. A close look into the components of economic growth reveals that Nepal’s overall growth has derived largely from the growth of the non-agricultural sector which now contributes about 60% of GDP. This has transformed the economy’s structure. However, the
structure of employment has not changed accordingly. About 78.1% of the Nepalese workforce still work in the agricultural sector. Consequently, the income distribution has become far more uneven, with severe impacts on those whose livelihood depends on the land, rivers and forests. The poverty is endemic in the rural areas, which raises the question of how pro-poor the country’s economic policies and growth have been.

Poverty in Nepal has persisted because of the low economic growth, inadequate social and economic infrastructure, relatively high population growth, low access to land, low access to non-agricultural income, and deep rooted cultural and historical practices that have segregated certain communities as untouchable and low-status people making them marginalized and disadvantaged and taking them inferior beings lacking good governance strength.

Ineffective delivery and access to public services keep the quality of life of average Nepali very low. Nepal ranks at low level even among the countries of South Asia, where the quality of life is one of the lowest one in the world. Service delivery system within the country is biased on more advantageous groups. Low-level investment combined with ineffective governance drastically undermines public services. The exclusion of citizens, especially women and disadvantaged groups from governance at the community level further compromises the basic services.

Ownership, equity, transparency, accountability and efficiency are the concepts of good governance, but these are complex issues. However, the state must ensure all these concepts met in the governance process. This requires developing appropriate policy, means and institutions. For Nepal, like many other developed and developing countries, the most functional means is decentralization, and the most appropriate institutions are local governments and civil societies.

Decentralization in Nepal has to be assessed in terms of the demand for rapid institutionalization of democratic good governance and people-centered development. The decentralization Act (separate for DDC, VDC and Municipality) promulgated in 1992 has suffered from various weaknesses. Since 1990, the Nepalese Government has generally supported decentralization. However, the performance in the specific areas of decentralization shows mixed results. Despite policy frameworks and legislative provisions for addressing access, equity and empowerment issues, weaker sections of the society have inadequate access to resources and decision-making process.

Local governments appear to have started to understand poverty reduction better and take more responsibility willingly. Local governments and civil society can complement each other in articulating local needs and ensuring public transparency and accountability that cannot achieve without community involvement and ownership. The governmental developmental plan has not been successful to establish specific linkages between decentralization and poverty reduction, nor to indicate how local governments could integrate their programmes with overall poverty reduction objectives. Gender equity needs to be integrated into all development activities of local governments, with regular follow up and monitoring.

The process of social mobilization in Nepal existed long before the concept was articulated. Before the beginning of the planned development in Nepal, the development history was founded on social participation. There were numerous success-stories, but such efforts were sporadic, limited to scope and inadequate for national development. The Compulsory Saving Scheme, State
Owned Cooperatives, Back to the Village National Campaigns and so on were the programmes lunched for social mobilization in the country. Despite active participation of the people, they all failed mainly because of the lack of ownership by the beneficiaries, inadequate focus on the deprived section of the population, domination by the state and the elite, ambitious expansion without adequate preparatory work at the grass-root level and lack of transparency and accountability. Nevertheless, in addition to contributing to social and economic progress in the country, these movements have laid the foundation for group based approaches.

Learning from the past since the half of 1970s, social mobilization efforts have been directed to pro-poor and made multidimensional. Small Farmers Development Program (SFDP), production Credit for Rural women (PCRW) and Grameen Bank are the major targeted social mobilization programmes. The SFDP targets small farmers where PCRW and Grameen Bank focus exclusively on the poor women to increase their access to resources.

Hundreds of NGOs and dozens of INGOs emerged particularly during early 1990s to mobilize the people for poverty reduction where such NGOs had together mobilized more households than the government sponsored poverty reduction programmes. The Village Development Program (VDP), Sustainable Community Development, Rural Energy Development, Rural Urban Partnership, Parks and People and social mobilization programmes are the programmes linked with decentralization. Coverage of the present programmes is significantly higher as compared to the past programmes because they have gone more to the community.

The government of Nepal has lunched some special programmes like Women Development and Bishweshwar with the Poor programme as an income generating programme in the rural areas to reach the poorest of the poor. But these programmes are still in their infancy. The overall social mobilization process shows positive impact on poverty reduction, good governance and human development. The percentage of people living at the very poor, poor and capable poor levels is decreasing both at community level and program level, whereas the position of the well-to-do level is increasing. (Table 1.3).

Table 1.3: Change in Poverty Status Over Time Through Social Mobilization

<table>
<thead>
<tr>
<th>Poverty Profile</th>
<th>Community Organization Level</th>
<th>VDC Level</th>
<th>Program level</th>
</tr>
</thead>
<tbody>
<tr>
<td>Very poor</td>
<td>7.7</td>
<td>0.0</td>
<td>17.6</td>
</tr>
<tr>
<td>Poor</td>
<td>20.5</td>
<td>10.2</td>
<td>18.6</td>
</tr>
<tr>
<td>Capable Poor</td>
<td>23.1</td>
<td>15.4</td>
<td>27.0</td>
</tr>
<tr>
<td>Better-off</td>
<td>48.7</td>
<td>74.4</td>
<td>34.3</td>
</tr>
<tr>
<td>Well-off</td>
<td>0.0</td>
<td>0.0</td>
<td>2.5</td>
</tr>
<tr>
<td>Total %</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
</tr>
</tbody>
</table>

Source: Central Bureau of Statistics (CBS)

Nepal does not have any effective poverty monitoring system. Project and program monitoring indicators often do provide district level data, but in many cases they are limited to specific regions or districts. All the actors, including the state, should bear the responsibility of monitoring poverty reduction and human development activities.
1.3.1.3 World Bank’s Studies

a) Economic Update 2002

World Bank’s Economic Update 2002 prepared for the Nepal Development Forum has reviewed comprehensively the economic situation of Nepal of the period 1990s. During this period, an average economic growth in Nepal increased by about 5% per annum, while population grew by 2.3% annually. Macroeconomic management strengthened in mid 1990s, resulting in healthy improvements in the external and internal balances. Inflation was kept low and stable, and exchange rates pegged to the Indian rupees, which was depreciated gradually to maintain stability and export competitiveness. Growth was mainly led by the non-agricultural sector. Exports played a key role on the demand level. Growth also became more broadly based as agricultural growth picked up in the second half of 1990s.

However, Nepal’s economic performance has radically deteriorated in recent months, halting the acceleration of output and export growth. Growth in the agriculture sector has been slowed down by one third in 2002 and the manufacturing value added expected to contract. Other constraining factors are the decline in export demand caused by the global economic slowdown, relatively slower growth of India and internal factors, such as, frequent strikes from different institutions; Maoist attacks on economic targets and power shortages. Nevertheless, agricultural and rural economic growth remains constrained by inadequate infrastructure, weak irrigation and inadequate other complementary inputs.

Growth of the non-agricultural sector accelerated remarkably during 1990s due to the economic liberalization and stability. Economic liberalization in early 1990s and successful stabilization of the economy in mid 1990s helped to create a favourable environment in the Nepalese economy. The private response in the non-agriculture sector was widespread; industry grew by 8% per year, the manufacturing sector over by 10% and service sector by over 7%. The rapid manufacturing growth was primarily exportable, but supplemented by growth in utility sector as new power sources like Khimti and Puwakhola increased power production capacity by 25% towards the end of the decade. The rapid growth of tourism also contributed to non-agricultural growth until it fell off sharply after the Indian Airlines hijacking incident of 1999.

Foreign trade, notably export growth, was the engine of growth for the economy during 1990s. Helping to produce an export friendly environment was the basic feature of the economic liberalization in early 1990s. It was followed by the successive round of trade liberalization through dismantling of non tariff barriers to imports. In response to these measures, trade and exports grew at 15% in US dollar terms throughout 1990s, and the share of exports and trade in GDP doubled. Most of the export growth had come from garments, carpets and pashmina mostly to OECD countries accounting for more than 50% of the total earnings, but unfortunately it has sharply decelerated in recent months. The declines have been caused by steep falls in exports of carpets, garments and pashmina in the case of OECD countries. The reasons for the fall in exports are due to the saturation in the demand for such products in European Market and high competition among the producing nations of such products. The fall has hurt the industrial sector badly. As a result, a number of industrial units are closed. During this period, not only export has fallen but the import also has failed remarkably causing an economic slow down.
Despite the slowdown in exports, the current account balance and balance of payment position remain strong at present and represents a significant improvement from mid 1990s mainly due to significant increase in the remittance from migrant labour, slow down of imports and the fall in the petroleum prices.

On the other hand, the fiscal position has deteriorated over the past three quarters due to the economic slowdown and political disturbances. Revenue collection is falling, while expenditure pressures are increasing. Difficulties in the revenue collection in the last quarter of FY 2001 contributed to an increased fiscal deficit of nearly 7 % of GDP and a sizeable increase in domestic borrowing (2.7% of GDP). Decline in imports have retarded economic activities and the attacks on liquor sales have contributed to fall in revenue collection, while increase in expenditures are due to rise in security related expenditures. At the current situation, positive fiscal developments are under threat.

The review of recent economic developments shows that the Nepalese economy is going down through a downturn at present. Without a strong program of reform to reverse this downturn Nepal will face difficult medium term economic prospects. This, in turn, will constrain Nepal’s ability to attack poverty and accelerate human development.

Lastly, it can be concluded that Nepal is at a crossroad in its development history. Medium term growth prospects are under threat due to the external shocks and slow implementation of reforms. Poor governance, rising insecurity and political instability are also hindering human development and poverty reduction. The government recognizes that faster growth of incomes and employment and improving governance and public service delivery have to be integral parts of the response to the current crisis.

**b) Nepal, Trade and Competitiveness Study 2003**

The study carried out by the World Bank on the competitiveness of Nepalese trade has identified many challenges to utilize trade potential of Nepal. Geographical structure, low per capita income of US$ 250, high transport cost due to the land-locked character of the country, and limited arable land are some of the challenges.

The study focusing current trade patterns identifies that limited export products like carpet and garment in limited countries like India, Germany and USA are the major challenge. The trade is considered as a major vehicle to overcome the poverty problem. A simulation exercise carried out on the study shows that trade and its other related activities could raise the income of the poor (especially the urban poor) through employment. Besides this, the farmers will be encouraged to switch to higher value crops. Based on the analysis of 1995/96 data with the assumption of average growth rate of 5%, the share of population living below the poverty line would be expected to fall by the end of FY 2007.

Nepal has its macroeconomic policies to carry out liberal economic practices, and the study has considered the trade policy of Nepal as one of the most liberalized policies like that of Sri Lanka. The average tariff has been reduced to 13.8% from 40% and most of the basic tariff structure do not discriminate against imports and are non-protectionist in nature.
But the competitiveness of the Nepal’s economy is considered as low as measured by firm level surveys in manufacturing, farm yields, and aggregate productivity estimates. Labour productivity in manufacturing and agriculture are among the lowest in the region, while manufacturing unit labour costs are among the highest. The three key factors which are found to be influencing productivity are: a) inadequate mechanism and incentives for firms to acquire new technology, b) weak infrastructure, and c) unfriendly business climate. Rigid labour markets in the formal sector with strict anti-dismissal restrictions, prevent incentive-based wages, constrain investment in labour training and decrease labour productivity. So the study emphasizes the labour market improvements to increase competitiveness and formal sector employment.

The study emphasizes the need of extra effort of Nepal to improve its investment climate relative to its competitors. It is noted that the foreign direct investment (FDI) is the lowest in Nepal, even among landlocked countries. Some measures like opening up business support services to foreign investment, rationalizing and reducing the number of organizations that handle investment and trade related issues from more than 10 to about 3, removing constraints on exporters by easing access to duty drawback and introducing a bankruptcy law and its implementations would help to improve the investment climate.

1.3.2 Individual Studies

During the review period, it is found that different researchers have studied the effect of globalization in Nepal. These studies have shown various results that are presented in the following paragraphs.

a) One of the early studies is the Impact of Liberalization, carried by Shanker Sharma and Pusker Bajracharya in 1996 (IIDS 1996). Since the study was made in the very early period of liberalization, the economic situation of that time was relatively better, and the findings of the study are relatively optimistic. The study shows that the average annual growth in exports almost doubled after the liberalization as compared to the pre-liberalization period. Similarly, it also shows that the share of trade in GDP increased by more than 40% during this period. On the other hand, import growth rates were smaller than the export growth rates for two years after liberalization.

This study, though based on the limited information, has found the impacts of trade liberalization and correction of real exchange rate to be positive on the production of food grains as well as cash crops.

The study shows the major changes in the financial sector, such as, opening up the financial sector to private investments, deregulating the interest rates, reducing direct control mechanism, moral persuasion and adoption of market based mechanisms etc. With these mechanisms, the financial market has matured, become more capable, and seems to have instilled confidence among the investors.

b) The study done by Prenushi for the World Bank (1998) has shown that significant gains in poverty reduction by 20% of poor people over the next ten years are achievable, but require growth rates of output which are higher than those experienced over the last couple of years, and which are closer to those of the first half of 1990’s. For achieving such a reduction, it would also
require significant changes in the distribution of income and pattern of growth. It also shows that the growth is not centered to agriculture and does not bring significant benefits to rural areas, which are bound to face growing inequality.

The report shows that the poor have lower agricultural productivity because they have marginal farm land, have limited access to modern inputs and technology, and are illiterate. Those households, which cannot survive only on the products of their land, often send a family member away for earning money, if they can work as agricultural labourers on other people’s land. Off farm work is important for both purposes - to provide required cash for agricultural inputs and to provide security if crops fail- but off farm employment opportunities are not easily available to the poor.

The report has suggested focusing of the poverty alleviation strategy to be broad growth-based, equitable and sustainable. With a low per capita income and almost no surplus to redistribute, there is little scope for targeted poverty alleviation efforts on any scale large enough to make difference at the national level; therefore, poverty alleviation will require faster per capita income growth and, in turn, faster output growth and slower population growth.

c) Acharya (1999) has viewed that the globalization in Nepal has disrupted traditional livelihood patterns of rural poor in Nepal. She emphasis that “The globalization process in Nepal is rather a process of deeper and still deeper penetration of the Nepalese market by the Indian capital and labour with very little gains for the mass of the population. A minority has benefited and income inequalities have increased, tearing the existing social fabric, which may lead to explosive political situation. One indicator of such ferment is the Maoist problem spiraling into higher and higher levels of violence, both from the government and insurgents’ sides”.

d) Sapkota (2002) in his study on Trade Liberalization and Poverty in Nepal: An Applied General Equilibrium Analysis has used the computable general equilibrium modeling system to understand functioning of market economy in a deep manner and present the facts of the policy outcome. The findings show that urban households have more benefited from the liberal market economy than the rural one. The poverty impact assessment of this study shows that poverty increases up to the average minimum and decreases thereafter. The impacts of trade liberalisation according to this study decreases household welfare and increases poverty at the lower income level and increases welfare and reduces poverty at the higher income level. Thus the study suggests for remoulding taxation system to address the problems of poverty and inequality.

1.4 Globalization Process in Nepal

During the period of 1980 to 1995, many ups and downs were felt in the world economic and political scenario. The political changes in the international arena also brought economic changes with it. Many countries began to reform their economies by adopting liberal and open market economy. Many developing countries began to change their economic policy from the government regulated mixed or socialist economy to the open market economy. The world oil crisis, due to the Gulf-War of 1990, is another important event, which influenced the world
The echoes of these events heard worldwide also largely affected the political and economic policies of least developed countries like Nepal.

The adoption of liberal market economy in both the neighboring countries - India and China further pressurized Nepal to be more open to participate in the competitive world. The dramatic changes in the economic structure of China from the controlled regime to the open market economy with a very high growth rate lessened the ideological influence of the advocates of the command economic philosophy.

1.4.1 Understanding of the Concept of Globalization in Nepal

In Nepal, the policy makers, academia and other people from different walks of life have understood the globalization as a means of bringing changes in the national economic activities through the adoption of liberal economic policy. Globalization is the process through which national economies in different part of the world are integrated. In fact, the globalization process was initiated by the developed world with the support of multinational organizations. The multinational organizations are motivated to promote the globalization process because of technological developments, wider trade and investment, and the changing production, organizational and marketing strategies promoted by them. The pace and depth of globalization differ across countries and regions, but the main economic aspects of the process are essentially the same. It takes into account the following elements:

- Free movements of goods and services
- Free movement of capital
- Subcontracting of activities by companies, greater specialization and new forms of work organization.
- Increase in the degree of openness

a. Its supporters advocate that it will bring the following results:

- Openness will create opportunities for jobs. Jobs are being created as business opportunity increases with the reduction of trade barriers and the decentralization of production to take advantage of benefits specific to the location of their facilities.
- Promotes efficient allocation of resources
- Promotes equitable distribution of income
- Promotes macroeconomic stability in the developing countries

b. Views of the Critics:

- Globalization will not create opportunities, rather it will limit the possibilities for the weak
- Large scale business houses influence the use of resources
- Inequality in the distribution of income and wealth; rich getting richer and the poor not improving themselves
• On the whole, job opportunities for women in high-growth sectors remain limited, mainly because of the lack of their required skills.

• Greater specialization and widespread application of advanced technologies have stimulated a rise in demand for skilled labour in fields, like information technology (IT), specialized financial and other business services etc.

• Technological change and specialized production strategies tend to favor skilled and well-educated workers – a category in which women are severely under-represented. In Nepal, this is more prominent. Women are in jobs which are more likely to be subcontracted, relocated abroad or eliminated by labour-saving technologies.

• The traditional gender disparities in wages appear to be widening. The cumulative effects of persistent discriminatory practices may explain this, a deepening polarization of skilled and unskilled labour with women being caught in a “low-skilled/low-paid job trap”.

The policy makers in Nepal that the globalization is in the panacea to solve all the problems. Because of the inefficiency of public enterprises due to the leakages, corruption etc, the privatization process is adopted in Nepal. It is conceived that the privatization will solve the problems of inefficiency because it is expected that the private sector will handle the resources more efficiently.

It is being felt that the neighboring countries of Nepal have adopted liberalized economic policy to exploit the opportunities provided by globalization process. If Nepal will not participate in this process, her economy may lag behind to use the opportunities.

1.4.2 Trend of Globalization in the World and South Asia from the perspectives of Nepal

• Majority of the countries of South Asia have joined the mission of globalization. Some of them have taken the membership of WTO from the beginning of its inception. Nepal had not taken the membership of WTO for a long time. Right now, its membership is accepted and recently, Nepal has already got the membership of WTO.

• Movements of FDI have increased in South Asia and competition is intensified among the countries of South Asia to increase the inflow of foreign direct investment.

• New types of production are emerging in these countries due to the working of multinational companies, internationalization of production and development of specialization in production. In new products, the products of IT, both hardware and software, are growing.

• Technological innovation and especially the development of information and communication technologies have transformed production processes, shortened product life cycles and revolutionized services.