Government of Nepal
Ministry of Finance

Fiscal Policy Statement for Fiscal Year 2023/24

I. Introduction

1. Budget for fiscal year 2023/24 is directed towards achieving high, sustainable, broad based and inclusive economic growth by boosting the confidence of the private sector, reducing transaction costs and improving effectiveness of public expenditure. Creating employment opportunities along with the expansion of income generating activities for the marginalized people and communities has been accorded high priority. This budget aims to achieve prosperity, ensure effective governance and social justice for Nepali Citizen.
2. The government has maintained a prudent financing strategy to support economic growth by maintaining macroeconomic stability as well as fiscal and debt sustainability. The government will continue efforts to improve public investment management, budget execution, domestic resource mobilization and adopt a prudent mix of domestic and concessional external borrowings to reduce financing costs.
3. The macroeconomic framework and fiscal policy statement for FY2023/24 is based on the policies set on the Fifteenth Plan and Medium-Term Expenditure Framework (MTEF) for FY2023/24-FY2025/26. The MTEF incorporates medium-term fiscal framework (MTFF), medium-term result framework (MTRF), and medium-term budgetary framework (MTBF). It includes current state of the economy and projections of fiscal parameters for the next three years. MTRF includes information of indicators and performance against current targets, and projections for the next three-year's results based on the government's projects and programs. MTBF includes budget and projections of sectoral allocation for the next three years, and information of major projects and programs. The targets outlined in the MTEF and the Fifteenth Plan serve as a basis for determining resource envelope for a sustainable fiscal path over the medium-term.

4. The objectives of FY2023/24 budget are: (i) to achieve broad-based, sustainable and inclusive economic growth to make economy vibrant; (ii) to ensure quality social development, social security, and social justice; (iii) to boost up private sector confidence by promoting investment-friendly environment and reduce poverty through the creation of income generating opportunities and gainful employment; (iv) to maintain macro-economic stability; (v) to strengthen federalism and good governance; and (vi) to enhance effectiveness of public expenditure through budgetary reforms.

5. Accordingly, the priorities of FY2023/24 budget are: (i) development of agriculture, energy and tourism sectors; (ii) investment promotion, industrial development, and improving trade balance; (iii) social sector development and social security; (iv) quality infrastructure development; (v) promotion of digital and green economy; (vi) environment protection, climate change and disaster management; (vii) human resource development and employment generation; (viii) financial sector development; (ix) strengthening fiscal federalism and service delivery; and (x) improvement in fiscal system.

II. Macroeconomic Framework and Fiscal Policy Statement

6. **Macroeconomic framework**. It is estimated that the economy will grow by 2.2 percent in FY2022/23, down from the revised estimate of 5.3 percent in FY 2021/22, owing mainly to a contraction in manufacturing industry, construction sector, and retail and wholesale trade. These sectors together contribute to about 28 percent of GDP. Adoption of some tight monetary policies in FY2022/23 helped maintain external sector balance in the current fiscal year. However, it resulted in a significant fall in merchandise imports. Fall in merchandise imports caused a decline in the revenue. Further, it weakened aggregate demand. While public investment contracted by 13.5 percent and private investment marginally increased by 0.1 percent, final consumption expenditure has increased by 8.3 percent. Lower than expected capital spending and recurrent spending rationalization, partly due to lower revenue mobilization, also affected economic activities and banking sector liquidity.

Consumer price inflation averaged 7.9 percent in the first nine months of this fiscal year.

7. Credit flow to private sector has grown at a slower pace during the first 10 months of FY2022/23 compared to the corresponding period of the previous fiscal year. In the month of May 2023, the weighted average interest rate of 91-days treasury bill remains at 9.7 percent, while inter-bank rate remains at 7 percent, deposit rate 8.3 percent and lending rate 12.8 percent. The high interest rates are attributed to the increase in cost of borrowing and fall in demand for credit by private sector.

8. Meanwhile, during the first 10 months of FY2022/23, trade deficit has decreased by 15.9 percent compared to an increase of 24.9 percent in the corresponding period of the previous fiscal year. During the period, remittance inflows increased by 23.4 percent partly due to the sharp increase in the number of out-migrants. Likewise, tourism sector is gaining momentum mainly after the setback of Covid-19 and therefore, travel receipt has significantly increased by 93.8 percent. Consequently, the current account deficit dropped to Rs.54.7 billion compared to a deficit of Rs.545.1 billion in the same period of the previous fiscal year. During this period, the balance of payments has remained at a surplus of Rs.214.7 billion and foreign exchange reserve is sufficient to finance the import of goods and services equivalent to 9.7 months. The external and overall debt are assessed at low risk of debt distress.

9. **Fiscal stance.** Against the backdrop of a slowdown in economic activities, there is greater need to increase investment in infrastructures to meet the infrastructure need and generate decent jobs simultaneously. The government will pursue a prudent fiscal policy for the rationalization of expenditure and increase the domestic revenue mobilization. Likewise, recurrent spending will be rationalized and the capital spending will be made effective with a robust implementation plan to boost absorptive capacity. The government will adopt a financing strategy to lower the cost of borrowing. Gross external borrowing is targeted to NRs 212.8 billion in FY 2023/24 lower than the estimated target of NRs 242.3 billion in FY2022/23. Similarly, gross domestic borrowing is targeted to NRs 240.0 billion in FY

2023/24 lower than the estimated target NRs. 256.0 billion in FY2022/23.

10. In line with the fiscal policy stance to support medium-term economic growth, FY2023/24 budget outlines the following:

    - Real GDP growth of 6 percent
    - Consumer price inflation to be contained within 6.5 percent
    - Expenditure outlay of NRs 1751.3 billion
    - Federal receipts of NRs 1298.6 billion
    - Recurrent expenditure to be covered by domestic revenue
    - Gross domestic borrowings to be contained below 5 percent of GDP

11. **Expenditure:** The expenditure outlay of Government of Nepal for FY2023/24 is 2.4 percent lower than the estimated target for FY2022/23 and 16.4 percent higher than the revised estimate for FY2022/23. It includes 65.2 percent for recurrent spending including fiscal transfers, 17.3 percent for capital spending and 17.5 percent for financial provision. The allocations for recurrent and capital budgets in FY2023/24 are lower than 3.5 percent and 20.6 percent respectively as compared to the estimated target of FY2022/23. It is 9.4 percent and 17.2 percent higher than the revised estimate of FY2022/23 respectively, making the FY2023/24 fiscal policy growth enhancing with an emphasis on higher spending on capital projects. Reduction in the size of budget is primarily focused on achieving fiscal discipline. Allocations for interest payments and social security in FY2023/24 have increased by 94.6 percent and 2.3 percent respectively compared to the estimated target of FY2022/23. It is higher than 71 percent and 26.4 percent respectively compared to the revised estimates for FY2022/23. These two together account for 20.8 percent of the recurrent budget.

    One of the challenges Nepal is facing is the substantial increase in recurrent expenses. It includes salary and allowances, social security expenses, fiscal transfers, administrative expenses and increasing liabilities on debt servicing. It consists of NRs.1280.25 billion which is 73.10 percent of the budget for FY2023/24. It has created pressure for resource management of capital investment. Estimated budget for fiscal transfer is NRs.400 billion. The focus of the fiscal policy in the medium-term is to achieve allocative efficiency by making expenditure more targeted and rationalized.

12. **Revenue mobilization.** With the gradual improvement in overall economic scenario of the country in the recent months, revenue mobilization in FY 2023/24 is expected to increase. The target of domestic revenue mobilization in the budget for FY2023/24 is NRs.1298.6 billion and that of foreign grants is NRs 49.9 billion. Overall, total federal receipts (revenue and grants) are targeted to increase by 0.2 percent in FY 2023/24 over the estimated target of FY2022/23. Domestic revenue is estimated to be sufficient for financing the recurrent spending including the inter-governmental fiscal transfers. The government's initiatives to increase the use of digital technology in revenue administration, control revenue leakages, broaden tax base and update tax rates for certain goods will be instrumental to achieve the targeted revenue in the budget of FY 2023/24. Likewise, government's policy of providing incentives for needy sectors will be helpful to boost national output and economic recovery.

13. **Fiscal and debt sustainability**. Government has been maintaining fiscal balance at a sustainable level. Fiscal deficit is projected to decline in FY 2023/24 resulting from the estimation of improved performance in revenue mobilization and various policy measures adopted by the budget of FY 2023/24 for rationalization of recurrent expenses. Overall government borrowing will be maintained within the ceiling prescribed by National Natural Resources and Fiscal Commission (NNRFC). The target of issuing domestic borrowing is below 5.0 percent of estimated GDP of FY 2023/24 and recurrent spending has been allocated within the coverage of domestic revenue. External and overall debt are assessed at low risk of debt distress by the IMF. Public debt of the government as of mid-May 2023 stands at NRs 2134.32 billion, which is equivalent to 39.6 percent of GDP and estimated to be around 42 percent of GDP by the end of FY 2022/23. Of the total outstanding public debt, internal and external debts are 50.3 percent and 49.7 percent respectively.

    Government initiation of adopting the policy measures of right mix of domestic and external borrowing will be helpful to lower the cost of financing. To generate long-term financing for infrastructure projects, the government will emphasize on increasing issuance of longer-term bonds.

Ministry of Finance has started publishing Fiscal Policy Statement from FY 2022/23 as a part of the budget reports. This statement will be updated annually by exploring fiscal stance based on adjusted primary balance that measures the fiscal position net of the impact of macroeconomic developments on the budget. Such an update will be continued in the future days.

14. **Economic and Budgetary System Reform:** The main thrust of the Budget of FY 2023/24 is to provide impetus for reforms in economic and budgetary system. Strengthening competitive environment, building productive capacity, increasing efficiency of the economy and promoting private sector are going to be the major activities under economic reforms. Furthermore, government's ability to mobilize fund and improve implementation of development projects will be achieved by amending existing laws and simplifying procedures.

    On fiscal side, this budget has taken four major initiatives. They are: reform in budgetary system and effectiveness of capital expenditure, austerity in recurrent expenses, expansion of tax base and reduction of fiscal deficit. For budgetary system reforms, the principles and priorities of the appropriation bill will be submitted to the parliament two and a half months before the submission of the next fiscal year's budget. It will provide sufficient time for the parliamentarians to discuss and review the principles and priorities of the budget for the next fiscal year.

    Similarly, effectiveness of the capital expenditure will be enhanced through allocation of resources in those priority projects which have strategic importance, produce quick return and benefit to the large segment of the people. Resource will be allocated to the priority sectors. The tendency of sprinkling money for numerous tiny projects will be discouraged through prioritization of the projects and allocative efficiency. Enhancing project appraisal, preparing action plan for budget implementation before the budget is enacted and taking special measures for monitoring of the programs, solving problems of site clearance of projects, simplifying procedures of acquisition of land, amending public procurement law to simplify the process, improving the process of multiyear assurance of resources etc. are some of the important measures proposed for improving implementation of the capital budget.

Government is also focused on the rationalization of recurrent expenses. Twenty redundant government structures will be removed. Standards will be set for reducing administrative costs.

Tax system will be enhanced through broadening and protecting tax base, improving utilization of ICT, simplifying administrative processes, while enacting policy and legal reforms to make the tax system investment friendly. Special measures will be taken to reduce tax evasion by enhancing institutional capacity and integration of customs administration, inland revenue and other systems. Exemption of 170 items in VAT and 340 items for excise duties have been removed.