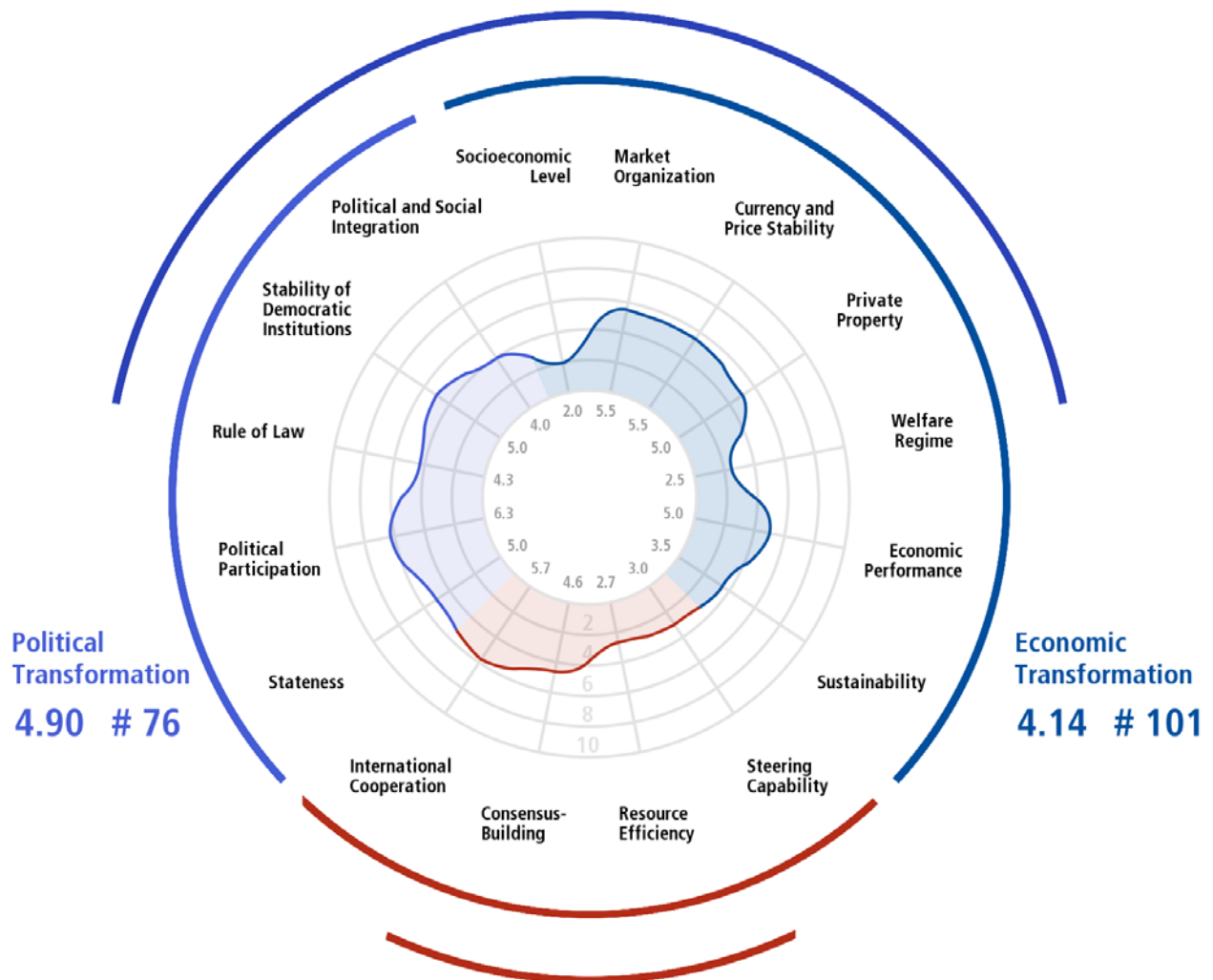


Nepal

Status Index

4.52 # 92

on 1-10 scale out of 129



Political Transformation
4.90 # 76

Economic Transformation
4.14 # 101

Governance Index

3.74 # 99

on 1-10 scale out of 129

This report is part of the Bertelsmann Stiftung's Transformation Index (BTI) 2018. It covers the period from February 1, 2015 to January 31, 2017. The BTI assesses the transformation toward democracy and a market economy as well as the quality of political management in 129 countries. More on the BTI at <http://www.bti-project.org>.

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Key Indicators

Population	M	29.0	HDI	0.558	GDP p.c., PPP \$	2468
Pop. growth ¹	% p.a.	1.1	HDI rank of 188	144	Gini Index	32.8
Life expectancy	years	69.9	UN Education Index	0.520	Poverty ³	% 50.9
Urban population	%	19.0	Gender inequality ²	0.497	Aid per capita \$	42.4

Sources (as of October 2017): The World Bank, World Development Indicators 2017 | UNDP, Human Development Report 2016. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$3.20 a day at 2011 international prices.

Executive Summary

In the last two years, Nepal has been hit by a 7.8 magnitude earthquake in April 2015 and a 7.3 magnitude aftershock in May 2015, which have killed over 9,000 people, injured over 22,000, and made homeless hundreds of thousand Nepalis. The World Bank has priced the damage at \$7 billion, with total reconstruction needs at \$6.7 billion.

On the political front, after the 2015 earthquakes, Nepal's political leaders vowed to "fast-track" the drafting of a new draft constitution and finally complete the peace process that had started in 2006. On June 8, the main four parties (Nepali Congress, UML, Maoists, and Madhesi Forum-L) reached a political settlement known as the 16 Point Agreement, which was to form the basis of the new constitution. Significantly, the negotiations included only four of the 31 parties represented in the Assembly and made little effort to include representation from the marginalized groups. The Agreement featured a parliamentary form of government with a mixed electoral system and a separate Constitutional Court but crucially sought to postpone the naming and demarcation of the federal units until the promulgation of the new constitution and the elections of the central and provincial legislatures. Despite these developments law and governance in the country remains very weak.

The postponement of the long-awaited process of federal restructuring immediately sparked protests across the country. As a result, petitions were filed in the Supreme Court to have the Agreement declared in violation of the 2007 interim constitution. In an unprecedented move, on June 19, a single bench of the Supreme Court issued an interim order against the implementation of the Agreement's postponement of federal restructuring. The apex Court arrived at its decision on the basis of Article 138(3) of the interim constitution, which mandates that "the final decision relating to the structure of the state and federal system shall be made by the Constituent Assembly." Politicians accused the Court of overreaching, and the Assembly's Constitution Drafting Committee (CDC) pressed on with the preparation of the draft on the basis of the 16 Point Agreement defying the Supreme Court's order. Protests grew increasingly violent, and the security

forces' response was heavy-handed, especially in the Terai, where the demands for federalism and equal citizenship have been historically the strongest. In the meantime, the Assembly opted for a fast-track procedure to pass the new constitution, allowing for a very brief period of public consultation over the draft. Amidst mounting tensions, on August 8, the political leaders relented and inked a six-province deal of federalism. As protests further intensified, on August 21 the Nepali Congress, UML, and Maoists agreed on a new seven-province federal deal (essentially carving Province 7 out of Province 6 and maintaining the controversial longitudinal division of the country), while the Madhesi Forum-L did not support the scheme.

On August 23, the draft constitution (with the seven-province model) was tabled in the Assembly for approval by the House as the members of parliament representing the marginalized groups walked out in protest. Violent demonstrations and communal violence erupted across the Terai, leading to the death of security forces and protesters in Kailali, the imposition of a curfew, and the deployment of the Nepal Army. This volatile situation was in turn exacerbated by an unofficial Indian trade blockade that lasted until February 2016 causing significant shortages of fuel, medicines and other goods of primary necessity in earthquake-struck Nepal. The World Bank has estimated that the combination of the earthquakes and the trade disruptions pushed down the country's overall growth in FY 2016 to 0.6% (at market prices) – the lowest in 14 years. Reflecting both the earthquake and trade-related disruptions, inflation spiked to over 12% (y/y) by mid-January rising five percentage points in just four months from mid-September 2015. This was the highest inflation level since FY 2009. As the trade disruptions ended, inflation eased back to single digits. In October 2016, the World Bank's Nepal Development Update predicted that growth in FY 2017 is forecasted to accelerate to 5% and expected to moderate in line with the country's potential during FY 2018.

While the new constitution was eventually framed, it did not bring about radical institutional restructuring, and in many respects, it was a step back from the previous 2007 interim constitution. The new constitution was ultimately promulgated on September 20, 2015, but it features controversial provisions on unequal citizenship discriminating on the basis of gender, a ban on religious conversion, limited notion of secularism, a weakening of the judiciary, an embattled demarcation of the federal units, a decrease in seats allocated through proportional representation and the inclusion of the category Khas-Arya (i.e., the historically dominant upper-caste Hindus, i.e., Bahun and Chetri) in the list of groups entitled to quotas.

In October 2015, Prime Minister Koirala (of the Nepali Congress party) resigned from office, and UML leader K.P. Oli was elected to succeed him on a nationalist conservative platform that further polarized and fragmented the Nepali polity. In August 2016, Prime Minister Oli lost a no-confidence vote and was succeeded by the Maoist leader Pushpa Kamal Dahal. By January 2016, the new constitutional dispensation had already been amended once, and in November a second amendment was registered but has not yet been passed. However, the amendments have failed to quell protests against the new constitutional settlement, and a new phase of political instability and further polarization along identity lines has begun in Nepal. Lack of consensus among political parties has significantly slowed Nepal's development, making poverty alleviation a major development challenge.

History and Characteristics of Transformation

Nepal's contemporary political history has been shaped by recurring episodes of mass mobilization and anti-regime contention. Until 1990, Nepal's political system was that of an authoritarian monarchy based on an exclusive and oligarchic social order. However, a pro-democratic people's movement brought down the royalist Panchayat system and transformed Nepal into a constitutional Hindu monarchy and a multiparty democracy in 1990.

However, this transition did not establish a stable, well-functioning and consolidated liberal democracy. Rather, Nepal experienced a series of weak governments with ineffective governance, and the emerging democratic regime remained highly defective. As a consequence, in the late 1990s, a Maoist rebellion erupted that affected almost all 75 districts of the country. The insurgent movement found support, especially among the impoverished and largely disadvantaged masses of the rural population, but internal armed conflict contributed to a further decline of democracy and human rights in the country. Moreover, in 2001, King Birendra and the entire royal family were murdered under mysterious circumstances, and the dead king's brother, Gyanendra, was crowned king on June 4, 2001.

Disappointed by the lack of success in combating the insurgents, King Gyanendra staged a royal coup in 2004/05, claiming full sovereignty and assuming executive authority. The restoration of royal authoritarianism led to the emergence of a broad opposition movement consisting of the Seven Party Alliance (SPA) and the Maoist insurgents. Finally, broad-based anti-regime contention orchestrated by the main opposition parties and civil society groups in April 2006 forced King Gyanendra to reinstate the dissolved parliament.

The newly formed multiparty government concluded a comprehensive peace agreement with the Maoists that opened the way for the new interim constitution, which came into force in January 2007. On the same day, an interim parliament including Maoist representatives was formed, and, in April that year, the Maoists also joined the government. It took another year before popular elections to a Constituent Assembly (CA), in April 2008, in which the CPN-Maoist finished as the strongest party. In May 2008, at the CA first meeting, the monarchy was abolished, and the interim constitution was amended to institutionalize Nepal as a Federal Democratic Republic of Nepal.

However, the years that followed these elections were disappointing in many respects, as the old power struggles between political leaders started once again. It was only in early 2009 that the CA could start its work on the new constitution. Even though the 2007 interim constitution established a secular, federal and republican state, deeply entrenched differences about the ideal form of the future state impeded agreement between party leaders, which in turn inhibited the CA's ability to reach consensus on key constitutional articles.

After four extensions of its initial two-year tenure, the CA was dissolved without promulgating a new constitution, in May 2012. Rather, both the coalition government under Prime Minister

Baburam Bhattarai (August 2011 – March 2013) of the Unified Communist Party of Nepal (Maoist), and the nonpartisan government of Acting Prime Minister Khil Raj Regmi (chief justice of Nepal since May 2011) that governed the country from March 2013 to February 2014, proved unable to break the constitutional deadlock.

In November 2013, however, the caretaker at least succeeded in holding new elections for the CA. These elections saw an impressive comeback of the Nepali Congress (the main opposition party under the Panchayat system and the ruling party for most of the period 1990 – 2006). After the CA assembled in January 2014, a multiparty coalition was formed under the leadership of Prime Minister Sushil Koirala (Nepali Congress) in February 2014.

The new CA featured many delays and made little progress on the constitution drafting front. In April and May 2015, two devastating earthquakes hit Nepal, causing great human loss and economic destruction. The natural disasters, however, acted as catalysts for constitution making and Nepal's political leaders fast-tracked the drafting. Amidst much controversy, violent protests in the Terai, and an unofficial Indian blockade the new controversial constitution was eventually promulgated on September 20, 2015. The document backtracked from many of the achievements of the interim constitution with regard to social inclusion. In October UML leader K.P. Oli became the new prime minister and his ultra nationalist stance further polarized Nepali society along identity lines. In August 2016, Maoist leader Dahal succeeding Oli at the helm of the Nepali government but the situation in the country remains unstable, and the polity divided.

The BTI combines text analysis and numerical assessments. The score for each question is provided below its respective title. The scale ranges from 1 (worst) to 10 (best).

Transformation Status

I. Political Transformation

1 | Stateness

Ever since the creation of the modern Nepal in the late 18th century, Stateness has been linked with the religion, language and culture of the so-called upper Hindu castes (Tagadhari), especially the Brahmans (Bahun), who dominate politics, the judiciary, the media, the civil service and all other spheres of public life. This changed little after the downfall of the Panchayat system in 1990. Moreover, public life and law and order were eroded by the Maoist insurgency as well as the counterinsurgency efforts of the Royal Nepali Army.

After several years of a multidimensional crisis of Stateness, driven by a Maoist rebellion and a royal putsch, the peace process since 2006, albeit slow and fragile, has helped to strengthen the state's monopoly on the use of force in many parts of the country. Furthermore, the 2006 Comprehensive Peace Agreement and subsequent tenures of the Constituent Assembly (CA), from 2008 to 2012 and again since 2013, provided a platform for wide-ranging public debate over both the real and ideal nature of Nepali Stateness.

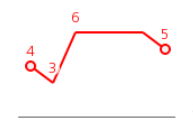
Although the legitimacy of the state's overall sovereignty or territorial claims within its international borders is uncontested in principle, the very nature of the state's internal power structures – both geographical and political – has been up for debate in the post-conflict period. These problems have been exacerbated by the extremely close relationship between Nepal's civilian government and the armed forces, which has only increased since the Maoists took power and a significant number of their ex-combatants were integrated into the Nepal Army (NA) from 2012 to 2014. Rather than enabling legitimate democratic control over the country as a whole, the politics of impunity and militant ethnic and regional movements have now become the main threat to the state's monopoly on force especially since the intensification of protests over the new 2015 constitution and the unofficial Indian blockade.

Question
Score

Monopoly on the
use of force

5

'06 '18 10



Finally, concerns have arisen over the activities of Indian border security forces in uniform acting beyond their jurisdiction. Additionally, along the northern border with China's Tibetan Autonomous Region, Chinese border troops have allegedly overstepped their jurisdiction by occasionally entering Nepali territory.

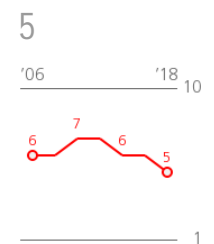
The promulgation of the new 2015 constitution marked a step back from the more inclusive 2007 interim constitutional settlement and to a degree a return to exclusionary ethno-cultural nationalist narratives. The new dispensation features a notion of secularism explained as “special protection for sanatana (Hinduism),” reiterates the long-standing ban on conversion, features discriminatory citizenship provisions on the basis of gender, introduces the new category Khas-Arya in the quota system, and reduces the quota of parliamentary seats elected under proportional representation. The new constitution was expected to “build a new Nepal” and bring about a more inclusive political settlement through radical state restructuring, but the new dispensation fell way short of these aspirations.

As a result, people of Indian ancestry living in the Terai (Madhesi), members of numerous ethnic groups (Janajati), women, and the so-called untouchable castes (Dalit) continue to face manifold legal, economic, and social discrimination from high-caste Hindus (often referred to as “hill elites” because they live in the central hill region) who still dominate the bureaucracy, political institutions, the cultural system and the economy.

Many public officials maintain strongly held, more or less private beliefs that Nepali citizenship should be defined by competence in the Nepali language and adherence to Hindu religion. Such attitudes have been strongly contested for decades by politically active members of the Madhesi (inhabitants of the Madhesh, or Terai, region) and Adivasi Janajati (indigenous nationalities) movements, who demand a reformulation of the nation-state's symbolic rhetoric and its concomitant citizenship policies. Since 2007, these identity-based movements have made significant gains in broadening notions of the nation-state and the basis for citizenship. However, since 2010, they have faced increasing resistance from counter-movements that deploy similar identity-based rhetoric to “protect” the privileged citizenship status of erstwhile dominant groups. This second view ended up prevailing at the time of the promulgation of the controversial 2015 constitution. The standoff between these two views of the nation-state contributed significantly to the delays in the CA process and ultimately to frame a document that could, on the one hand, recognize as legitimate the demands of marginalized groups, and, on the other, ensure equality and justice for all citizens. Therefore, the existing citizenship agreement remains embattled and unstable.

The 2015 constitution defines the Nepali state as secular but includes an explanation by which “secular means the protection of sanatana” (a Sanskrit expression that denotes Hinduism). The document also reiterates a ban on religious conversion, which has been in place since 1959. The Country Code (Muluki Ain), which

State identity



No interference of religious dogmas

6

represents the backbone of Nepali civil and criminal law, still retains numerous provisions more or less directly influenced by a certain reading of Hindu scriptures. While more progressive political forces and activist lawyers have sought to reform the legal system, the changes remain piecemeal and incomplete.

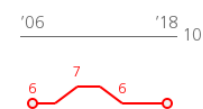
The administrative system is moribund, riddled with corruption and urgently in need of reform. As in most South Asian countries, various indicators, such as the ability of the state to tax the economy, indicate a weak state capacity in Nepal. While the administrative structure of the state extends beyond maintaining law and order, the country's weak administration is unable to provide equitable access for all citizens to administrative services. Especially in rural areas, the infrastructure is too weak to provide a sound administrative basis for political, social and economic development. In urban areas as well, electricity and water are rationed by municipal providers. Citizens seeking to avail themselves of basic state services such as birth and death registration, health care and education – let alone legal redress – encounter labyrinthine procedures over which individual incumbents often have undue discretionary influence. Decision-making is often highly centralized, both geographically (i.e., petitioners from all over the country often must come to Kathmandu to attain their objective) and individually (lower-level functionaries are often unwilling to take responsibility for decisions, so power is concentrated at the top levels).

A general restructuring of the civil administration has been under discussion for years. With the promulgation of the new constitution in September 2015, consultations have been under way to adapt Nepal's administration to the country's new federal structure. However, no significant changes have yet occurred.

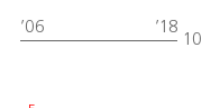
2 | Political Participation

In November 2013, general elections for a new CA took place. These multiparty elections were conducted more or less properly. But, as the election was boycotted by an alliance of more than 30 fringe parties, led by the Communist Party of Nepal-Maoist (CPN-M), it was a manifestly disputed means of filling political posts.

To counter threats by boycotting parties to disturb the poll, the caretaker government deployed more than 140,000 security personnel in all 75 districts of the country. There had been incidents of election violence ahead of the poll. The CPN-M enforced a strike in three western districts and banned other parties from campaigning in Bardiya district, and party cadres engaged in numerous low-intensity clashes. But, in the end, the CPN-M refrained from using violence or obstructing the vote, and turnout was close to 70%. Initially, the United Communist Party of Nepal-Maoist (UCPN-M) rejected the outcome of the election, alleging fraud. Eventually, the party agreed



Basic administration
4



Free and fair elections

7



to remain in the CA and participated in the formation of a coalition government led by the Nepali Congress party.

Numerous national and international observation teams reported that the 2013 elections were free and fair, although cases of intimidation and booth capture were reported. The Sidney-based Electoral Integrity Project, in its 2013 report, evaluated the quality of the electoral laws and procedures as well as the vote count and the neutrality of electoral authorities relatively high, but aspects such as fraudulent voter registration, unregulated campaign finances and irregularities during the voting process were seen as especially problematic. In contrast, candidate registration, media coverage and the drawing of district boundaries were seen as minor (but relevant) problems.

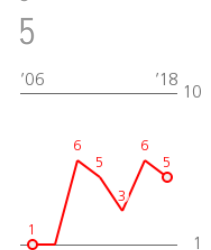
At the moment, Nepal's political parties are negotiating whether to hold local elections, which have not taken place since 1997.

The new 2015 constitution has reduced the percentage of seats selected under proportional representation in the directly elected Lower House (60% of the seats elected under first past the post and 40% under proportional representation) from the arrangements under the previous 2007 interim constitution (42% of the seats elected under first past the post and 58% under proportional representation), thus making the Lower House less inclusive than before. This has been the cause of major grievances from Janajati, Madhesi and other marginalized groups.

Since the November 2013 elections of the second CA and the promulgation of the new constitution in 2015, democratically elected political representatives have had the power to govern, which is, however, significantly constrained in various ways. First, various political parties, including those that boycotted the election and are therefore not represented in the CA, exercise veto power. Secondly, although the Nepalese Armed Forces (NAF) are traditionally under government control, day-to-day monitoring is weak. Third, the CPN-M has had problems in replacing its militant outlook with adherence to democratic norms. On the one hand, the political parties that decided to boycott the 2013 election could be seen as “veto groups.” But on the other hand, integrating these groups into the constitutional process in one way or another and giving them the opportunity to veto the political process seems mandatory in order to achieve sustainable peace-building.

On a positive note, the urgent task of integrating the former People's Liberation Army (PLA) into the Nepalese Army (NA) has seen some progress in the post-2006 period and especially between 2010 and 2014. By 2015, 1,420 former Maoist combatants were integrated into the Nepal Army, hailing the Nepali example as one of the few successful instances worldwide of post-conflict army integration. Furthermore, despite allusions to the possibility of a military coup in recent years, the army top brass has not raised explicit objections to government policies. It is widely assumed that India has strongly discouraged any army involvement in politics at this stage.

Effective power to govern



Other potential veto groups, such as landowners and business elites, enjoy sufficient access to political parties, the CA and the cabinet and hence can try to influence policy-making through institutionalized politics. Therefore, they do not count as “veto groups” as defined in the BTI.

Finally, there are veto actors at the local levels (landowners, traditional elites, groups or individuals with control over means of violence and coercion). However, since the political system is still highly centralized, these actors do not exercise a veto over local democratic decision-making; what they can do, however, is to block the implementation of policies at the local level.

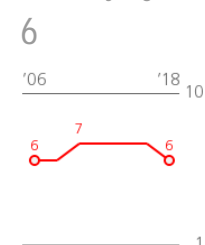
Freedom of association and assembly is guaranteed under Article 17 of the new constitution promulgated in September 2015. The constitution allows for “reasonable restrictions” to be imposed by ordinary laws in an extensive range of circumstances. During the protests in the Terai, from August 2015 to February 2016, the government issued curfew orders and declared “prohibited zones.” Nevertheless, individuals in Nepal are free to join political and civic groups, and many people possess multiple affiliations. For the most part, such groups operate freely, and mass rallies and programs are common, both in urban centers and far-flung district headquarters.

Most exceptions have involved the Tibetan community, members of which have repeatedly been detained and arrested for staging protests and holding cultural festivals that invoke the Dalai Lama. This differential treatment is largely due to Chinese pressure on Nepal, which, in violation of both international law as well as its own interim constitution, often does not view the rights of Tibetan refugees as equivalent to those of its own citizens.

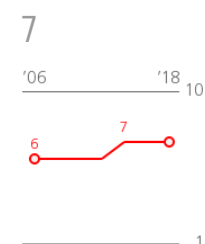
Freedom of opinion and expression is guaranteed under Article 17 of the new constitution promulgated in September 2015. The constitution allows for “reasonable restrictions” to be imposed by ordinary laws in an extensive range of circumstances. Under Prime Minister Oli’s tenure, there have been a few high-profile incidents in which freedom of expression has been curbed: the arrest on sedition charges of Madhesi activist C.K. Raut and the deportation of Canadian citizen Robert Penner both on the grounds that their speech was disturbing Nepal’s social harmony and threatening national unity.

Notwithstanding these incidents, Nepal has a vibrant media, with scores of print dailies, weeklies and monthlies in the national language of Nepali, as well as English and several ethnic and regional languages. Community radio has also expanded rapidly as an important source of news and information for people around the country, especially in rural areas. Growing electric grids, complemented by satellite and mobile technology, have also fostered a diverse and contentious public sphere in which many different voices are increasingly heard at both local and national levels. The 2016 Reporters Without Borders Press Freedom Index ranked Nepal at 105th out

Association /
assembly rights



Freedom of
expression



of 180 countries, a marked improvement from previous years (2014: 120th out of 180).

3 | Rule of Law

Article 56 of Nepal's 2015 constitution expressly protects the separation of powers. Compliance with the principle can be seen at the level of institutional design, from the creation of three separate branches of government to the extensive mechanisms of checks and balances. However, the new constitutional settlement weakens the position of the judiciary compared to the previous interim constitutions (e.g., the ease with which the impeachment proceedings of Supreme Court justices can be initiated and the creation of a separate constitutional bench within the Supreme Court). In terms of constitutional practice, the executive continues to overreach and often does not comply with court rulings.

Nepal's 2015 constitution establishes an independent three-tier judicial system consisting of the Supreme Court, a High Court for each Federal Province and a District Court for each District.

The Supreme Court is the highest court of the country, which hears appeals from the lower courts. The new constitution has now created a Constitutional Bench within the Supreme Court, which is the only body empowered to review legislation. However, the Bench has not yet been established adding to the Court's enormous backlog. The apex Court is also weakened by the new impeachment procedure, which has a lower threshold.

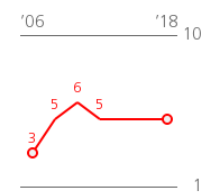
The independence of the judiciary is supposed to be ensured by law. The constitution created the Judicial Council as an exclusive authority for dealing with some of the most important issues relating to an independent judiciary.

The Supreme Court exercised considerable power by impeaching several political leaders on corruption charges and taking courageous decisions on transitional justice, citizenship, quotas, etc. The court system suffers from functional deficits and remains inaccessible to the majority of the Nepalese people due to insufficient geographical dispersal and scarce resources, both within the system and among those seeking juridical protection of their rights.

Additionally, the judicial system suffers from a number of other problems, including a lack of citizen awareness for the judicial process and delays in the system. According to assessments by the Nepal Bar Association, corruption is deeply rooted in the court system, especially at the District level. A large number of pending cases; undue delays in the implementation of court decisions; and controversial appointments of judges, resulting from a lack of transparency and from political

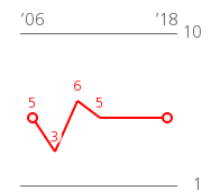
Separation of powers

5



Independent judiciary

5



interferences in the appointment process, together contribute to an overall impression of a judiciary that is highly impaired by political interference and corruption.

A lack of effective legal consequences has been and still is a serious obstacle in ensuring the rule of law and protection of human rights. The inclusion of extensive provisions in the new 2015 constitution allows the President unrestricted authority to grant pardons and enables the political elite to sweep past misdeeds under the carpet.

Feeding into a broader culture of impunity is Nepal's failure to effectively prosecute any crimes committed by the security forces during the civil war and in the years since 2006. So far, neither the crimes of the Maoists or the security forces, nor the political responsibility for these crimes by the different governments, have to date been the subject of investigation. Only the universal prosecution for torture of Colonel Kumar Lama took place in the UK but resulted with the accused being cleared of all charges in 2016.

Corruption in Nepal is entrenched in politics and business. Funds, including aid money, are routinely stolen at all levels of government, and corruption scandals frequently make the news. Political parties continuously dispense patronage to members and supporters, both in terms of material resources and administrative favors. The business sector is well adapted; companies long ago learned to work through the system, and some indeed profit from it. The result is a self-perpetuating system: endemic corruption results in weak rule of law, which in turn renders corruption a matter both of necessity and convenience for parties, civil servants, citizens and businesses.

The nation's anti-graft body, the Commission for the Investigation of Abuse of Authority (CIAA), occasionally arrests high-level government officials on corruption charges. In recent years, prominent politicians were convicted on corruption charges and jailed, including high ranking politicians. Overall, however, corrupt officeholders or authorities who abuse their office can do so without fearing legal consequences. This is especially the case with local officials, whereas, at the national level, there are at least frequent reports in the media, which trigger adverse publicity. The commission was severely weakened in its standing by the impeachment of its Chairman Lokman Singh Karki.

In principle, the new 2015 constitution provides full protection for civil and political rights and an impressive catalog of economic, social and cultural rights. In reality, it is an issue of constitutional implementation, and many of these rights remain dead letters due to the lack of accountability and good governance. The protests around the new constitution in the Terai led to over 50 casualties and many injuries among both protesters and security forces. As such, the law-and-order situation remains difficult.

Moreover, there has been a complete lack of political commitment to foster systematic investigation and prosecution of the grave and well-documented human-

Prosecution of
office abuse

3

'06 '18 10



1

Civil rights

4

'06 '18 10



1

rights abuses during the ten years of civil war (extrajudicial executions, forced disappearances, rape and torture). On February 10, 2015, the government established the Commission on Investigation of Disappeared Persons (COIDP) and the Truth and Reconciliation Commission (TRC). However, many human-rights activists and the U.N. Office of the High Commissioner for Human Rights warned that the legal basis of these institutions contradict fundamental human-rights principles as they allow for full amnesty even in the case of grave and gross human-rights violations. Immediately after the establishment of the commissions, the Supreme Court ruled the courts must fulfill the primary role in delivering justice for conflict violations, invalidating the amnesty provision. The government ignored the decision and the commissions have continued working with great difficulty. They have received 60,000 complaints, but as their terms end in February 2017 (now extended for another year), no perpetrators have been brought to justice so far.

Amnesty International has reported that discriminatory relief distribution after the earthquakes disproportionately impacted marginalized groups, while reconstruction efforts were delayed in all affected areas.

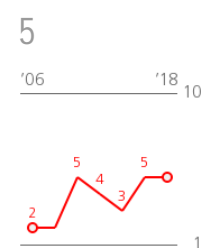
Beyond the legacy of the civil war, systemic weaknesses in the rule of law encourage rights violations. For example, criminal gangs, mafias and small armed groups (the boundaries between them are fluid) often enjoy various degrees of political protection. The police frequently use disproportionate force to quell political protests but do little to enforce order during the often violently enforced shutdowns. Levels of protection also significantly depend on class and caste status. Caste-based discrimination and sexual violence often go unpunished.

4 | Stability of Democratic Institutions

Democratic institutions exist at the national level, but they are unstable, somewhat contested and – because of the perpetual political controversy and the resulting deadlock – of little effectiveness. Since the CA election in November 2013, Nepal has had four different prime ministers (including former Chief Justice Khil Raj Regmi, who served as prime minister until February 2014), supported by uneasy and unstable coalitions leading to incoherent and ineffective policy-making. Vested interests among the parties have undermined the effectiveness of democracy.

Since the disbanding of the elected village councils in 2002, there have been no democratically elected representative bodies at the local level. The lack of democratically legitimized bodies on the regional and local levels adds to a picture of a democratic system that is limited to a set of national institutions. Political leaders are now negotiating to hold local elections, but no agreement has been found. Similarly, federal restructuring has yet to take place, and the administrative structure of the seven Provinces has not been created.

Performance of democratic institutions



Political parties suffer from an absence of democratic structures and norms in many respects. Disadvantaged segments of society have won a voice in the process, thanks to the proportional election system quotas (which have now been reduced under the new constitution), but they are still playing a minor role in the higher reaches of the parties.

Most political actors support the 2007 agreement on democratic transition and institutions. This was confirmed by the elections to the Constituent Assembly in April 2008 and, again, in November 2013. Even the Communist Party of Nepal-Maoist, which decided to boycott the poll, confirmed its commitment to the constitutional process.

However, legislative deadlock and ineffective governance undermine the legislature and government's authority, weakening their legitimacy. The difficulties in amending the embattled new constitution and forming stable and effective governments provide an entree for conservative critiques of the constitutional process as a whole. One indicator of this is the re-emergence of royalist parties as a significant political force in the 2013 election.

5 | Political and Social Integration

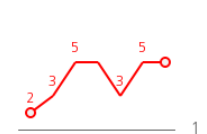
The political party system is fractionalized, polarized, based on factionalism and elite-dominated. Thanks to the fact that 60% of the Constituent Assembly's seats were elected under the proportional system, with quotas for marginalized groups, disadvantaged groups have been at least adequately represented in the legislature. But the same cannot be said for the government, political parties, administration, judiciary, media, education system or business. Moreover, the new 2015 constitution has reduced the percentage of seats allocated through proportional representation to 40%.

The traditional parties – Nepali Congress and CPN-UML – have strong social roots but face difficulties recruiting and maintaining the allegiance of cadres from Dalit and Janajati backgrounds and lack adequate democratic and participatory mechanisms. Most political parties remain personality-oriented organizations with authoritarian power structures. All power is concentrated in the party headquarters in the Kathmandu Valley; any participation at the local level or in rural areas is very limited. None of the established parties make any effort to achieve balanced popular participation in its own leadership posts or in the country's political institutions. The upper Bahun and Chetri caste groups (especially the former) dominate in all areas. Despite promises of revolutionary social transformation, the Maoist parties have fared only slightly better at democratizing their ranks. The Maoists may have a greater support base at the local level due to their protracted mobilization in rural areas during the civil conflict, but they have rapidly lost legitimacy over the past year as their government has floundered. There is a high degree of clientelism, patronage

Commitment to democratic institutions

5

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Party system

3

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and even corruption exercised by the political leadership at each level of governance. While these practices may – for a limited period – engender a degree stability, they make sociopolitical and economic transformations difficult to achieve.

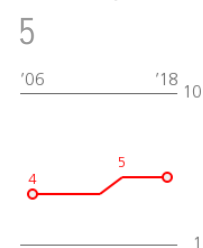
Recent years have seen several new parties arise, largely organized around regional or ethnic affiliations. Additionally, there are many vocal civil society organizations representing the full spectrum of political perspectives. Some are accepted as more legitimate than others, but most civic associations maintain explicit political allegiances. It is rare to find organizations attracting membership across party lines, and therefore few organizations are accepted as equally legitimate by all relevant actors. In addition, many ethnic and regional identity-based groups perceive the political parties (and therefore the structures of governance that they operate) as seeking to keep power in the hands of long-dominant upper-caste Hindus, and therefore are not fully representative of the citizenry as a whole. By the same token, many of the regional and ethnically based parties are viewed by those elites as exclusionary and potentially threatening to national unity. Given the embattled nature of the new constitutional settlement, it is reasonable to expect that such polarization will only deepen in the future.

Supported by socioeconomic changes and the presence of many international NGOs, several civic organizations and interest groups have established themselves since the first transition to democracy, in the early 1990s. These include labor unions, community-based groups, local NGOs and organizations for women’s rights. They are playing a role in representing social interests and interest mediation. Organizations such as the Nepal Federation of Indigenous Nationalities, the Nepal Bar Association, and the Federation of Nepali Journalists have exercised significant influence in fostering public debate and pressing for political commitments during the most recent phase of transformation. Some of these interest groups are funded by international development agencies, while others derive their support exclusively from local, national or regional actors. Some donors and NGOs act in a parastatal fashion, in many cases delivering services and/or exerting strong influence in policy arenas. Such organizations also serve an important liaison role between citizens and policymakers at the center.

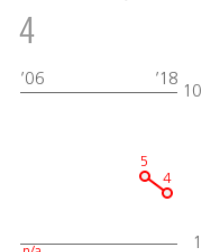
However, the effectiveness of these INGOs and NGOs are regularly questioned.

The most recent data available regarding approval for democracy in Nepal is the 2013 Citizen Survey: Nepal in Transition, which was conducted after the dissolution of the first Constituent Assembly in May 2012. The Survey was conducted by the State of Democracy in South Asia/Nepal Chapter (SDSA/N) of the Nepal Center for Contemporary Studies (NCCS) and International Institute for Democracy and Electoral Assistance (IDEA). According to study, support for democracy dropped to 53% of respondents in 2013 from 67% in 2007. Moreover, 36% of respondents said it “does not make a difference” when asked to choose between democracy and authoritarianism, and 11% favored a non-democratic government in certain

Interest groups



Approval of democracy

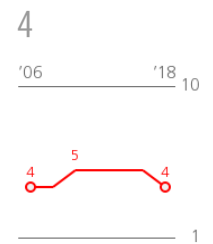


circumstance. An often-cited survey (Himalmedia Public Opinion Poll 2013) seems to indicate that the long-standing inability of high-level political actors to ensure the continuity of democratic institutions has contributed to relatively low levels of public trust. According to the survey, 61.1% of respondents thought democracy was under threat, and 39.4% said the reason for this was “wrangling political parties.” On the other hand, the widespread participation of voters in the 2013 elections and the success of ideologically moderate parties such as the Nepali Congress (NC) seem to demonstrate that there is a broad understanding of the importance and approval of democratic procedures among Nepali citizens. However, the period under review has witnessed the promulgation of a controversial constitution pushed through the CA in an exclusionary fashion, protracted protests in the Terai, little progress on post-earthquake reconstruction, and no advancements on the transitional justice front. It seems reasonable to deduce that these factors have further weakened support for democracy in Nepal. Political parties are motivated by self-interest and often keen to change the government to their advantage rather than the interests of the country. As a consequence, people have lost faith in the democratic systems as fights between political parties continue.

Studies of the level of trust, strength and forms of social capital in Nepal are not available, except for a few anthropological and ethnographic studies that provide anecdotal evidence. It remains uncertain if these insights can be viewed as representative or aggregated to the whole society.

Nonetheless, associational activities have been improving in the last 25 years. Networks of cooperation and mutual support are well developed along not only political party, business and alumni, but also along ethnic, caste and regional lines. In many localities, such organizations fill the spaces that might otherwise be filled by effectively decentralized state agencies. However, they often act to further the interests of a specific group, whether defined in ethnic or regional terms. Therefore, it could be argued that these networks do reproduce bonding social capital instead of bridging social capital, and, therefore, do not support the formation of civic self-organization. A recent study about social cohesion in Asia found Nepal to be part of a South Asian cluster of weak cohesion, which also points toward a rather low level of trust among the population.

Social capital



II. Economic Transformation

6 | Level of Socioeconomic Development

Nepal is one of the poorest countries in the world, with per capita GNI of about \$730 and per capita GDP of \$691.70 (2014). Remittances continue to represent a significant part of Nepal's revenue, estimated at 28% of GDP in 2013. According to the UNDP's Nepal Human Development Report 2015, the country ranked 145th out of 188 countries, with an HDI score of 0.540 (2015), in the same position as in 2014 (note: the two rankings are not directly comparable). That put Nepal two ranks above Pakistan (147) and well ahead of Afghanistan (171). It is important to note that the tables in the UNDP's Nepal Human Development Report 2015 use data available to the Human Development Report Office (HDRO) as of April 15, 2015, so before the earthquakes. The World Bank Post Disaster Needs Assessment (PDNA) priced the damage at \$7 billion, with total reconstruction needs at \$6.7 billion. The largest single need identified by the PDNA was housing and human settlements, estimated at about \$3.27 billion.

According to the Asian Development Bank, in 2016, 25.2% of Nepal's population lived below the national poverty line. With regard to the economic impact of the earthquakes, the World Bank suggests that an additional 3 per cent of the population had been pushed into poverty as a direct result of the earthquakes. This translates into as many as a million more poor people.

The UNDP Human Development Report identifies a Gini coefficient of 32.8 and a Gender Inequality Index of 0.489. Socioeconomic inequalities in Nepal on the basis of gender, caste, ethnicity, language, region and sexual orientation remain structurally ingrained and pervasive. These long-standing social hierarchies continue to restrict the access to political influence and economic opportunities of the many marginalized groups. For instance, Nepal's ranked 110th among 144 countries in the Global Gender Gap 2016.

Question
Score

Socioeconomic
barriers

2

'06 '18 10



Economic indicators		2013	2014	2015	2016
GDP	\$ M	19271.2	20003.0	21313.5	21143.9
GDP growth	%	4.1	6.0	2.7	0.6
Inflation (CPI)	%	9.0	8.4	7.9	-
Unemployment	%	3.3	3.0	3.0	3.2
Foreign direct investment	% of GDP	0.4	0.2	0.2	0.5
Export growth	%	10.3	18.8	6.8	-2.8
Import growth	%	14.2	20.9	9.6	3.3
Current account balance	\$ M	1160.2	496.2	2446.6	-
Public debt	% of GDP	31.9	28.3	25.0	27.3
External debt	\$ M	4013.3	4166.0	4138.9	4251.3
Total debt service	\$ M	221.5	228.5	221.9	229.6
Net lending/borrowing	% of GDP	1.7	1.8	1.1	1.4
Tax revenue	% of GDP	15.3	15.9	16.8	18.7
Government consumption	% of GDP	9.9	10.3	11.0	10.9
Public education spending	% of GDP	3.5	4.0	3.7	-
Public health spending	% of GDP	2.2	2.3	-	-
R&D expenditure	% of GDP	-	-	-	-
Military expenditure	% of GDP	1.5	1.6	1.5	1.5

Sources (as of October 2017): The World Bank, World Development Indicators | International Monetary Fund (IMF), World Economic Outlook | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database.

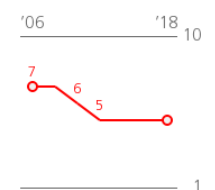
7 | Organization of the Market and Competition

Lack of good governance and effective institutions have led to ineffective operation of market forces in Nepal. There are often price hikes and artificial shortages of basic necessities, and no one seems to be accountable or even questioning this status quo.

According to the US Department of State, “the first privatization of a state-owned corporation was conducted in October 1992 through a cabinet decision (executive order). The Privatization Act was passed fourteen months later in January 1994. A total of 23 state-owned corporations have been privatized, liquidated or dissolved so far. The process, however, has been static since 2003 [...] Former public monopolies

Market-based competition

5



1

in banking, insurance, airline services, telecommunications and trade have been eliminated.”

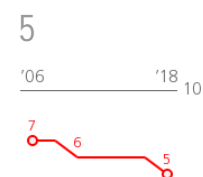
Nepal acceded to the World Trade Organization in April 2004 as the first Least Developed Country (LDC) to do so. Nevertheless, the institutional and legal structures to implement the WTO agreement have not been properly developed. Red tape, delays and strikes have significantly discouraged investment in the country. Structural difficulties of trade-related services and infrastructure prevented the realization of potential comparative advantages. Apart from the WTO, Nepal is also a member of two regional trade frameworks: the South Asia Free Trade Area (SAFTA: Afghanistan, Bangladesh, Bhutan, India, the Maldives, Pakistan, and Sri Lanka) and the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC).

Its commitments under the WTO framework are extensive, with most tariff lines bound at an average final bound rate of 26.2%; all trading partners hold at least Most Favored Nation (MFN) status. The effectively applied average tariff rate of 12.5% in 2012, which was significantly higher than the regional average of 7.2%. This includes strategic sectors such as agriculture and manufacturing, in which simple average MFN tariff rates fall significantly below final bound lines. Non-tariff measures, in the form of import license requirements, affect only a small number of products. Negotiation priorities under the WTO framework are improved market access for LDCs in general, and Nepal’s export products in particular, as well as easier movement for LDC’s semiskilled and unskilled labor.

While in principle, Nepal has a number of investment-friendly laws and regulations in place, the operation of foreign banks, repatriation of profits and currency exchange facilities remain constrained. India is the largest single source of foreign investment in Nepal, accounting for 43% of greenfield FDI inflows in 2013. Trade with India made up almost 70% of the country’s total trade in 2013 but is subject to special regulations and somewhat restrictive requirements. Moreover, the unofficial Indian blockade of Nepal in 2015-6 deteriorated both trade and bilateral relations between the two countries.

As mentioned before, with the 2007 Competition Promotion and Market Protection Act, legislation to prevent monopolies and cartels exists, but it is scarcely implemented due to the lack of good governance and institutions. Tentative efforts to dissolve syndicates often meet with fierce resistance from militant labor unions and private business, and have proven unsuccessful so far. Indigenous investment is slowly starting, such as in the power generation sector, but is hampered by shortages of essential goods.

Anti-monopoly
policy



The 2016 World Bank Report “From evidence to policy: supporting Nepal’s trade integration strategy” has stated that Nepal remains poorly integrated and has more to gain from integration into regional and global value chains. Yet, Nepal’s current remittance-driven growth model is introducing an anti-export bias, adding barriers to reaping full gains from integration.

Good governance, quality institutions and physical infrastructure are essential to facilitate foreign trade and foreign investment. In the absence of the essential prerequisites, Nepal has failed to benefit from trade liberalization attempts. In addition, a poor industrial relations environment, which makes hiring and firing an employee extremely difficult, has also discouraged labor-intensive activities in the country.

Traders in Nepal not only face the challenges of distance but also challenges related to transit due to Nepal’s landlocked position. These include frequent checks by border security officers and police, time-consuming customs formalities, shortages of containers at the borders, differential tariff rates for the Nepalese consignment at the Kolkata port and long delays at the port, which obviously add to the cost of international trade. According to a rough estimate transit costs associated with overseas imports are as high as 20% of the value of goods. This is attributed to the high costs of transport, damage and pilferage (while goods are in transit), time-consuming customs formalities and numerous fees, both official and unofficial.

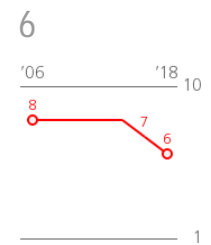
The Nepalese customs are not connected to the Indian customs through computer networks, causing delays at customs points on either side. Consequently, customs clearance remains a highly document-intensive and time-consuming formality. Often, payment of unofficial fees is unavoidable to reduce the clearance times.

Moreover, the Australian Trade Commission advises that tariffs and duty rates in Nepal are constantly revised and are subject to change without notice. In terms of tariff barriers, customs duty rates vary from item to item and can range from 0% to 130%. Regarding non-tariff barriers, the Export/Import (Control) Act 1956 permits businesses registered in Nepal to import a range of goods, except goods which are either fully or partially prohibited.

Nepal ranks at 107 on the World Bank’s Doing Business 2017 report compared to 99 last year. The main reasons behind the drop are a decline in Nepal’s business regulatory environment and data revisions. Nonetheless, Nepal ranks second highest in South Asia after Bhutan (73) and ahead of Sri Lanka (110). The IMF highlights that there is considerable scope to simplify trading across borders, enforcing contracts, paying taxes and getting credit in Nepal.

FDI inflows into Nepal are very low. At less than 1% of GDP, Nepal’s FDI inflows are the lowest among comparators. According to the World Bank, while this is partially explained by firms’ perceived risks of operating in the country, the

Liberalization of
foreign trade



investment regime in Nepal is more restrictive than in other countries at a similar level of development. Restrictive FDI policies compound the challenges the country faces in attracting foreign investment. The World Bank (2015) lists the following difficulties for FDI in Nepal. Firstly, the cumbersome processes for the repatriation of funds and the lengthy processes needed to hire foreign workers. Secondly, foreign ownership limitations. For instance, Nepal retains a foreign ownership limit of 51% in some selected sectors, such as legal, accounting and engineering services. Thirdly, sector caps, a long negative list, and restrictions in non-equity modes of investment.

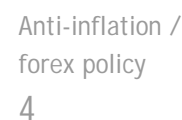
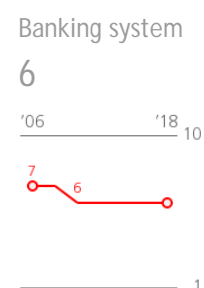
Despite eliminating the minimum investment requirement of \$200,000, the new Foreign Investment Policy (FIP) significantly expanded the negative list to include poultry, fishery, print and electronic media. This limits the amount of foreign investment entering Nepal and constrains the ability of important sectors of the economy, including manufacturing, to attract FDI. Restrictions in non-equity modes of investment, such as franchising, in which there is significant technology, training and skills transfer, face additional delays and costs during entry and operations in Nepal. In particular, slow and arbitrary approval processes, dual registration procedures, delays in trademark registration, and difficulties in remitting royalties and technical fees are among several obstacles faced by these type of investments.

According to the US Department of State, Nepal's banking system assets totaled approximately \$19.91 billion as of February 2015, and deposits equaled \$15.75 billion. As of February 2015, 3.07% of the total asset base was estimated as non-performing.

Nepal's banking and financial sectors suffer from persistent structural problems. Key problems include the central bank's limited independence (despite the 2002 enactment of legislation to increase central bank autonomy) and weak supervision and enforcement capabilities; the high number of banks and financial institutions and the lack of a competitive environment resulting from fragmentation of the banking system; ineffective enforcement of capital requirements; an extensive sector of state-owned banks with high proportions of non-performing loans; and weak incentives for improving corporate governance, accountability and transparency in the banking system. The non-performing assets (NPA) volume declined in recent years, at the same time that total loans have been continually increasing, thus resulting in a more favorable proportion. However, the NPA ratio is still a long way from being satisfactory.

8 | Currency and Price Stability

The Nepali rupee (NPR) is pegged to the Indian rupee (INR) at a rate of 1.6 to 1.0, which Nepali policymakers and international organizations such as the IMF insist is important for overall macroeconomic stability. Accordingly, the value of the NPR fluctuates with the INR and weakened against the U.S. dollar considerably with the



exchange rate of U.S. dollar to NPR improving from an early 2015 low of 1:98 to 1:107 in January 2017. Foreign exchange is not freely available. Under the 1962 Foreign Exchange (Regulation) Act, commercial transactions payable in convertible currency need approval from the central bank (Nepal Rastra Bank, NRB). According to World Bank data, reflecting both the earthquake and trade-related disruptions, inflation spiked to over 12% (y/y) by mid-January 2016 rising five percentage points in just four months from mid-September 2015. This was the highest inflation level since FY 2009. As the trade disruptions ended, inflation eased to back to single digits.

The IMF Nepal country report of 2010 stated that Nepal's central bank (the Nepal Rastra Bank, NRB) featured limited independence, negatively affecting supervision and enforcement. A 2014 Asian Development Bank (ADB) report concludes that while Nepal Rastra Bank's supervisory capacity has generally improved, its independence and enforcing authority have remained weak.

According to the IMF, the 2015 earthquakes represented a major shock to Nepal's economy, but the risk of debt distress is expected to remain low thanks to the low starting level of external debt and the high concessionality of new debt. At the government level, after the earthquakes Nepal suffered short-run revenue (especially in agriculture and tourism) followed by a gradual recovery over the medium term.

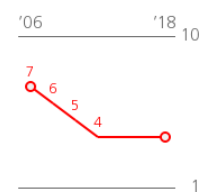
Fiscal policy is expected to remain responsible. The external current account is projected to move from a sizable surplus in 2013/14 to moderate deficits over the medium term. The IMF forecasts that the ratio of public debt to GDP will rise gradually from 28.3% in 2014 to 31.2% in 2035. However, debt dynamics may be susceptible to volatility in remittance flows.

The government's challenge is to continue its prudent fiscal policy, while effectively carrying out the reconstruction plans, restructuring state-owned enterprises and the financial sector, while at the same time increase spending on infrastructure development to encourage domestic growth.

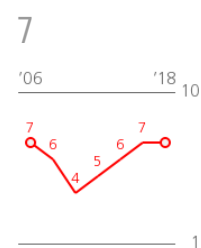
9 | Private Property

Despite the fact that property rights and the regulation of property are defined by the 2015 constitution, in the absence of good governance, they are regularly violated. Though the Maoists committed themselves to the constitution, they have nevertheless hesitated in restoring all the property – mostly land – they had confiscated during the insurgency. As part of the peace process that began in 2006, the Maoist agreed in principle to return all of it, and have done so in the majority of cases, but some land remains to be restored even if there is no official data on contested titles.

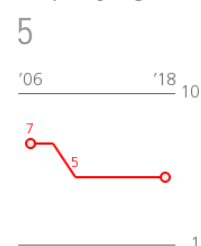
Insecure property rights are a particular problem for the poor, who often lack proper documentation for land titles, and are ill-equipped to maneuver through local courts



Macrostability



Property rights



and administration. Smallholders in the Terai region are often caught in a catch-22, whereby they require citizenship certificates to register their land properly (only Nepali citizens can own land), and land titles are among the most important supporting documents through which the local administration ascertains citizenship status. Among the poor, women find themselves at a particular disadvantage.

Even though legal provisions regarding property and inheritance have been declared equal in the constitution since 2006, women are often unable to make rightful claims in the face of continuing discrimination through prevailing social practice.

Private companies are constitutionally permitted and protected. Some restrictions apply to foreign ownership. Bureaucratic and legal hurdles an entrepreneur must overcome to incorporate and register a new firm are among the lowest in South Asia. Yet, the real problem for setting up a private commercial or industrial enterprise is not registration, but political and bureaucratic interferences in day-to-day business once a firm has begun to operate.

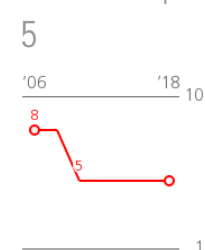
Many of the more than 80 public enterprises in diverse sectors were privatized in the 1990s. The process came under some critique, as many newly privatized companies soon found themselves in choppy waters. There were also allegations that privatization processes were not transparent, and that state assets were widely undervalued. Privatization of state-owned enterprises has been on hold since 2008. In 2015, there were 37 public enterprises in Nepal, such as the Nepal Airlines Corporation (NAC) and the Hetauda Cement Industry Limited (HICL). Many (15) have faced high cumulative losses and unfunded liabilities for years due to operational inefficiencies and other problems. Overall, most observers think public enterprises will be an increasing burden on taxpayers and consumers because of their poor performance. However, further privatizations are blocked by opposition from interest groups, bureaucratic inefficiencies, the general lack of political stability, lack of political consensus and a weak domestic financial market. According to the United States Department of State, after the Constituent Assembly elections in 2008 and 2013, the government has been reluctant to restart stalled privatization.

10 | Welfare Regime

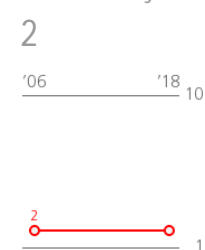
Nepal has virtually no welfare regime outside of social networks based on familial structures. In some cases, NGOs attempt to fill this gap, but they only provide locally specific piecemeal services. This means that the social welfare options may vary greatly depending on the area of residence and access to international donors.

Family support structures are strong but increasingly weakened by widespread, long-term out-migration by young people, especially men. Although their financial remittances certainly help compensate for social risks, their physical absence often

Private enterprise



Social safety nets



means that the elderly and other dependents are left on their own, or are reliant upon more distant relations.

Private initiatives are isolated, and public social services are underdeveloped and insufficient, although access has been improved in recent years. Over the last decade, Nepal has seen tremendous growth in medical colleges and other institutions of medical education. However, these institutions concentrate mainly on urban centers, and especially the Kathmandu Valley, while most rural Nepalese are still without health care.

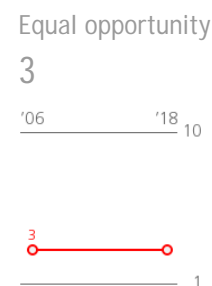
Public expenditure on health (in the percentage of GDP and government expenditure) are relatively high by South Asian standards but are still insufficient (as in almost all South Asian countries), and resource waste and inefficient use of finances remain huge problems.

Legally sanctioned social inequality on the basis of ethnicity, language, caste and gender was a defining feature of the Nepali state until very recently. While discrimination on the basis of caste was in principle outlawed in the 1960s, in practice, it remains a defining feature of life for many Nepali citizens.

Laws that discriminate on the basis of gender have remained on the books until much more recently. Activist lawyers have succeeded in having the Supreme Court declare a number of these provisions unconstitutional. However, the new 2015 constitution still discriminates between men and women in passing Nepali citizenship to offspring. While the Supreme Court has repeatedly ruled confirming gender equality on citizenship matters, implementation is still erratic at best.

Many of Nepal's recent episodes of political contention have been driven by social mobilizations that place the rectification of such inequalities at the top of their agenda. People from certain ethnic, caste, and regional backgrounds, and especially women, routinely experience discrimination in public life and are excluded from accessing resources and positions of power. Social and economic caste-based discrimination was an important underlying cause for the rise of the Maoist insurgency in the 1990s, as is evident from the participation of a large number of marginalized people in the upheaval.

Since 2006, a range of measures designed to improve this situation have begun to take effect, although their implementation and impact are still limited. These include the establishment of proportional representation guidelines for the Constituent Assembly elections, which, although controversial in their details, established a mechanism for ensuring significant diversity in elected office; and the 2007 second amendment to the Civil Service Act, which established, for the first time, affirmative action provisions for the civil service, including the police, provisions that aim to increase the representation of women, indigenous nationalities, Madhesis, Dalits, disabled people and people from "backward" regions. Significantly, the new



constitution has reduced the percentage of parliamentary seats elected under proportional representation from 60 to 40% and introduced the new controversial category of Khas-Arya (i.e., high-caste Pahari Hindus, Bahun and Chetri) for affirmative action purposes.

Male members of the Brahmin caste (Bahun), who comprise only 12.74% of the country's population, continue to occupy the overwhelming majority of civil service posts. In addition, over 40% of the NAF's ranks filled by soldiers and officers from the Chhetri caste (15.8% of the population). Moreover, the same traditional groups dominate the judiciary, the education system, the media, labor unions and even NGOs.

Nepal's labor market provides highly unequal chances; approximately 70% of the workforce is employed in the informal sector (ILO), facing multiple challenges and constraints and left unprotected by basic social safety nets. Workers are subject to exploitation and deprived of many fundamental rights at work. In the past, Nepalese governments have turned a blind eye to abuses.

Recently, a labor law was drafted to address issues crucial to workers in the informal economy. Given the climate of political stagnation, there is little expectation this essential reform will be implemented.

According to official data from ILO, 87.5% of men and 80.1% of women were employed in the formal and (mostly) informal sector in 2014. The agricultural sector accounts for 73.9% of employment, while 16.9% of the labor force is employed in the service sector and 6.6% in manufacturing.

In 2013/14, 527,814 labor permits were issued, a marked increase from the previous years. The main destinations through the permit system are as follows: Malaysia (40.6%), Qatar (23.7%), Saudi Arabia (16.4%) and the UAE (10.3%). Men account for more than 95.1% of the registered labor migrants.

The majority of international migrants from Nepal head to India (37.6%), for which no visa is needed. They work in India's private sector, mostly in manual labor jobs in industry, construction work, agriculture or the service sector. Their wages tend to be low, and the work is often dirty, dangerous and even degrading. While reliable data is missing, some 100,000 to 150,000 Nepali women are estimated to be employed in the sex industry across India.

11 | Economic Performance

Despite modest GDP growth in Nepal, gross consumption remains very strong increasing from NPR 42.8 billion in 2003/04 to NPR 61.4 billion in 2012/13 in real term (up from 88% of GDP in 2003/04 to about 91% in 2012/13). Soaring consumption is mainly due to increased inflows of remittances, which surged from

Output strength
5

just under 11% of GDP in 2003/04 to 25% by 2012/13 (Sharma, 2015). However, Nepal remains one of the poorest countries in the world, with per capita GNI of about \$730 and per capita GDP of \$691.70 (2014). The World Bank estimates that the earthquakes, coupled with trade disruptions that occurred from September 2015-January 2016, pushed down tax revenues and the overall growth of FY 2016 to 0.6 per cent (at market prices) – the lowest in 14 years. Reflecting both the earthquake and trade-related disruptions, inflation spiked to over 12% (y/y) by mid-January rising five percentage points in just four months from mid-September 2015. This was the highest inflation level since FY 2009. As the trade disruptions ended, inflation decreased. Following two years of low growth, the Nepal Development Update (October 2016) predicted a rebound.

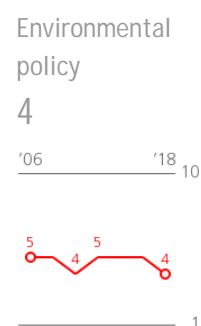
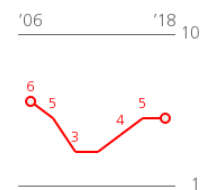
According to the IMF, real GDP growth is expected to fall from 5.4 per cent in 2013/14 to 3.4 percent in 2014/15, due to significant economic losses resulting from the earthquake. Nepal's external debt stood at 17.9% of GDP by the end of FY 2013/2014 (\$3.5 billion), of which 86% was concessional borrowing from the World Bank and the Asian Development Bank (ADB). Domestic debt, instead, declined from 12.2% of GDP in 2012/13 to 10.4% by the end of FY2013/14, as low budget execution resulted in a budget surplus. Nepal's reliance on remittances remains critical. Moreover, according to Nepal's National Planning Commission, Nepal faces an alarming level of trade deficit. Over the years, export has almost been stagnated, and the import skyrocketed. Nepal's import is now nine times bigger than export. The Three-Year Plan ending on July 15, 2016, aimed at maintaining a trade deficit of 20% of the GDP, but the preliminary estimates indicate such deficit to be around 35% of the GDP. India commands the biggest share of Nepal's foreign trade at 64% while China has increased its share to 12%.

According to the UNDP Human Development Report, 81.1% of Nepal's population is in employment. However, the ILO highlights that the majority of workers remain in vulnerable employment and that such a situation is compounded by the lack any social protection schemes.

12 | Sustainability

Nepal has endured two major earthquakes in the spring of 2015. Many international observers, local media and foreign tourism agencies criticized the lack of preparation and rapid responses by the government to weather-related risks. On top of the devastation caused by the earthquakes, previous patterns of extensive deforestation make the country particularly susceptible to landslides and flooding, especially during the monsoon.

Moreover, with its unique geographical position and complex ecology, Nepal is one of the main countries to experience significant negative effects of climate change.



Economic growth in recent years has been achieved at high environmental cost and will probably lead to even greater environmental degradation, especially because of increasing air pollution and deepening problems of water sanitation and water resource management. In recent years, there have been calls from environmental experts for the implementation of measures protecting the wetlands, flora and fauna of the country. Corresponding government policies are still pending.

In 2016, Nepal had an Environmental Performance Index (EPI) score of 50.1 (ranked at 149th out of 180), which placed it below all other South Asian countries (except Bangladesh and Afghanistan). Ambient air pollution remains a major problem in Kathmandu. Particulate pollution is mainly driven by vehicle traffic, both in terms of combustion emissions and dust re-suspension, as well as by other forms of combustion, and industrial sources such as brick kilns within the valley. Long-term effects on public health have not yet been established with certainty, but experts assume they are severe. The 2016 EPI estimates that nearly 75% of Nepal's population is exposed to poor air quality (i.e., unsafe levels of fine particulate matter) alongside poor drinking water and sanitation.

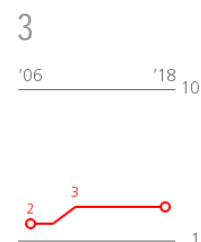
Nepal has also put in place a comprehensive set of environmental policies in close partnership with the international donor community. Efforts have been particularly successful in the areas of conservation/biodiversity and forestry. Large swaths of Nepal's forests are administered through community forest user groups, and the forest cover generally decreases at a very low rate. Large-scale deforestation still occurs, however, especially in the southern Terai belt.

The expansion of sustainable energy use has been less successful. The main energy source at the household level, outside of urban centers, is biomass (firewood). The government has drawn up plans to facilitate investments in the hydropower sector to alleviate the crippling power cuts during the dry season, but so far with little to show for it. Several donor agencies also assist with incipient plans to incentivize companies to invest in energy efficiency and sustainable energy sources.

Nepal's last National Census in 2011, identifies the country's literacy rate at 65.9%, among men the literacy rate is at 75.1% and among women the literacy rate is at 57.4%. According to 2015 UNESCO data, Nepal's public expenditure on education amounts to 3.75% of the country's GDP. The Ministry of Education launched a school sector reform program for 2009 – 2015 with an estimated budget of \$568 million. According to World Bank data, the primary school completion rate has significantly improved between 2013 and 2015.

The results of the nationally conducted school-leaving certificate examinations in 2016 demonstrated the dismal state of the country's educational system, as 72% of pupils in government schools who took the exams failed. Moreover, teachers and

Education policy /
R&D



school personnel frequently complain about undue interference by officials in human resources affairs, curriculum development and financial matters.

Reforms in higher education are underway, but implementation has stalled. The central aspect of current reform efforts is to break up the centralized university system. However, underfunding remains a problem of the higher education sector as only about 10% of overall public spending is allocated to university education. Finally, overall national spending on research and development remains insignificant.

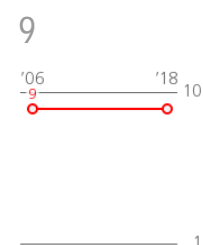
Governance

I. Level of Difficulty

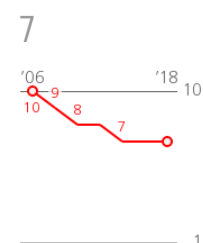
The Nepali political leadership faces significant structural constraints in achieving good governance goals. Highly unfavorable conditions for economic and political transformation include a low level of economic and social development; a population with relatively low, though improving, educational attainment; the geographical disadvantages of a landlocked state; resource scarcity, and still-weak Stateness. Nepal's environment is prone to the effects of natural disasters as seen with the devastating 2015 earthquakes and man-made ecological devastation. The country's terrain is challenging to navigate, and, coupled with an overly centralized state machinery, it is often difficult for policymakers at the center to effectively assess citizen aspirations and needs. Widespread poverty, as well as uneven educational resources across the country, rapid urbanization and ongoing brain drain, as nearly a quarter of the country's workforce is employed outside of Nepal. Militancy and crime are widespread, despite the end of the Maoist insurgency. Most affected is the Terai flatland along the southern border with India, especially due to the protests against the new constitution and the unofficial Indian blockade on the open border. Nonetheless, the political leadership is also in large part responsible for the long and unstable political settlement, which in itself has contributed to the current challenges by drawing attention away from much-needed infrastructural development agendas.

Nepal is one of the major recipients of official development assistance (ODA) and has a fairly large sector of international and national NGOs. Spaces for civic participation are manifold in Nepal and have improved in recent decades, contributing to the emergence of indigenous civil society movements. Many forms of engagement observed may not match conventional definitions of civil society, in the sense that they are often grounded in very specific local or ethnic affiliations, rather than articulated in highly visible forms at the national level. However, the number and range of civil society organizations operating even in the most remote and impoverished areas of the country are astounding. The challenge for these groups, however, is to articulate their agendas with national organizations and political actors to achieve sustained change in concert with the aspirations of multiple constituencies. Broad-reaching alliances between a range of different interest groups were key to the successes of both the 1990 and 2006 anti-regime mass movements.

Structural constraints

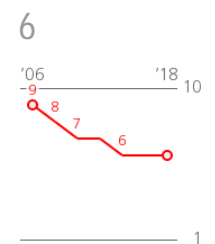


Civil society traditions



Public perceptions of polarization and cleavage along ethnic and regional lines have grown over the last several years, exacerbated by scaremongering in many national media outlets. The protests in the Terai over the new constitution and the heavy-handed response from the state have deepened the Pahari-Madhesi cleavage and brought further instability to the country. Moreover, other ethnolinguistic groups remain dissatisfied with the new political settlement. Many tensions run only slightly below the surface, and the society and the political elite are deeply split into social classes and ethnic or religious communities. Confrontations between cadres of different political parties, as well as between members of different social groups mobilized around identity-based platforms, run the risk of erupting into outright conflict if these groups perceive that their interests are inadequately addressed.

Conflict intensity



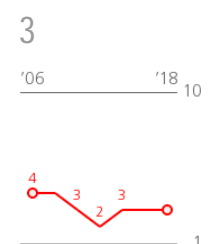
II. Governance Performance

14 | Steering Capability

Though the structural constraints on governance are high, the political leadership's low steering capability is another important cause of Nepal's current crisis. In general, policy-making plays a relatively minor role in Nepal's politics. The heterogeneous character of multiparty coalition governments before 2004, between 2006 and 2012, and again since January 2014 to date make it extremely difficult even for determined policymakers to set strategic priorities. Important policy decisions are frequently subject to fierce distributional battles between different ministries, either at the political or even the upper administrative level.

Question
Score

Prioritization



While the main priorities of the new coalition government of Prime Minister Dahal (Maoist, since August 2016) is to implement the new 2015 constitution and focus on the post-earthquake reconstruction, the focus on constitutional politics (amendments), federal restructuring and elections overshadow other urgent policy needs. Given the fragmented and factionalized party system, prime ministers (both Maoist and NC-based) are occupied with short-term challenges of political bargaining, which leaves little political space for the prioritization and organization of policy measures. Moreover, the segmentation of the cabinet along party lines contributes little to coordination between different ministries, weak prime ministerial leadership and control over line ministries. In addition, there are no regulatory impact assessments, nor is there a strategic planning unit, which contributes to a very low strategic capacity of the government to prioritize and organize its policy measures. Finally, the ongoing political struggle over the future character of the Nepali state contributes to a standstill regarding any administrative reforms.

With regard to the steering capabilities of Nepal's governments, the crucial bottleneck lies less in the drafting of good policies than in their implementation. Thus, successive governments have, over the last decades, instituted countless industrial growth, investment and trade promotion policies, often with substantial and systematic donor input, and very little effect on the ground. Different governments' capabilities to implement reform policies effectively have been weak, partly because of confrontational tactics, and the lack of clear strategic priorities. A startling example of this inefficiency has been the delay in setting up the National Reconstruction Authority and the ongoing failure to bring relief to the millions of earthquake victims across the country. The government is very weak in implementing its policies or policies that are necessary for the advancement of the country.

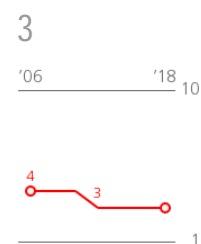
With regard to the implementation of the new 2015 constitution, the embattled process of federal restructuring of the state has not yet taken place. The political parties most opposed to federalism have pushed for local elections to take place before substantive institutional reforms most likely to delay further and stall the federalization of the country.

Regarding innovation in policy-making and implementation of drafted policies, the record of three different governments, as well as that of the opposition parties, was mixed during the review period. Learning from past experiences did not seem to happen: Nepal's political elite, by and large, support the perpetuation of traditional social cleavages, ensuring their grip on power. The political force that has shown itself to be the most flexible in the recent past is the Maoists, with mixed results. Notably, the former rebels have adapted to mainstream politics, including the system's dysfunctional patronage-based aspects, while continuing to pursue some, if not all, of their progressive policies. Nepal's political leaders seem to employ the strategy that flexibility guarantees political resilience. But flexibility does not necessarily lead to innovation. As new political players with change agendas were incorporated into patronage politics, new struggles over distribution occurred. Fundamental changes to the rules of the game dropped out of sight. The process by which the new constitution was passed and the government's response to the protests in the Terai, exemplify the endurance of this situation.

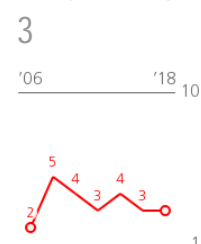
15 | Resource Efficiency

Neither the Congress-led government from 2014 to 2015 nor the UML-led government (2015 – 2016) efficiently used available economic and human resources for their economic and social policies. Often, resources intended for development vanished due to corruption. One significant positive step that took place under the current Maoist-led government has been the drastic reduction of electricity cuts, with a number of areas being declared load-shedding free in early 2017. This represents a significant boost for the industrial sector.

Implementation



Policy learning



Efficient use of assets



A pressing problem remains the inveterate job shortage, which has forced hundreds of thousands of young Nepalese to migrate to India, the Gulf region, Malaysia and eastern Asia in search of employment. Job-creating policies are de facto nonexistent, leading to a drain-off of Nepal's human capital.

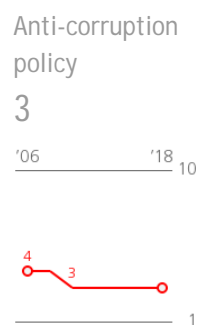
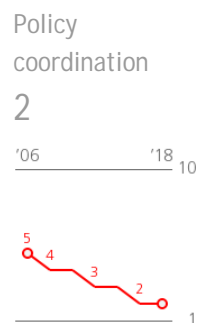
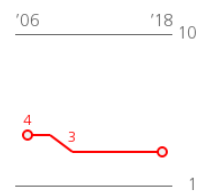
Development aid from India, China and the West alongside earthquake reconstruction funds play an important role in Nepal's budget. However, monitoring of these funds continues to be insufficient. While Nepal's administrative and civil services remained severely underfunded and also understaffed, other major problems of Nepal's administration are fragmented decision-making processes and the opaque and politicized system of transfers and promotions. Problems of timely spending also increased and contributed to serious delays and waste of resources.

The current Maoist-led coalition government is the ninth government to be formed over the last eight years. While the heterogeneous nature of the current party government (and of the previous ones) is one important reason for its failure to coordinate between conflicting interests and policy objectives, the need for all major political parties to deliver on promises to their competing constituencies and supporters is another. These parties remain deeply divided over fundamental policies, and, hence, there is little political space for effective policy coordination. Rather, policy decisions are frequently held hostage to demands for changes in government leadership, or other short-term political gains.

The misappropriation of public resources and other forms of corruption are endemic in Nepal. Rules and regulations to ensure transparency exist but are enforced poorly. Anti-corruption agencies lack the political or administrative support necessary for working effectively. The most important among them, the Commission for the Investigation of Abuse of Authority (CIAA), did not have a Commissioner for eight years, until 2013. Regrettably, in 2013, Loman Singh Karki – a controversial politician and businessman – was appointed as the head of the CIAA. In October 2016, he was eventually impeached and suspended from office. The Supreme Court made a landmark verdict in January 2017, disqualifying Karki as the Commission's Chief leaving the CIAA yet again with no head. The government is not effective at all in controlling corruption as there is no rule of law. Even the institutions like CIAA are regularly influenced by the ruling government as seen in the recent past.

Corruption among government officials concerning the distribution of permits and approvals, the procurement of goods and services, and the award of contracts presents significant obstacles to doing business. The situation is further complicated by the fact that government services are in scarce supply outside the capital. Most of the countryside lacks basic public services or local offices. Bribes are often the only way to get access to public services or to accomplish even ordinary activities.

There has been some additional regulatory progress over the last years. For example, a Right to Information Act was passed in 2009. Other steps, such as laws to govern



political party financing, might help. Ultimately, however, the best regulation will matter little as long as there are no agencies strong enough to enforce them. For example, regulations exist to compel political parties to declare their income, and parliamentarians to declare their sources of income and assets. Both regulations are outright ignored or subverted in the vast majority of cases.

16 | Consensus-Building

Nepal's political parties have a long history of supporting parliamentary democracy. Even the former Maoist rebels, when they laid down their arms in 2006 at the beginning of the peace process, agreed to conduct politics within constitutional democratic boundaries. In reality, political parties do not live with their values.

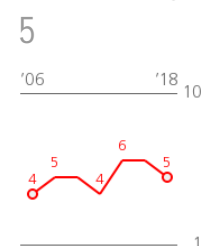
Nepal's mainstream political parties have all been committed to a market economy for decades. There is a general consensus that essentially capitalist economic growth is the best way to safeguard the achievements of the 2006 people's movement and ensure Nepal's sovereignty. At the same time, the Maoists' official ideology still espouses a socialist revolution as their final goal. Still, it is difficult to ignore the argument that the Maoist leadership will be unable to formulate a coherent market economic growth policy as long as it retains the explicit goal of achieving a socialist revolution, and as long as this line has a strong following within the party base. The fact that the CPN-Maoist dropped "people's war" from its charter and toned down its anti-Indian rhetoric is a promising sign but needs to be supplemented by concrete political action. However, it is not only the various Maoist parties that have proclaimed consensus on the goal of market economic transformation without corresponding actions. The same is true for other parties, such as the Congress, which seems either unwilling or unable to develop coherent policies of economic transformation that would match its political rhetoric.

Despite the protests over the new 2015 constitution, the major political parties share a basic pro-democratic consensus. While in government, neither Maoists nor the Nepali Congress can completely control all powerful semi-democratic actors or agents with de facto veto power at the local level. Nevertheless, they can limit their influence significantly.

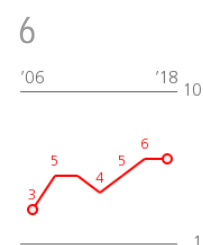
Despite some worries about a possible military coup d'état in 2012/13, the Nepal Army has refrained from overt political engagement in recent years. Its priority during the postwar years was to protect its institutional autonomy, and it appears content having achieved this goal. In addition, the army is highly dependent on India, which similarly has made clear that it will suffer no infringements on the NAF's autonomy, but otherwise does not wish it to play a larger role in politics.

Finally, the former royal family appears far too discredited for a comeback. Popular frustration with multiparty democracy is high, particularly since the lapse of the CA;

Consensus on goals



Anti-democratic actors



conservative parties may well see a significant increase in their vote shares on platforms stressing a return to Hindu values, and defending Nepal's old style of culturally homogenous nationalism. However, these parties have either distanced themselves explicitly from a revival of a constitutional monarchy or grown suspiciously quiet about it. Significantly, the conservative-royalist RPP-N finished the 2013 elections as the fourth-largest party. The party demands that Nepal be, once again, declared a Hindu state and is the only party that advocates a return to the pre-2008 monarchy. While not openly anti-democratic, this indicates a split regarding the basic type of state and the character of Nepal as a multi-religious nation and a secular state. Furthermore, all along the political spectrum, there is still a strong tendency for politics to be played out in the streets rather than through institutional mechanisms. Nonetheless, in many areas of the country, the last several years have seen a significant shift in the scope of social mobilization, with new spaces opening up for previously marginalized individuals to participate in associational life.

In Nepal, there are some 125 ethnic groups, 127 spoken languages, scores of castes and three distinct ecosystems that have long divided its 27 million people into feuding communities, making political consensus and conflict management extremely difficult.

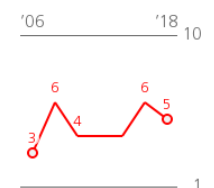
The political leadership's record of conflict management has been mixed in the last two years. On the one hand, the relevant political parties and elites have done little to counteract the growing polarization of the political sphere along ethnic lines especially since the protests over the new constitution. In addition, identity-based cleavages increasingly find expression in the party landscape, as demonstrated by the results of the 2013 elections and the increasing fragmentation of the political spectrum. On the other hand, political leaders from various parties and political camps to some extent successfully prevented cleavage-based conflicts from further escalating. However, the violence during the protests in the Terai and the unofficial Indian blockade have exacerbated tensions and deepened the Madhesi-Pahari cleavage.

Parts of civil society have also aligned themselves along emerging identity-based fault lines. Some social movements, civic associations and non-governmental organizations are accepted as more legitimate than others, but most maintain explicit political allegiances. It is rare to find organizations attracting membership across party lines, and therefore few organizations are accepted as equally legitimate by all relevant actors. In addition, many ethnic and regional identity-based groups perceive the political parties (and therefore the structures of governance that they operate) as seeking to keep power in the hands of long-dominant upper-caste Hindus, and therefore not fully representative of citizens at large.

While identity-based tensions may occupy the foreground in the public debate, it is also important not to forget the class tensions that both drive and crosscut them. Support for the Maoists during the civil war depended on a complicated mix of ethnic

Cleavage /
conflict
management

5



sentiments, local political alignments and class consciousness, and the latter played a role at least as central as the others. And despite the successful holding of the 2013 election and the formation of a new government, Nepali politics and society remain deeply divided.

With mass mobilizations in 1960, 1990, 2006 and 2015 a tradition of civil resistance and nonviolent mass mobilization has built up, which can rightly be considered civil society participation. Tellingly, however, this participation took the form of street politics, which is to a large extent a reflection of the insufficient openness of the political system for civil society and popular access to institutionalized politics.

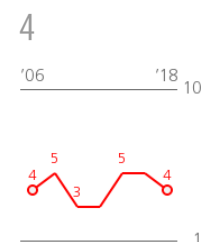
There have been signs of increasing political activism among non-governmental organizations and civil society groups since the return to legitimate democratic institutions since 2008, which has continued in the last two years.

In the realms of women's rights, and rights for ethnic, language and cultural minority groups, civil organizations have intensified efforts to advocate reforms. But the struggle to improve the representation of women's interests (including the embattled issue of citizenship) and those of ethnic and religious minorities is still an uphill battle, as the dominant upper-caste elite refuses to allow the equal participation of all social groups. Madhesi and ethnic organizations forced a number of concessions from the dominant state elite, and the new constitution was already amended in January 2016. However, while a second amendment has been tabled, no consensus has been yet found on the Bill.

Some of Nepal's most pressing policy debates are being held in the broader sphere of civil society. This is particularly true of questions around federalism and measures aimed at identity-based inclusion. Here, civil society organizations advocating for lower caste, ethnic and regionalist concerns were crucial in pushing these concerns onto the political agenda. While Nepal retains a thriving civil society, since the protests over the new constitution and the unofficial Indian blockade, it appears that Nepal's political leadership has been less willing to enable the participation of civil society in the political process.

However, except when resorting to strikes and demonstrations that severely affect public life, interest groups and civil society groups' impact on public policies remains limited. Moreover, many civil society organizations, including human-rights organizations and labor unions, are informally but closely associated with political parties. In addition, many civil society organizations are highly dependent on donor funding. While this funding can provide much-needed support for progressive projects, it also skews agendas as civil society activists work to realign their work with donors' funding priorities.

Civil society participation



There is consensus across the political board to prevent the prosecution of wartime crimes in any systematic manner. To this day no prosecutions for wartime atrocities have taken place in Nepal. Both the 2006 Comprehensive Peace Agreement and the 2007 interim constitution promised the establishment of transitional justice mechanisms and relief to the families of the victims. However, after much delay, in April 2014, the second CA passed the Act on Commission on Investigation of Disappeared Persons and Truth and Reconciliation, creating the Commission on Investigation of Disappeared Persons (COIDP) and the Truth and Reconciliation Commission (TRC). The Act contained extensive amnesty provisions that fell below international human rights standards. In February 2015, Nepal's Supreme Court ruled that any provisions of the Act to grant amnesties and divert such cases from the courts or to interfere in such cases are unconstitutional. The government, however, ignored the Court's ruling and proceeded to establish the two bodies. To date, neither commission has investigated a single case.

This situation reflects the fact that Nepal's political leaders press for token reconciliation efforts and blanket amnesties for perpetrators, while there is no discussion of investigations into command and administrative responsibilities.

17 | International Cooperation

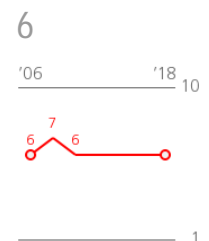
Nepal has a long history of working with international partners. Although this partnership has yielded good results, especially in the areas of education, health, drinking water, telecommunications, road construction and power generation, there is still a need to improve coordination and harmonize earthquake reconstruction funds, as well as development aid and debt relief, to increase efficiency and effectiveness.

Donor agencies and international financial institutions exert significant influence on Nepali policy-making, as do their diplomatic counterparts. The role of such actors in shaping Nepal's peace process and political transition has been controversial. During the conflict years, many donors were unable to efficiently retask funds to avoid appropriation by violent actors (both state and insurgent), and in the post-conflict years, they have refigured much of their engagement in terms of good governance, peace-building support, and technical support to the Electoral Commission and Constituent Assembly. Such assistance has often been proffered in an ad-hoc manner, driven by strategic priorities emerging from these organizations' home offices, rather than by conditions on the ground in Nepal – but the Nepali state has been happy to accept whatever is on offer, rather than seeking to align development support with well-articulated priorities of its own. Some critics have suggested that donors should withhold aid in order to compel better performance from Nepali political actors, but a more accurate reading of the scenario would locate the international community itself as complicit in creating the conditions that have led to the current state of affairs.

Reconciliation



Effective use of support



Both before and after the 2006 revolt, Nepali governments would cooperate with international donors and agencies. The same is true for later governments. However, the Maoist-led governments may have put more emphasis on improving cooperation with China and increasing economic support from Beijing (the PRC continued to increase its support and, for example, increased budgetary assistance to Nepal). This is reflected in the increased aid from, and trade with China.

While Nepal receives a significant amount of international assistance, in the presence of weak governance and institutions, together with the lack of a long-term strategic development agenda, this assistance has made only a marginal economic impact.

Moreover, since the dissolution of the first CA in May 2012, international donors have progressively reoriented their agendas away from the issue of social inclusion (aside from gender equality) and since the promulgation of the new constitution in September 2015 great focus has been placed on implementation of the new document and the impending local elections.

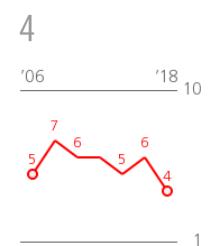
While Nepali governments have tried to present the country as a reliable partner over the years, its reputation as a credible and reliable partner is continuously deteriorating. This is largely due to the lack of political commitments and growing fights between the parties.

In terms of regional cooperation, the relationship with India has been at an all-time low due to the tensions over the Madhesi protests against the new constitution and the unofficial trade blockade. The government in Beijing has capitalized on the situation and supported the Nepal government during the crisis. However, China may see its interests threatened by the growing demand for ethnicity-based federalism in Nepal and continues to pressure the Nepali government to adopt a tough stance toward the Tibetan exile community.

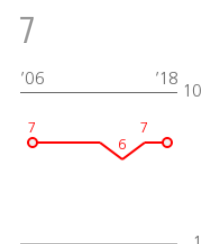
In recent years, Western governments (U.S., UK, and EU) have become increasingly disillusioned by continued selfish politics pursued by all parties and their leaders. The situation has been exacerbated by the delays on the part of the Nepal government to administer the earthquake relief funds. As a result, some local and international critics have suggested that donors should withhold aid in order to compel better performance from Nepali political actors.

The Kingdom of Nepal has only two neighboring states: India and the People's Republic of China. Historically, the relationship with India has been stronger, but the Maoist leadership has made new overtures to China in very recent years. Nepal has improved its relations with both in recent years. Nepal hosted the 2014 SAARC summit, the first such meeting since 2011. The summit itself, however, produced little by way of substantial results, except for the conclusion of a joint agreement on electricity. In 2014, newly elected Indian Prime Minister Modi visited Nepal, the first Indian prime minister in 17 years to make a state visit there. While the visit garnered

Credibility



Regional cooperation



a great amount of good will in Nepal, this soon dissipated when India supported the Madhesi protesters alongside an unofficial trade blockade at the Terai border.

Hydropower resources comprise the most significant axis of trans-regional cooperation, as well as contestation. China has increasingly funded hydropower projects, along with associated road construction, while India seeks to access hydropower produced by Nepal for purchase. Nepal contributes migrant labor to both countries, especially India, which remains the most popular site for Nepali workers even as new routes to the Middle East and beyond open up. The 1950 Indo-Nepal Friendship Treaty enables such mobility since it mandates an open border, but it also engenders disputes between the two countries over citizenship and security. The Sino-Nepali border is more rigorously policed by both sides, and China carefully watches Nepal's response to Tibetan activities within its borders.

Strategic Outlook

The main priorities for the government Nepal are to implement the 2015 constitution, accommodate the various disgruntled groups within the new political settlement and deliver economic relief after the devastating earthquakes of 2015.

Constitutional implementation requires the government to initiate the process of federal restructuring and set up the various bodies mandated by the new constitution. Moreover, elections will need to take place for all the three tiers of government, central, provincial and local, which are mandated by the new constitution.

The accommodation of various disgruntled groups entails the integration of newly emerging minority parties, the strengthening of state capacity, the development of a sustainable approach to reconciliation and transitional justice, and the distribution of relief funds. Moreover, the ability to manage conflict and cleavages needs to be improved, especially with regard to the newly emerging transnational proletariat that is spread across Nepal, India, the Gulf and Malaysia and has concerns distinct from the traditionally poor – and whose interests remain ignored by all major political forces. In addition, organized labor unions feel their interests have been sacrificed to appease business, not only by non-Maoist governments but also by the Maoist themselves. In addition, the rapidly expanding middle classes have not found an outlet for political articulation of their interests except social media and sporadic street protests. The marginalized groups feel that, despite investing so much energy in social movements, and faith in the CA, the traditionally dominant groups consolidated and conspired to deprive them of their rights. The traditionally dominant can see their powers and privileges slipping away, and feel unfairly victimized. There has not even been a token decision on land reform and agriculture modernization, leaving the landless and marginal farmers dissatisfied. Labor militancy and infrastructure gaps have left the business community in a more dismal state than five years ago. Reconciliation law left those who have borne the brunt of atrocities aggrieved about the lack of justice. However, given the questionable ability of the political leadership and the fragile and polarized party system, it remains uncertain if that can be accomplished in the near to midterm future.

As the political process moves forward, politicians and policymakers should work with the public administration and the international development community to attend to the country's fragile post-earthquake economic situation. It is also important that political parties and policymakers are made accountable for their acts. The business community should work with state regulators to shelter strategic long-term growth sectors, such as hydropower, from political interference, protecting and encouraging investment. New forms of public-private partnership should be considered that support both state and community initiatives, with donors and NGOs working in concert with the state whenever possible. Through this framework, creative mechanisms might be proposed to channel remittance inflow into civic organizations and long-term initiatives for broad-based development at village, district and national levels. In all of these processes, both the state and the international donors that support it should be consistent in their engagement with local actors, improving transparency and monitoring of implementation and impact over time.