

# 1. Economic Activities

## World Economy

1.01 The world economy witnessed an expansion of 4.9 percent in 2007. This is slightly lower than that in the previous year. In the backdrop of the currently observed economic slowdown emanated mainly from the US sub-prime mortgage crisis, the world economy is projected to grow at a lower rate of 3.7 percent in 2008 and to continue at about the same pace in 2009. These estimates reveal a contractionary trend similar to the ones observed at the beginning of this millennium. Earlier, notwithstanding the higher growth of 4.7 percent recorded in the year 2000, the world economy had observed slowdown and grew at a lower rate of 2.2 percent in 2001 and 2.8 percent in 2002. However, the world economy rebounded in the subsequent years and grew by 3.6 percent, 4.9 percent, and 4.4 percent in 2003, 2004 and 2005 respectively. Also, the per capita income growth is estimated to remain lower in 2008 and 2009. The per capita income growth for advanced economies for both of these years is projected at 0.8 percent compared to 2.1 percent in 2007. The per capita income growth for developing economies is projected at 5.4 percent in both 2008 and 2009. This was 6.6 percent in 2007.

**Table 1(a) : World Economic Growth Rates**  
(Annual Percentage Change)

	2005	2006	2007	Projection	
				2008	2009
<i>World Output</i>	4.4	5.0	4.9	3.7	3.8
<i>Advanced Economies</i>	2.6	3.0	2.7	1.3	1.3
<i>Major Advanced Economies</i>	2.3	2.7	2.2	0.9	0.9
<i>Other Advanced Economies</i>	3.2	3.8	3.9	2.5	2.7
<i>Developing Economies</i>	7.1	7.8	7.9	6.7	6.6
<i>Developing Asia</i>	9.0	9.6	9.7	8.2	8.4
<i>Emerging European Economies</i>	5.6	6.7	5.8	4.4	4.3
<i>African Economies</i>	5.7	5.9	6.2	6.3	6.4
<i>Middle-East Economies</i>	5.7	5.8	5.8	6.1	6.1
<i>Oil-Exporting Middle-East Asian Economies</i>	5.6	5.8	5.6	6.0	5.9
<i>Emerging Asia</i>	8.7	8.9	9.1	7.5	7.8

	2005	2006	2007	Projection	
				2008	2009
<i>Newly Industrialized Asian Economies</i>	4.8	5.6	5.6	4.0	4.4
<i>ASEAN-5</i>	5.1	5.7	6.3	5.8	6.0
<i>Per Capita Income</i>					
<i>Advanced Economies</i>	1.9	2.4	2.1	0.8	0.8
<i>Developing Economies</i>	5.8	6.5	6.6	5.4	5.4

Source: IMF, *World Economic Outlook*, Washington DC, April 2008

- 1.02 As a fall-out of the financial market problems, the US economy is expected to experience a major slowdown with a meager growth rate of 0.5 percent in 2008 and 0.6 percent in 2009. This follows a low growth trajectory from 3.6 percent in 2004 to 2.2 percent in 2007. This is also likely to affect other advanced as well as emerging and developing economies through trade and financial linkages. However, the US has been actively exercising the instruments of major macroeconomic policies (monetary policy and fiscal policy) to check the probable economic recession. In the same vein, the US government unveiled a US\$ 150 billion fiscal stimulus package in January 2008, and the US central Bank-Federal Reserve-has gradually slashed the federal funds rate from above 5 percent in early September 2007, to 2 percent in April 2008.
- 1.03 The world trade, owing to the difficulties facing the US economy, is expected to decline in 2008. The world trade is projected to grow at a lower rate of 5.6 percent in 2008 and 5.8 percent in 2009, compared to the 6.8 percent growth experienced in 2007.

**Table 1(b) : World Trade**  
(Annual Percentage Change)

	2005	2006	2007	Projection	
				2008	2009
<b>World Trade Volume (Goods and Services)</b>	7.6	9.2	6.8	5.6	5.8
<b><u>Import</u></b>					
<b>Advanced Economies</b>	6.3	7.4	4.2	3.1	3.7
<b>Developing Economies</b>	12.0	14.4	12.8	11.8	10.7
<b><u>Export</u></b>					
<b>Advanced Economies</b>	6.0	8.2	5.8	4.5	4.2
<b>Developing Economies</b>	11.1	10.9	8.9	7.1	8.7

Source: IMF, *World Economic Outlook*, Washington DC, April 2008

- 1.04 Along with the slowdown in global growth and trade fronts, skyrocketing oil-prices in the world market and growing food-crisis in developing economies have exerted pressure on general price level. The inflation in advanced economies is estimated at 2.6 percent for 2008 up, from 2.2 percent in 2007. In developing economies, inflation is estimated 7.4 percent in 2008 from 6.4 percent in 2007. The inflationary trend follows the increased demand in emerging and developing economies and burgeoning food and energy prices in most of the economies around the world.

**Table 1(c) : World Price Situation**

(Annual Percentage Change)

	2005	2006	2007	Projection	
				2008	2009
<b>Petroleum Products (oil) *</b>	41.3	20.5	10.7	34.3	-1.0
<b>Non-fuel goods</b>	6.1	23.2	14.0	7.0	-4.9
<b><u>Consumer Prices</u></b>					
<b>Advanced Economies</b>	2.3	2.4	2.2	2.6	2.0
<b>Developing Economies</b>	5.7	5.4	6.4	7.4	5.7
<b>Developing Asia</b>	3.8	4.1	5.3	5.9	4.1
<b>Emerging European Economies</b>	4.9	5.4	5.7	6.4	4.3
<b>African Economies</b>	5.1	5.4	5.6	6.4	4.3
<b>Middle-East Economies</b>	6.2	7.0	10.4	11.5	10.0
<b>Petroleum Product Exporting Countries</b>	6.7	7.6	10.5	12.2	10.4
<b>Emerging Asia</b>	3.5	3.7	4.8	5.5	3.9
<b>Newly Industrialized Asian Economies</b>	2.2	1.6	2.2	3.0	2.7
<b>ASEAN-5</b>	7.3	8.1	4.5	6.1	4.7
<b>China</b>	1.8	1.5	4.8	5.9	3.6
<b>South Asia</b>	5.0	6.5	6.9	5.9	4.7
<b>Bangladesh</b>	7.0	6.5	8.4	9.3	8.1
<b>Bhutan</b>	5.3	5.0	4.9	4.7	4.3
<b>India</b>	4.2	6.2	6.4	5.2	4.0
<b>Maldives</b>	3.3	3.7	5.0	6.0	6.0
<b>Nepal</b>	4.5	8.0	6.4	6.4	4.9
<b>Pakistan</b>	9.3	7.9	7.8	8.5	7.5
<b>Sri Lanka</b>	1.6	9.5	19.7	11.5	9.0

\* Average of the price of Brent Oil (UK) and price of raw petroleum products of Dubai and West Texas

Source: IMF, World Economic Outlook, Washington DC, April 2008

- 1.05 Instability surfacing the global financial market, low growth of the world economy, shooting price of petroleum products and foodstuff

including the increasing global imbalances are major challenges facing the global economy.

## Neighboring Economies

1.06 Nepal's two large neighboring economies India and China witnessed an impressive growth in 2007 as well. These economies grew by 9.2 percent and 11.4 percent respectively. The projection for these economies for 2008, however, is at the lower side of 7.9 percent and 9.3 percent respectively. Nepal, a low growth economy with a lower per capita income in the region, needs to make the best use of the available opportunities through learning lessons from the amazing performance of her neighboring economies.

**Table 1(d) : Economic Growth Rate of Neighbouring Economies**  
(Annual Percentage Change)

	1990/99	2000/04	2005	2006	2007	Projection	
						2008	2009
<i>China</i>	9.9	9.2	10.4	11.1	11.4	9.3	9.5
<i>South Asia</i>			8.6	9.1	8.6	7.5	7.7
<i>Afganistan</i>			16.4	6.1	12.4	8.6	8.4
<i>Bangladesh</i>	4.8	5.4	6.3	6.4	5.6	5.5	6.5
<i>Bhutan</i>	5.6	7.8	6.9	11.0	22.4	7.8	6.7
<i>India</i>	5.6	5.7	9.1	9.7	9.2	7.9	8.0
<i>Maldives</i>	6.5	6.6	-4.5	19.1	6.6	4.5	4.0
<i>Nepal</i>	4.9	4.1	3.1	2.8	2.5	4.0	4.5
<i>Pakistan</i>	4.0	4.3	7.7	6.9	6.4	6.0	6.7
<i>Sri Lanka</i>	5.2	4.0	6.0	7.4	6.3	6.4	5.6

Source: IMF, *World Economic Outlook*, Washington DC, April 2008

**Table 1(e) : Per Capita National Income**  
(2006)

In US Dollars	
<i>China</i>	2000
<u><i>SAARC Countries</i></u>	
<i>Afganistan</i>	—
<i>Bangladesh</i>	450
<i>Bhutan</i>	1430
<i>India</i>	820
<i>Maldives</i>	3010
<i>Nepal</i>	320
<i>Pakistan</i>	800
<i>Sri Lanka</i>	1310

Source: www.worldbank.org, World Development Indicators database, World Bank, April 11, 2008

## Nepal in Human Development Index

1.07 Nepal's Human Development Index (HDI) is at the lower ebb as mentioned in the Human Development Report 2007. Of the 177 countries included in the Report, Nepal is at 142nd position—the lowest among SAARC countries. The HDI that incorporates education, health, and per capita income is a composite index to measure the overall human development. This reflects that Nepal is trailing behind not just from low economic growth but also from the dimensions of overall human development.

**Table 1(f) : Situation of Human Development**  
(2005)

	Position in Human Development Index
<i>China</i>	81
<u><i>SAARC Countries</i></u>	
<i>Sri Lanka</i>	99
<i>Maldives</i>	100
<i>India</i>	128
<i>Bhutan</i>	133
<i>Pakistan</i>	136
<i>Bangladesh</i>	140
<i>Nepal</i>	142
<i>Afganistan</i>	.....

### Box 1(a) : Government's Role in Economic Growth

The (i) Government, (ii) Culture, and (iii) Geography, Environment and Natural Resources are taken as the basic pillars of economic growth. Economists point out the need for government's role mainly due to the market failure. It is therefore government's role is important in the economy mainly because of the following reasons:

- a) Providing public goods such as rule of law, effective regulation and development of physical infrastructure.
- b) Managing positive externalities such as those emanating from the investment in education, health, and research, and the negative ones such as the effect of the pollution.
- c) Controlling and monitoring monopoly, and
- d) Managing the coordination failure occurring in the private sector

A number of world economies that were at the same level with their neighboring economies in terms of education, health, per capita income and natural resources some five decades ago, have been successful in attaining significantly higher level of economic development because of

the government's role. Countries like Sri Lanka, Botswana, China, and South Africa have proved that significant progress could be achieved even in a short period mainly due to the qualitative improvements in and effectiveness of the government's role. The Human Development Report 2003 highlights that Sri Lanka had increased life expectancy of her people from 46 years to 58 years during 1946 to 1953. Botswana was able to increase the primary school enrollment rate from 46 percent to 89 percent during 1970 through 1985. China successfully reduced the poverty rate from 33 percent to 18 percent in the decade of 1990s. And South Africa was able to reduce the number of people lacking access to clean drinking water from 15 million to 7 million only in a period of 4 years during 1997 through 2001.

In the background of these theories and instances, Nepal's need of the hour is to develop a far-sighted vision to ensure an effective state mechanism, even taking into account the experiences of other economies, that facilitates in attaining higher level of economic growth.

Source: David N. Weil, Economic Growth (2005) and UNDP Human Development Report (2003)

## National Economic Activities

- 1.08 The Government of Nepal (GON) released the Three-Year Interim Plan (TYIP) for 2007/08-2009/10 in December 2007. The main objective of the Interim Plan is to lay the foundation of economic and social transformation for developing a prosperous, modern, and judicious Nepal. The Plan aims at reducing unemployment, poverty, and inequality to support enduring peace and to make people experience change directly in their life-style.

### **Box 1(b) : Three-Year Interim Plan (2007/08-2009/10)**

The average annual economic growth targeted for the Plan period is 5.5 percent with a per capita income growth of 3.3 percent. Of the total growth, agriculture is expected to grow by 3.6 percent and non-agriculture by 6.5 percent. The Plan has laid out the following considerations at the basis for the sectoral distribution of investment for attaining the targeted growth.

1. Taking the post-conflict situation into account, priority will be given to allocation of resources for reconstruction, rehabilitation and inclusion.
2. Resources will be provided to priority areas that will support broad-based, inclusive and sustainable development. Public investment will be concentrated more on effective delivery of services and infrastructure development.
3. In agriculture development, special attention will be paid to agricultural roads, agricultural credit, research and dissemination of technology,

- irrigation, rural electrification and market mechanism development.
4. Backward geographical areas, ethnic groups, communities, women, disabled, senior citizens, and the Madhesi will be included in the development process and outcomes.
  5. Concrete contribution to poverty alleviation and economic growth will be made by emphasizing programs that raise the income of the poor and marginalized communities, and empower them.
  6. Emphasis will be given to increase the private sector investment in potential areas like electricity, communications, rural electrification and roads, where the government is currently engaged.
  7. Investment will be made in some big projects in order to generate people's confidence towards the state and to generate opportunities for employment. At the local level, multiple projects that are identified and manageable by the communities will be implemented, thereby increasing people's participation, ownership, and employment.

*Source: Three-Year Interim Plan 2007/08 -2009/10*

- 1.09 The Central Bureau of Statistics (CBS) introduced new series of National Accounts Statistics since 2006/07 taking 2000/01 as the base year. This follows the System of National Accounts, 1993. The preliminary estimates for 2007/08 are based on six-to-nine months data collected from various economic sectors.

**Box 1(c) : New Series of National Income Statistics**

New series of the National Income Accounts, which takes 2000/01 as the base year, was introduced in 2006/07. The base year 2000/01 has been selected since the timing of a number of censuses such as population census, agricultural census; and industrial census are closer to this year and also it could be useful to make comparison with international statistics as well. Nepal's national accounts data series in the past were based on succeeding benchmark years, namely, FY 1964/65, FY 1974/75, FY 1984/85 and FY 1994/95.

The need for a new series arose in order to reorient the national accounts preparation method, introduce new concepts and definitions, and respond to the need for new classification. Prior to this, Nepal's national income statistics was based on the system of national accounts 1968. A number of countries around the world had already adopted the SNA 1993. This had also made it necessary for Nepal to adopt SNA 1993. Adoption of the SNA 1993 is indeed a step forward in defining and conceptualizing the major macroeconomic variables such as production, consumption and investment. Economic activities, under this system, have been classified into 15 sectors while there were only 9 sectors in SNA 1968. The new system provides the estimation of value addition, production and intermediate consumption. The International Standard Industrial

Classification (ISIC), Revision 3 has classified entire economy into 17 sectors. In Nepal's case, however, constitution of workers in the private household and from activities of foreign missions, and INGOs to the GDP is found negligible. It is therefore data pertaining to these two sectors have been included in the Other Community, Social and Individual Services category.

New series includes many activities not included in the previous series. These consists of microbus, cable car services under transportation; PCO, mobile telephone, internet, cable television, communication; renting; services of employment agencies, cooperatives, consultancies, computer and photography, private postal services, private sector education services, community forestry and others. Thirty new surveys and studies were conducted to strengthen the national income statistics.

Improvement has also been made in the national accounts survey-frame and estimation methods. For example, revision has been made in the costing ratios of the production that have changed especially on account of the technological progress in many of the services activities. In addition to the construction of traditionally prepared series such as GDP, GNI and consumption, attempt has been made to make the national accounts data user friendly by providing reliable estimates of saving, disposable income, value added, consumption, capital formation and saving by institutional sectors such as government, business enterprises, households, and non-profit organizations. The new accounting system based on the SNA 1993 aims at making Nepalese statistics comparable with the international assumptions and standard.

*Source: Central Bureau of Statistics*

- 1.10 Higher economic growth has been attained in FY 2007/08 compared to the past few years. According to the National Accounts Statistics prepared by the Central Bureau of Statistics on the basis of six to nine months data of the current fiscal year, the economic growth is estimated to have been expanded by 5.56 percent at the basic price and by 4.7 percent at the producers' price. The upside estimate mainly comes from the substantial increase of 16.8 percent in the paddy production following the favorable weather condition and expansion in the production of vegetables and fruits. These expansions contributed to a higher growth of 5.65 percent in the agriculture sector that alone contributes 32 percent to GDP. It is noteworthy to mention that the agriculture as well as the overall growth rebounded this year reflecting the highest performance amongst those in the last seven years. In the non-agricultural sector, the growth of wholesale and retail trade, hotel and restaurant,

transport, storage and communication and financial sector remained encouraging. Gradual improvement in the peace and security situation, establishment of additional bank and financial institutions, and increase in the tourist arrival with the restoration of peace led expansion of these sectors. However, the industrial production accounting around 7 percent to the GDP grew meagerly. Frequent industrial disputes, bandhs, strikes, and waning competitive strength badly hampered the industrial production.

**Table 1(g) : GDP growth (According to the Industrial Classification)**  
(Percentage Change in Constant Price)

Industrial Classification	Fiscal Year						
	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07*	2007/08**
Agriculture and Forest	3.01	3.32	4.72	3.45	1.67	0.94	5.65
Fisheries	8.71	4.00	12.23	7.13	9.91	2.99	7.09
Mining and Quarrying	8.79	3.20	-0.43	6.80	8.26	1.47	2.84
Industry	-5.32	0.04	2.15	2.62	2.00	2.55	0.18
Electricity, Gas and Water	11.37	19.04	4.07	3.97	4.01	13.00	3.44
Construction	6.41	2.10	-0.35	2.90	7.67	2.49	3.11
Wholesale and Retail Trade	-11.57	2.26	10.81	-6.24	3.66	-4.45	6.43
Hotel and Restaurant	-18.23	2.01	12.74	-5.41	5.99	3.54	7.55
Transport, Storage and Communication	8.37	5.20	7.49	1.98	6.95	4.45	6.60
Financial Intermediation	3.82	1.66	6.19	24.30	24.35	11.39	13.81
Real Estate, Rent and Professional Services	-4.89	-3.97	-2.09	10.03	6.34	11.76	4.42
Public Administration and Defense	36.85	11.52	-0.64	6.64	6.88	1.35	5.65
Education	21.05	13.71	5.12	9.82	3.75	6.24	4.62
Health and Social Services	7.38	15.26	6.11	11.33	5.91	6.71	7.39
Other Community, Social and Individual Services	-8.62	4.40	13.43	-3.38	3.34	11.78	11.07
Gross Value Added (including financial intermediation services valued indirectly)	0.46	3.45	5.13	2.97	4.36	2.96	5.60
Financial Intermediation Services indirectly measured	10.67	-6.62	30.13	6.23	11.20	12.41	6.48
GDP (at basic price)	0.16	3.77	4.41	2.85	4.11	2.58	5.56
Goods and Services, net tax	-0.47	6.55	8.60	6.87	-1.51	11.82	-6.41
GDP (at producers' price)	0.12	3.95	4.68	3.12	3.72	3.19	4.70

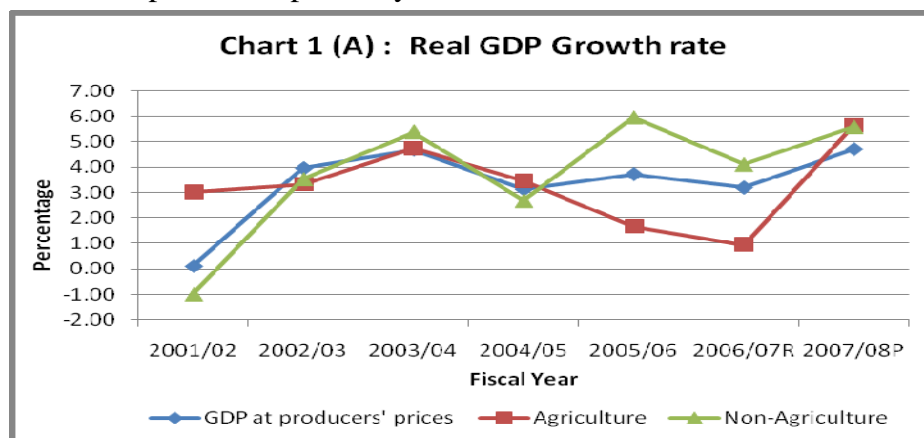
\*revised, \*\* preliminary

Source: Central Bureau of Statistics

1.11 The Central Bureau of Statistics uses the implicit GDP deflator while converting the national account statistics available at the current market price to the base year price. The GDP deflator adjusts GDP at nominal price with GDP at constant price. As earlier mentioned, FY 2000/01 has been taken as the base year in the new National Accounts Statistics. According to the deflator estimate, the overall price index has been estimated to go up by 7.7 percent in 2007/08. The overall inflation based on consumer price is estimated at 7.4 percent this year. This follows the data released by Nepal Rastra Bank for the first nine months for which the average increase in the consumer price stood at 6.7 percent, and the inflationary estimates for the remaining three months. On the wholesale price front, an 8.6 percent average inflation is estimated for FY 2007/08. This is based on the average wholesale price inflation of 8.1 percent in the first nine months of 2007/08 and estimated average wholesale price inflation of 10.3 percent for the remaining period of the year. The upside projection is based on two forces exerting pressure on the price front. These include the substantial hikes in the prices of petroleum products on three different occasions in FY 2007/08 together with escalating food prices observed in the market.

## Real GDP

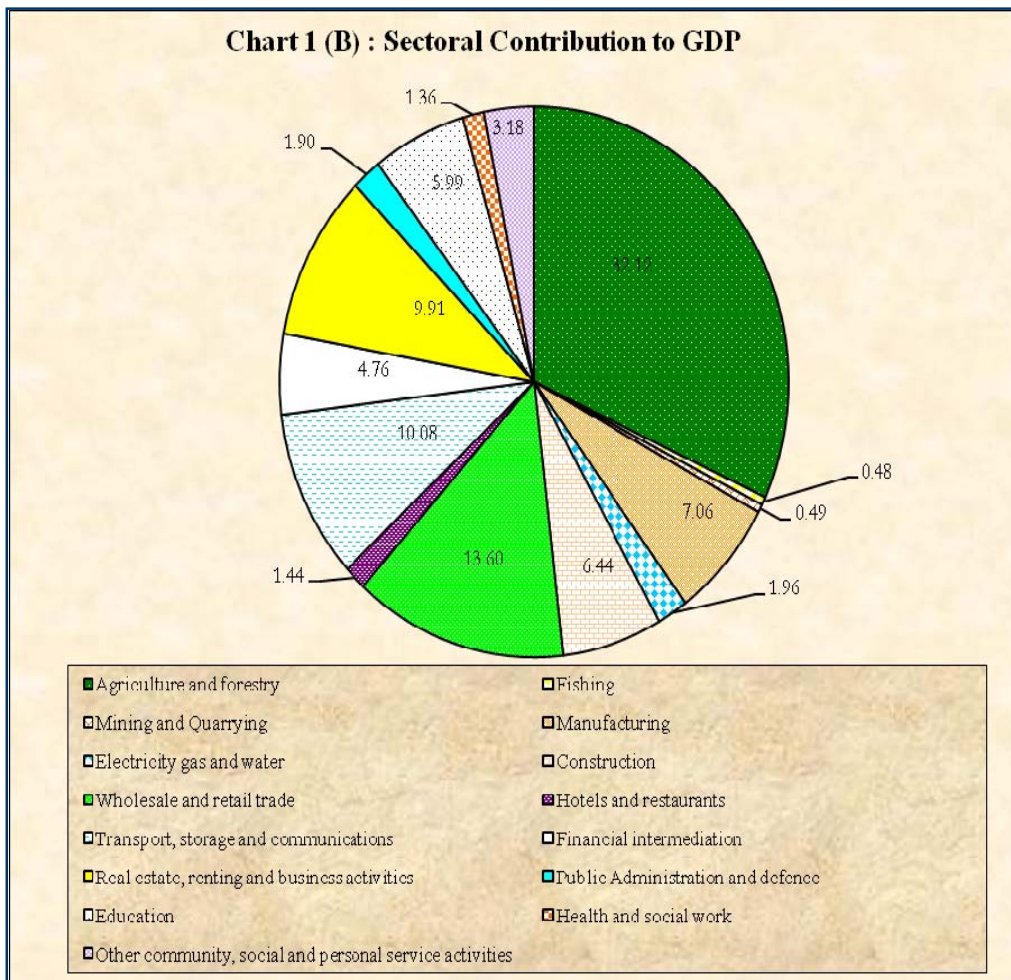
1.12 As stated earlier, GDP growth for FY 2007/08 at basic price is estimated at 5.56 percent. Last year, the GDP growth rate was 2.58 percent. GDP at the producer's price is estimated to increase by 4.7 percent in FY 2007/08 compared to 3.2 percent last year. The growth estimate is supported by the expansion of both the agriculture, and nonagricultural sectors, with their estimated growth of 5.65 percent and 5.57 percent respectively.



- 1.13 The contribution of agriculture and non-agriculture sector at producers' price is estimated at 34.6 percent and 65.4 percent respectively. In the previous year, these ratios were 34.3 percent and 65.7 percent respectively.
- 1.14 According to the agricultural production index, which is prepared by grouping several agricultural produces, food crops is estimated to have gone up by 7.27 percent. In this group, paddy, maize and wheat crops are estimated to grow by 16.8 percent, 3.23 percent and 3.76 percent respectively. Similarly, the production of vegetables and nursery is estimated to have increased by 9.59 percent and fruits and spices by 5.4 percent. Preliminary estimates for the growth of livestock and bird-rearing are 2.58 percent and 3.09 percent respectively. The estimated growth of forest and forest-related produces is 0.2 percent and of fisheries is 7.09 percent.
- 1.15 Mining and quarrying is estimated to have grown by 2.84 percent, compared to 1.47 percent growth a year ago. This sector grew because of the increase in the production related to quarrying, despite a downturn observed in the mining.
- 1.16 Despite relative growth of other sectors, the preliminary estimate shows that the manufacturing sector remained sluggish. The growth of this sector is estimated at 0.18 percent in FY 2007/08 compared to 2.55 percent last year. According to the production index for the first six months of the current fiscal year, the production of mustard and soybean oil, rice, wheat, biscuits, sugar, instant noodles, tea, liquors, cigarette, jute products, paper among others showed a growth. However, the decrease in the production of vegetable-ghee, milk-products, woolen carpets, readymade garments, soap, plastic products etc, that has a higher weightage on the production index accounted for the minimal growth of this sector.
- 1.17 The growth of electricity, gas and water is estimated at 3.44 percent compared to 13 percent in the last year. Similarly, the growth of construction sector is estimated at 3.11 percent compared to 2.49 percent last year. As shown by the manufacturing index of the first six months, the production of construction materials such as bricks, cement, iron rod, and electricity products has witnessed an increment.
- 1.18 On the wholesale and retail trade front, the estimated growth is 6.43 percent. This sector had experienced a negative growth of 4.45 percent in the previous year. The higher growth of this sector is

estimated to have come from tradable domestic agro-products and imports. Similarly, the growth of hotel and restaurant sector is estimated at 7.55 percent compared to the growth of 3.54 percent last year. This higher growth is estimated given the significant inflow of tourists together with the expansion of domestic tourism.

- 1.19 The growth of the transport, communication, and storage sector is estimated at 6.6 percent compared to 4.45 percent last year. This sector expanded because of the extension of communication services. As in the last year, financial intermediaries sector recorded a higher growth in 2007/08. This is estimated to have grown by 13.84 percent compared to 11.39 percent last year. Similar to the last year, the establishment of new banks and financial institutions and expansion in their transactions contributed to the higher growth of financial intermediation sector.



- 1.20 Real estate, rent and professional services sector is estimated to have grown by 4.42 percent in 2007/08. This sector increased by 11.76 percent in the previous year. The growth of this sector remained lower compared to last year due mainly to the decline in the transaction of Rural Housing Company Ltd. in the current fiscal year. Also low level of transactions of some of the other professional services contributed to this slowdown. The public administration and defense sector is expected to grow by 5.65 percent. Last year, the growth of this sector was 1.35 percent. This is based on the GON's projection of the expenses in public administration and defense.
- 1.21 The educational sector is estimated to have grown by 4.62 percent in the current fiscal year. Last year, this sector recorded a growth of 6.24 percent. On the basis of the change in the indicator of educational activities carried out by the government and the non-government sector, the said growth rate is likely to be achieved. Similarly, the health sector is estimated to have grown by 7.39 percent in the current fiscal year, compared to 6.71 percent last year. The increased growth of health sector has been estimated given the expansion of private sector health services. Other community, social and individual services sector is estimated to grow by 11.07 percent. This sector had increased by 11.78 percent last year. Several types of social and individual services including, community services provided by the government sector falls under this category. This sector also includes the contribution of domestic workers and economic activities of international organizations and missions as these activities did not require separate classifications because of their narrow level.

**Table 1(h) : Major Macroeconomic Indicators<sup>a</sup>**

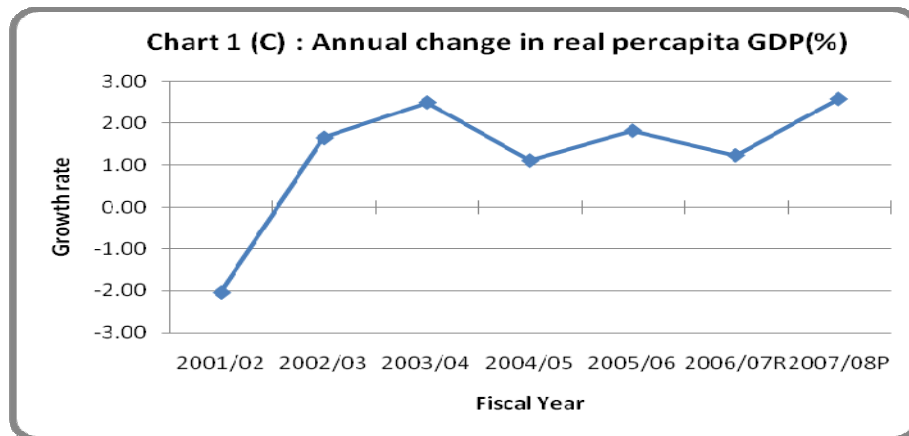
Indicators	Unit	Fiscal Year						
		2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08 <sup>1</sup>
<i>Real GDP</i>	Annual % Change	0.2	3.8	4.4	2.9	4.1	2.6	5.6
<i>- At Basic Prices</i>	„	0.5	3.4	5.1	3.0	4.4	3.0	5.6
<i>- At Basic Prices Including FISIM</i>	„	3.0	3.3	4.7	3.4	1.7	0.9	5.7
<i>* Agriculture</i>	„	-1.0	3.5	5.4	2.7	6.0	4.1	5.6
<i>* Non-Agriculture</i>	„	0.1	4.0	4.7	3.1	3.7	3.2	4.7
<i>- At Producers' Prices</i>	„	-2.5	1.6	2.3	1.7	2.3	1.5	2.8
<i>Per capita national income (constant price)</i>	„							

Indicators	Unit	Fiscal Year						
		2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08 <sup>1</sup>
<b>Overall Agricultural Index</b>	„	2.4	3.7	3.2	2.8	1.7	0.9	5.7
- <i>Food and other crops</i>	„	2.3	2.0	3.4	1.5	1.4	-2.7	7.27
- <i>Livestock</i>	„	2.5	3.2	3.4	2.1	2.5	3.1	2.6
- <i>Vegetables and Horticulture</i>	„	5.1	3.6	5.0	9.3	6.0	6.4	9.60
- <i>Forest Production</i>	„	1.9	1.9	1.0	0.2	-2.5	1.7	0.2
<b>Major Industrial Production Index</b>	„	-6.6	2.4	2.1	2.6	1.9	2.1	-0.2
<b>GDP price deflator<sup>2</sup></b>	„	3.9	3.1	4.0	6.3	6.6	7.4	7.7
- <i>Agriculture</i>	„	3.5	0.8	2.7	3.5	4.3	6.7	7.7
- <i>Non-Agriculture</i>	„	4.1	4.5	4.8	7.7	7.6	7.9	7.6
<b>National Urban Consumer Price Index<sup>3</sup></b>	„	2.9	4.8	4.0	4.5	8.0	6.4	7.4
<b>Ratio as percent of GDP at current producer's price</b>								
- <i>Gross Domestic Saving</i>	%	9.5	8.6	11.8	11.6	9.0	9.7	11.5
- <i>Gross National Saving</i>	%	24.2	23.8	27.3	28.4	29.0	28.5	32.0
- <i>Gross Fixed Capital Formation</i>	%	19.6	19.9	20.3	19.9	20.7	20.4	21.1
- <i>Gross Investment</i>	%	20.2	21.4	24.5	26.5	26.8	28.0	32.0
- <i>Gap between Domestic Saving and Investment</i>	%	-10.7	-12.8	-12.7	-14.9	-17.8	-18.3	-20.5
- <i>Gross Consumption</i>	%	90.5	91.4	88.3	88.4	91.0	90.3	88.5
- <i>Government Expenditure<sup>4</sup></i>	%	17.4	17.1	16.7	17.4	17.0	18.4	19.7
- <i>Recurrent Expenditure<sup>4</sup></i>	%	10.6	10.6	10.3	10.5	10.2	10.6	11.3
- <i>Capital Expenditure<sup>4</sup></i>	%	5.4	4.5	4.3	4.6	4.5	5.5	6.5
- <i>Principal Repayments<sup>4</sup></i>	%	1.4	1.9	2.0	2.3	2.2	2.3	1.9
- <i>Debt Service (principal and interest payments)</i>	%	2.7	3.3	3.2	3.4	3.1	3.2	2.6
- <i>Revenue</i>	%	11.0	11.4	11.6	11.9	11.1	12.1	13.0
- <i>Tax Revenue</i>	%	8.6	8.7	9.0	9.2	8.8	9.8	10.2
- <i>Non-Tax Revenue</i>	%	2.4	2.8	2.6	2.7	2.3	2.3	2.8
- <i>Budget Deficit</i>	%	5.0	3.3	2.9	3.1	3.8	4.1	4.0
- <i>Foreign Loan</i>	%	1.7	0.9	1.4	1.6	0.6	1.6	1.4
- <i>Foreign Loan and Grant</i>	%	3.1	3.2	3.5	4.0	2.7	3.8	4.1
- <i>Outstanding Domestic Debt</i>	%	15.1	16.4	15.2	14.1	14.5	14.3	13.1
- <i>Outstanding Foreign Debt</i>	%	47.9	45.4	43.4	37.3	35.8	29.8	26.3
- <i>Total Outstanding Debt</i>	%	63.0	61.8	58.5	51.3	50.3	44.1	39.4

Indicators	Unit	Fiscal Year						
		2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08 <sup>1</sup>
<i>-Merchandise Export</i>	%	10.2	10.1	10.0	10.0	9.2	8.4	7.3
<i>-Merchandise Import</i>	%	23.4	25.3	25.4	25.4	26.6	26.4	27.3
<i>-Trade Deficit</i>	%	-13.2	-15.1	-15.3	-15.4	-17.4	-18.0	-22.6
<i>-Tourism Income</i>	%	1.9	2.4	3.4	1.8	1.5	1.4	2.2
<i>-Workers' Remittance</i>	%	10.3	11.0	10.9	11.1	14.9	13.8	16.5
<i>-Current Account</i>	%	4.0	2.4	2.7	2.0	2.2	0.5	0.2
<i>Outstanding Foreign Debt /Total Revenue</i>	%	436.4	397.4	373.5	313.2	323.7	247.0	202.8
<i>Outstanding Foreign Debt/Export</i>	%	468.9	447.5	431.8	374.1	388.4	356.3	362.6
<i>Government Revenue</i>	% Change	3.2	11.5	10.9	12.5	3.1	21.3	21.5
<i>Recurrent Expenditure</i>	% Change	6.6	6.6	6.6	11.0	8.6	15.1	20.4
<i>Capital Expenditure</i>	% Change	-12.5	-9.8	3.3	18.4	8.3	34.2	34.9
<i>Principal Repayments</i>	% Change	13.1	48.6	12.9	25.4	5.4	17.4	-7.1
<i>Total Government Exp</i>	% Change	0.3	4.9	6.5	14.7	8.1	20.5	21.3
<i>Debt Service (principal and interest payment)</i>	% Change	17.5	32.6	7.1	13.9	3.4	12.2	-5.2
<i>Debt Service/Recurrent Expenditure</i>	%	25.0	31.1	31.2	32.0	30.5	29.7	23.4
<i>Narrow Money (M1)</i>	% Change	9.3	8.6	12.2	6.6	14.2	12.2	11.3
<i>Broad Money (M2)</i>	% Change	4.4	9.8	12.8	8.3	15.6	14.0	13.4
<i>Private sector credit as % of total outstanding credit of the banking sector</i>	%	65.7	67.4	70.1	70.3	75.5	76.9	78.4
<i>Total Export</i>	% Change	-15.6	6.4	8.0	8.9	2.6	0.9	-1.9
<i>Total imports</i>	% Change	-7.2	15.8	9.6	9.7	16.3	10.3	17.0
<i>Export/Import ratio</i>	%	43.7	40.2	39.6	39.3	34.7	31.7	26.6
<i>Tourism Income</i>	% Change	-26.1	35.7	54.5	-43.3	8.7	6	80
<i>Workers' Remittance</i>	% Change	0.7	14.0	8.1	11.9	49.0	2.5	35.0
<i>Current Account Balance</i>	In bln Rs	18.16	11.62	14.60	11.55	14.26	3.49	1.76
<i>Balance of Payments (+ surplus/-deficit)</i>	In bln Rs	-3.34	4.36	16.01	5.74	25.60	5.91	12.54
<i>Forex Reserve</i>	In bln Rs	105.90	108.23	130.21	129.90	165.03	165.13	182.01
<i>Exchange Rate<sup>4</sup></i>	US\$ =Rs	78.3	75.0	74.4	70.6	74.4	65.15	64.8
<i>Total Population</i>	In mln	23.7	24.2	24.7	25.3	25.9	26.4	27.0

1. Annual preliminary estimates (based on first 8 and 9 months data)
2. Base year 2000/01=100
3. Annual average (base year 1995/96 = 100)
4. Average of buying and selling rates at the end of mid-July each year, and for the current year, the average of buying and selling rates in mid-March

- 1.22 While classifying GDP into primary sector (agriculture and forestry, fisheries, and mining and quarrying), secondary sector (manufacturing, electricity, gas and water, and construction) and tertiary sector (rest of the service sector), the growth of the primary sector, secondary sector and tertiary sector is estimated at 5.64 percent, 1.78 percent and 6.9 percent respectively. In the previous year, the growth of these sectors was 0.98 percent, 4.02 percent and 4.16 percent respectively. The contribution of these sectors to the GDP is 33.09 percent, 15.46 percent and 51.44 percent in the current fiscal year compared to the ratios of 33.03 percent, 16.09 percent and 40.88 percent respectively in the last year.
- 1.23 In FY 2007/08, the GDP at current producers' price increased by 12.9 percent to Rs 820.81 billion. Last year, GDP at current producers' price had increased by 11.2 percent. Similarly, the GDP at current basic price increased by 13.8 percent to Rs 768.83 billion. Last year, it had increased by 10.5 percent.
- 1.24 The GDP per capita at constant price is estimated to have grown by 2.59 percent to Rs 20,816 in FY 2007/08. It had increased by 1.24 percent to Rs 20,289 last year.

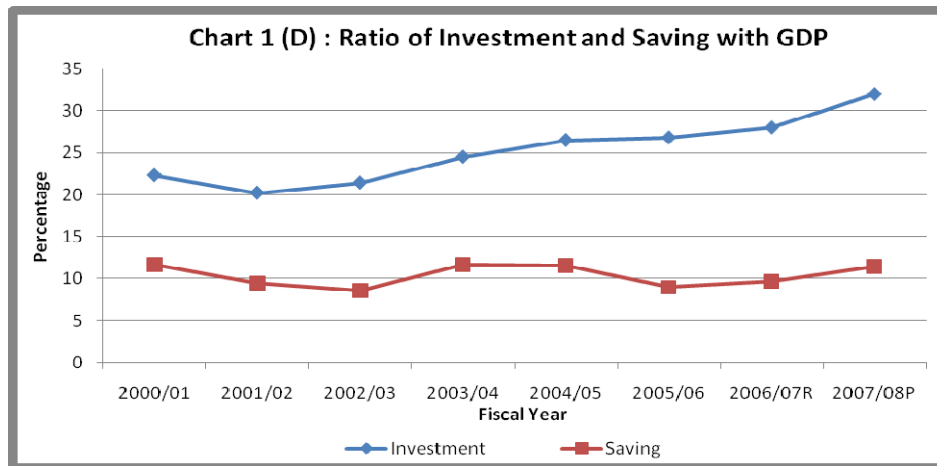


- 1.25 According to the Central Bureau of Statistics, GDP per capita at current price is estimated to increase by 10.42 percent to Rs 30,361. Last year, GDP per capita was Rs 27,497. In US Dollar terms, per capita GDP at current price is estimated at US\$ 470 compared to US\$ 390 a year ago.

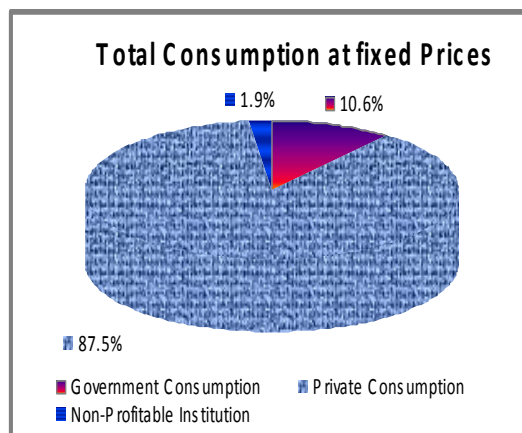
1.26 While analyzing the contribution of the major sectors, the share of agricultural remains 32.12 percent, wholesale and retail trade 13.60 percent, transport, storage and communication 9.3 percent, real estate, renting and business services 9.91 percent, industry 7.03 percent, construction 6.44 percent and education 5.99 percent.

### Consumption, Savings and Capital Formation

1.27 It is estimated that the ratio of consumption to GDP remains 88.53 percent in 2007/08 compared to 90.26 percent a year ago. Similarly, the ratio of gross domestic savings to GDP increased to 11.47 percent from 9.75 percent last year. This shows that the gross domestic savings has increased. The ratio of gross fixed capital formation and the ratio of gross capital formation to GDP are 21.05 percent and 32 percent respectively. Last year, these ratios were 20.41 percent and 28 percent respectively.



1.28 At constant price, the gross consumption increased by 2.7 percent to Rs 498.61 billion in 2007/08. Last year, the gross consumption had increased by the same rate to Rs 485.58 billion. The ratio of gross consumption to GDP at constant prices decreased to 89.7 percent in the



current fiscal year from 91.5 percent in the last year. Of the total consumption, the share of government consumption and private consumption is estimated 10.6 percent and 87.5 percent respectively. These shares were 10.4 percent and 87.6 percent respectively last year. The private sector consumption increased by 2.5 percent compared to 2 percent a year ago. However, the government consumption is estimated to grow by a lower rate of 4.5 percent compared to 7 percent last year.

- 1.29 The gross national disposable income at current price is estimated to have increased by 14.6 percent to Rs 989.38 billion in the current fiscal year compared to the growth of 10 percent to Rs 863.51 billion in 2006/07.
- 1.30 In the current fiscal year, the gross domestic savings at constant price is estimated to increase by 26.3 percent to Rs 57.23 billion. Last year, the gross domestic savings had increased by 9.1 percent to Rs 45.30 billion. The ratio of gross domestic savings to gross domestic product increased to 10.3 percent in 2007/08 from 8.5 percent in a year ago revealing a positive trend.
- 1.31 At constant price, the gross fixed capital formation is estimated to have grown by 6 percent to Rs 109.75 billion in 2007/08. Last year, the gross fixed capital formation had grown by 2 percent to Rs 103.51 billion. The ratio of gross fixed capital formation to GDP at producers' price is 19.7 percent in 2007/08, higher compared to the ratio of 19.5 percent a year ago. The ratio of government sector's fixed capital formation to GDP is estimated at 2.9 percent this year compared to the ratio of 2.7 percent a year ago. Similarly, such ratio of private sector is estimated at 16.82 percent compared to 16.75 percent a year ago.
- 1.32 The import of goods and services at constant price is estimated to have increased by 10.6 percent in FY 2007/08 compared to a decline of 5.4 percent a year ago. Contrary to the import expansion, the export of goods and services has been estimated to decline by 4 percent compared to the increase of 1.8 percent last year. Against this background of import expansion at a higher rate and contraction of export, the deficit of net export of goods and services increased by 24.7 percent to Rs 102.87 billion in 2007/08. Last year, such deficit was at Rs 82.52 billion. The ratio of export of goods and services to GDP at producers' price remained 14.4 percent in 2007/08 compared to 15 percent a year ago. However, the import as percent of GDP

would increase to 33.8 percent in the current fiscal year from 30.6 percent last year. The net export to GDP ratio is estimated to remain negative 19.4 percent in 2007/08 compared to negative 15.5 percent a year ago. Following the import expansion and export contraction, the export to import ratio would decline to 42.7 percent in FY 2007/08 from 49.1 percent a year ago.

## **Challenges**

- 1.33 Nepal could not attain higher economic growth despite the five decades of planned development efforts. Though the country attained annual average economic growth of 5 percent in the Eighth and Ninth Plan periods, the growth rate remained 3.4 percent in the Tenth Plan period (2002/2003-2006/07). Amongst the projected average annual growth rate of 6.2 percent at the higher side and 4.3 percent at the lower side, Nepal's average annual growth was less than the lower limit. Political instability and armed conflict adversely affected the development efforts and worsened the internal and external investment environment. While neighboring India and China could attract huge level of foreign direct investment in the past couple of years, foreign investors did not choose Nepal as their investment destination on the face of surrounding instability and uncertainty due to the conflict. Also, the level of domestic saving mobilization remained low resulting in a saving-investment gap at a whopping 20.5 percent in FY 2007/08. This reinforces the need for higher level of domestic saving mobilization for the sustained increase in investment. At the same time, it is important to recall that Nepal could hardly remain aloof from the main stream of globalization whatsoever the gravity of the problems surrounding the domestic realm. Nepal has no alternative of developing an investment friendly environment and tapping the advantage of globalization that has eased the transfer of capital, technology, and know-how. Only after this, the much-awaited economic transformation in the aftermath of the political regime shift is possible. The current challenge is to mobilize investment internally and externally by strengthening institutions. However, this requires guaranteeing rule of law, smoothening service delivery, and establishing a transparent and effective administrative mechanism.
- 1.34 Significant increase in the workers' remittances has contributed towards the goal of poverty reduction. However, the increasing income inequality catalyzes the need for equitable and justifiable

distribution of resources. Increasing inequality does not just mean that the access of the poor and general people to available resources is decreasing but that also signals the risk that increasing gap between the haves and the have-nots could further spike conflict in one or another form. Several countries around the world lacking equitable distribution of resources and having high-income disparity have been experiencing conflicts. In Nepal's case, income inequality is widening mainly due to unfair distribution of land, increasing urbanization, limited access of rural and suburban people to information technology, limited financial inclusion, high access of urban and rich people to high-valued urban houses, land and financial assets, increasing gap in access to quality education, and unjustifiable competition to accumulate wealth through any means. In view of these realities, inability to increase the access of the rural and poor people to the resources and to impose progressive tax effectively on financial and non-financial assets could further deteriorate the situation of income disparity.

- 1.35 Higher economic growth is a sine qua non for the economic development. Mobilizing higher investment in areas possessing comparative advantage such as hydropower, tourism, agro-processing industry, herbal industry, education, and health could help in attaining higher economic growth. The current challenge is to mobilize investment in these industries in order to bring people out of the vicious cycle of poverty, scarcity, and conflict and pave the way for sustainable economic development.
- 1.36 It is evident that agriculture is one of the sectors having high comparative advantage for Nepal. This sector alone contributes one-third to the GDP and provides income and employment opportunities to a broader section of the people. The fact that more than 80 percent of the people live in rural areas and that agriculture has been the primary source of livelihood for most of these people justifies that the role of agriculture in Nepal's development spectrum is immensely high. Also the current food crisis in the world has given a message that our agriculture needs to be modernized so as to make it self-sufficient. However, proper management of basic infrastructures such as irrigation, organic fertilizer, storage, seeds and agricultural transportation is lacking. Further, human resources professionally and technically competent need to be fostered while those having these attributes need to be utilized. Therefore, the challenge is to tap

the potentialities of agriculture for the economy through its rapid modernization and commercialization.

- 1.37 Nepal has now entered into federal republican state. In addition to paving the way for economic development through high and sustainable economic growth, there is an urgent need to take immediate and long run measures to expand economic activities in order to fulfill peoples' heightening aspirations. On one hand, there is a need to promote inclusion by caste, sex, language and region into the process of economic development and opportunities and, on the other, there is a need to give special emphasis on development of quality human resource by balancing possible issues raised by different groups and sectors. If the State mechanism has to concentrate on the issues raised by one particular group or region, it will not only affect the quality service but could also affect the process of creating an investment friendly environment. To attain higher and sustainable economic growth, there is a need for maintaining balance between the equitable participation of all groups and sectors and quality services through the state mechanism.
- 1.38 The tendency of using road and creating disturbances in movements just to pressurize for fulfilling all sorts of demand has increased the cost of economy, reduced competitive strength, and retarded the normal expansion of economic activities. Also, the waning harmony between laborers and industrialists has adversely affected the growth of industrial sector. Thus, the immediate challenge is to improve this situation prioritizing the agenda of economic development.