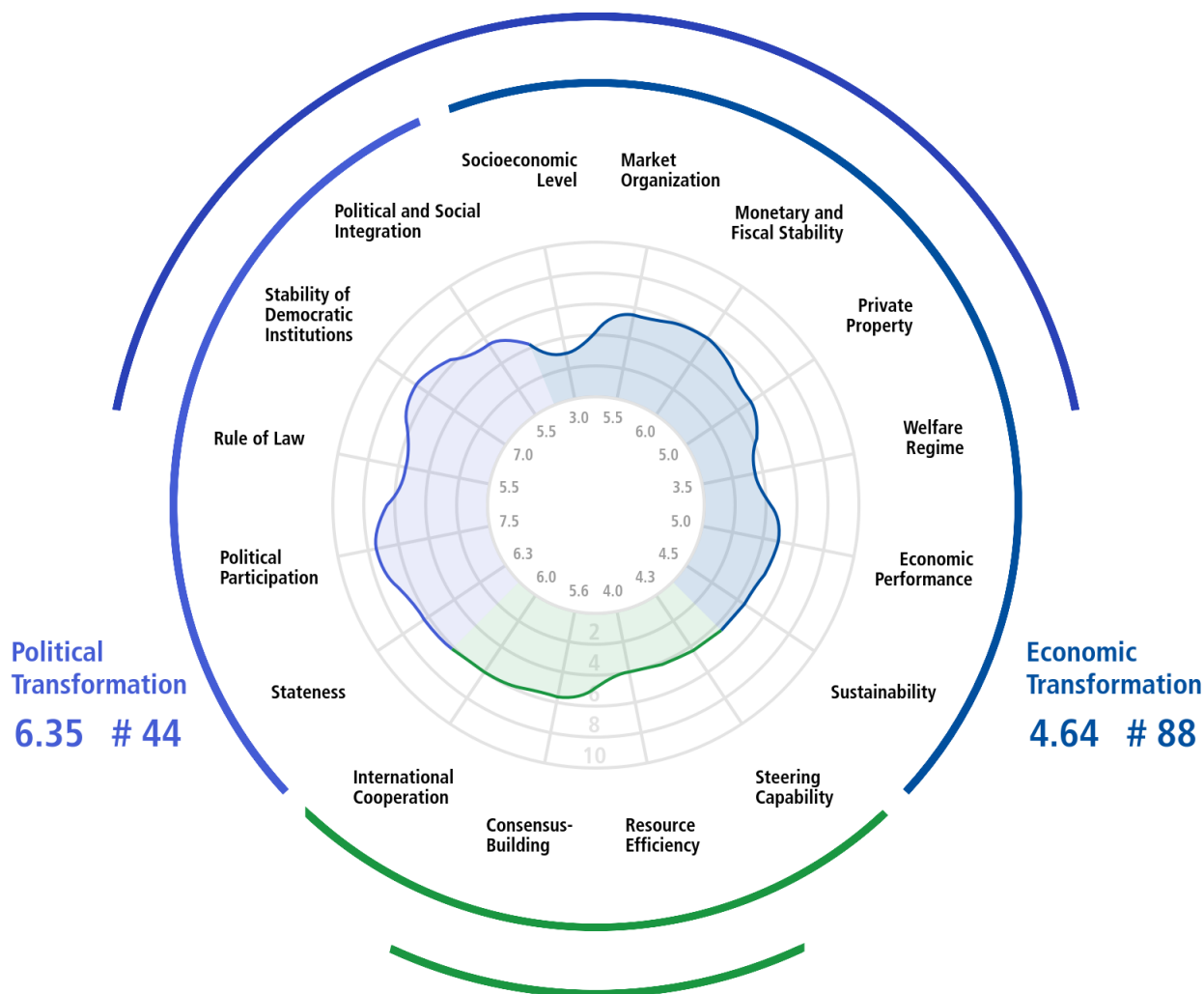


# Nepal

## Status Index

**5.50 # 61**

on 1-10 scale out of 137



## Governance Index

**4.60 # 73**

on 1-10 scale out of 137

This report is part of the **Bertelsmann Stiftung's Transformation Index (BTI) 2024**. It covers the period from February 1, 2021 to January 31, 2023. The BTI assesses the transformation toward democracy and a market economy as well as the quality of governance in 137 countries. More on the BTI at <https://www.bti-project.org>.

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**Key Indicators**

Population	M	<b>30.5</b>	HDI	<b>0.602</b>	GDP p.c., PPP \$	<b>4725</b>
Pop. growth <sup>1</sup>	% p.a.	<b>1.7</b>	HDI rank of 189	<b>143</b>	Gini Index	<b>32.8</b>
Life expectancy	years	<b>68.5</b>	UN Education Index	<b>0.529</b>	Poverty <sup>3</sup>	% <b>40.0</b>
Urban population	%	<b>21.5</b>	Gender inequality <sup>2</sup>	<b>0.452</b>	Aid per capita \$	<b>52.2</b>

Sources (as of December 2023): The World Bank, World Development Indicators | UNDP, Human Development Report 2021-22. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$3.65 a day at 2017 international prices.

## Executive Summary

There has been continued improvement in Nepal during the review period, despite significant obstacles to achieving sustainable governance and transformation. Post-pandemic, Nepal's leadership learned a variety of lessons and seems to have improved its state capacity. In 2022, it conducted local, provincial and national elections – the second round since the introduction of the 2015 constitution. These elections were free and fair and led to the formation of a government.

While Nepal's political situation has been relatively stable since the adoption of its 2015 constitution, Prime Minister K.P. Oli of the ruling Nepal Communist Party dissolved parliament in December 2020 and announced elections for April 2021. Immediately following this move, his party fragmented due to internal divisions. Concurrently, street protests erupted in response to Oli's seemingly self-serving actions. Surprisingly, representatives of the state's coercive machinery showed restraint, and the protests remained largely peaceful, indicating the potential for a new era in Nepali politics in which protest is tolerated and peacefully addressed.

Oli's actions launched a constitutional crisis, creating uncertainty as to whether Nepal would remain democratic. Eventually, the involvement of the Supreme Court resolved the crisis by reinstating parliament and installing Sher Bahadur Deuba of the Nepali Congress as the prime minister. Deuba took measures to institute stability leading up to the local, provincial and national elections, which occurred in May and November of 2022. All major players supported holding elections, respected the outcomes and approved democratic governance.

The dominant development in this election cycle was frustration over the political establishment and the rise of newcomers – many of whom were first-time, independent candidates with no political background or party support. The election outcomes were surprising. The new Rastriya Swatantra Party (RSP), or National Independent Party, won an unexpectedly high number of seats. The pre-electoral alliance between Congress and the CPN-Maoist Center dissolved after the election. The Nepal Communist Party, which had split up in 2020, somewhat reunited with the

CPN-Maoist Center, the CPN-UML and the RSP in an unanticipated post-electoral coalition. Although the RSP has since left the coalition (February 2023), the CPN-Maoist Center and CPN-UML are still in the coalition.

Economically, Nepal is beginning to recover from the impacts of COVID-19 but faces challenges due to a difficult global macroeconomic environment. However, unlike most other countries, in Nepal, the government has managed to keep inflation relatively low. In 2021, the country's GDP growth reached 4.2%, bouncing back from a pandemic low of -2.4%, while inflation remained at 4.1% (2021). Nevertheless, there was a slight increase in unemployment and tax revenues decreased, indicating the presence of economic headwinds. The stabilization of Nepal's economy relies heavily on domestic hydro-energy production and the return of remittance workers. Minorities and women continue to be disproportionately represented among the poor, partially due to specific affirmative action measures in place. Nepal still has a long way to go in terms of economic development, particularly with regards to trade liberalization, funding for education, research and development (R&D) and the promotion of industrial economic growth.

Challenges remain on the governance front. Nepal faces a remarkably challenging structural environment. Although poor governance structurally contributed to poverty and economic stagnation, recent years provide hope for Nepal's future. The pandemic tested Nepalese governance. While its steering capability and resource efficiency remain relatively poor, it has made infrastructural advancements lately, such as completing the Melamchi Pipeline and opening a second international airport at Pokhara, among other accomplishments. Still, governance challenges prevail, including border issues with India and China, despite efforts to maintain steady relations.

## 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, the political system in Nepal was an authoritarian monarchy based on an exclusive and oligarchic social order. However, a pro-democratic people's movement in 1990 led to the downfall of the royalist Panchayat system and resulted in the transformation of Nepal into a constitutional Hindu monarchy and multiparty democracy.

This transition did not establish a stable, well-functioning, consolidated liberal democracy, however. Instead, a Maoist rebellion erupted that found widespread support, especially among Nepal's impoverished, disadvantaged rural population, much of which experienced neglect by the state. This conflict contributed to a further democratic decline and the start of an era of human rights issues in the country. In 2001, King Birendra and almost the entire royal family were murdered under mysterious circumstances, and the dead king's brother, Gyanendra, was crowned king on June 4, 2001. Support for the monarchy waned even among royalists after this event, as Birendra was respected and Gyanendra was not.

Gyanendra failed to garner public support for the continuation of a constitutional monarchy in Nepal. Dissatisfied with the government's inability to effectively combat the Maoist insurgents, Gyanendra executed a royal coup in 2005, asserting complete sovereignty and acquiring executive power. In response, a widespread opposition movement formed, comprised of the Seven Party Alliance (SPA) and the Maoist insurgents. Ultimately, in April 2006, a broad-based, anti-regime resistance organized by the main opposition parties and civil society compelled King Gyanendra to restore the parliament.

The newly formed multiparty government concluded a comprehensive peace agreement with the Maoists, opening the way for an interim constitution that came into force in January 2007. It took an additional year before popular elections to a Constituent Assembly (CA) occurred – in April 2008 – with the CPN-Maoists emerging as the strongest party. In May 2008, at the CA's first meeting, the monarchy was abolished and the interim constitution was amended to institutionalize Nepal as a federal democratic republic.

In the years that followed these elections, old power struggles between many of the same political leaders reemerged and it became clear that there was no consensus on which institutions should govern Nepal going forward. It should not be surprising, then, that after four extensions of its initial two-year tenure, the CA was dissolved without promulgating a new constitution. None of the three governments during this period were able to break the constitutional deadlock.

In November 2013, a caretaker government succeeded in holding new elections for the CA. These elections saw an impressive comeback of the Nepali Congress, which was the main opposition party at the time and the ruling party for much of the period from 1990 to 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 had made little progress in drafting the constitution when, in April and May of 2015, two devastating earthquakes hit Nepal, causing many casualties and severe economic and infrastructural destruction. Awful as these events were, the natural disasters served as catalysts, and Nepal's political leaders fast-tracked the drafting of a new constitution. Amid considerable controversy, violent protests in the Terai and an unofficial blockade of the border with India, the new constitution was eventually promulgated on September 20, 2015. The document backtracked on many of the achievements of the interim constitution, especially regarding social inclusion. In October 2015, CPN-UML leader K.P. Oli became the new prime minister.

In August 2016, an unusual Congress-Maoist coalition took power. The coalition agreed to run the government and share the prime ministership in tandem as it oversaw local, provincial and national elections. Maoist leader Pushpa Kamal Dahal took the helm first, overseeing the first phase of local elections. In June 2017, he voluntarily handed power to Sher Bahadur Deuba of the Nepali Congress to oversee the latter two phases of local elections, as well as the provincial and national elections later that year. Though some pre-electoral violence took place, elections for all levels of government were hailed as free and fair, and newly elected representatives took their seats, marking a watershed moment in Nepal's political transformation.

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

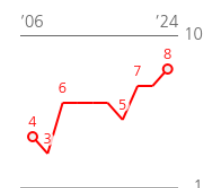
After many years of crisis, the state's monopoly on the use of force appears to have become stronger in many parts of the country. The end of the conflict, the peace process, and the 2008 and 2012 constituent assemblies have provided a platform for wide-ranging public debate about the real and ideal nature of Nepali stateness. Overall, political violence in Nepal has continued to decrease since 2019. There are no threats to the territory and the state's monopoly on the use of force by insurgencies or militant factions. However, a large number of demonstrations have been reported in Nepal, with a 16% increase in 2021 over the previous year. More significantly, there has been a 100% escalation rate since 2018. During the enforcement of COVID-19 restrictions, there were reports of notable police brutality, including 70 violent confrontations and assaults within a year. Significant, violent human rights violations occur in connection with domestic violence and human trafficking. Although criminal organizations are believed to exist in Nepal, they have posed no significant threat to territorial integrity during the review period.

From Nepal's creation in the late 18th century through the Maoist conflict, stateness has been linked with the religion, language and culture of the upper Hindu castes (Tagadhari). This was especially true for 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. Though the Maoist insurgency contested control over the state and dramatically undermined its monopoly on violence, no major group contested Nepal's statehood. With the promulgation of the 2015 constitution and successful elections in 2017 and 2022, stateness has become reinforced. Power is shifting geographically away from those who have traditionally wielded it, particularly with the recent rise of the Nepal Independent Party.

Question  
Score

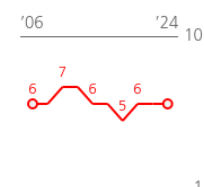
Monopoly on the  
use of force

8



State identity

6



In 2015, a new constitution came into force and two rounds of national, provincial and local level elections have been held since. With time passing since the conflict, the protests over the 2015 constitution and the unofficial blockade of the border with India, which was resolved in early 2016, political contestation appears to have largely shifted to the electoral arena, with a wide variety of groups vying for political power there (as opposed to in the streets or through violent means).

While the 2015 constitution fell short of the more inclusive aspirations of the 2007 interim constitution draft and, to some degree, reinstated exclusionary ethno-cultural nationalist narratives, it is largely accepted among politicians and the population. It includes a version of secularism that calls for “special protection for sanatana (Hinduism)”; reiterates the long-standing ban on religious conversion; features discriminatory citizenship provisions on the basis of gender; introduces a new category, Khas-Arya, into the quota system; and reduces the quota of parliamentary seats elected under proportional representation. However, quotas still exist for marginalized groups and women. The constitution also establishes “all the mother tongues spoken in Nepal” as the official language(s) of the nation, with Nepali as the language of official transactions. Provinces are allowed to select one or more local languages, other than Nepali, in which to conduct official business. In practice, thus far, Nepali has remained the dominant language in most official proceedings.

People of Indian ancestry living in the Terai (commonly known as Madhesis), members of numerous ethnic groups (Janajatis), women and the untouchable castes (Dalits) continue to face substantial legal, economic and social discrimination from high-caste Hindus (often referred to as “hill elites” because they live in the central hill region). The latter still hold dominant positions in the bureaucracy, political institutions and Nepal’s complex socioeconomic system.

Many public officials continue to maintain fairly strongly held beliefs that Nepali citizenship should be defined by proficiency in the Nepali language and adherence to the Hindu religion. Such attitudes, largely rooted in the recent past when Nepal was officially a Hindu Kingdom, 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. More recently, there has been an expansion of citizenship so that Nepali women can now more readily pass citizenship onto their children. Furthermore, the reform seems to apply to foreign-born husbands, and it appears, from recent election results, as if the voting public is open to representation by a wider variety of individuals than in the past. However, a Citizenship Amendment Bill that was passed twice by the parliament in 2022 to bring the citizenship law into compliance with the constitution, was not ratified by the president, which may have been an unconstitutional move. The present government intends to table the bill again in 2023.

The 2015 constitution defines the Nepali state as secular, which is a significant improvement from Nepal's previous status as the world's only Hindu kingdom, despite de facto religious diversity on its territory. However, according to the constitution, "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 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. Laws adhering to religion have remained consistent over the review period. In Nepal, the legislation makes it easier for Hindu organizations than for other religious groups to obtain legal recognition. There were certain improvements regarding religious laws in 2021, improving Christians' and Muslims' ability to buy land and establish or enlarge existing cemeteries. One setback has been the difficulty of entering into inter-religious marriages due to various cultural and social constraints. Progressive political forces and activist lawyers are diligently trying to reform the legal system, but changes remain incomplete.

No interference of religious dogmas

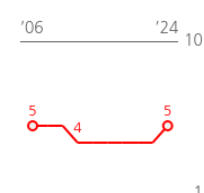
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The administrative system is riddled with corruption and urgently in need of reform. As in most South Asian countries, in Nepal, various indicators, such as the ability of the state to tax the economy, indicate weak state capacity. Indeed, many Nepalis, even those who can afford to do so, try to avoid paying taxes because they believe their funds will be misused. While the state's administrative structure extends beyond maintaining law and order, the country's administration is also weak and largely unable to provide equitable access to administrative services for all citizens, particularly in rural areas, though the situation has improved substantially. Citizens seeking to avail themselves of basic state services such as birth and death registration, health care, education and legal redress, in particular, encounter complex procedures over which individual political and administrative actors often have discretionary influence.

Basic administration

5



World Bank data indicates that 89.9% of people in Nepal have access to electricity. However, areas that require significant attention include access to basic resources, such as water and sanitation. According to UNICEF, 10.8 million Nepalese citizens lack access to improved sanitation, and 3.5 million have no access to basic water services. In 2022, the World Bank signed an \$80 million project with the government of Nepal, focused on improving water supply and sanitation services across the country. The aim is to implement the Water Sector Governance and Infrastructure Support Project in towns and rural municipalities in the regions of Karnali and Sudurpashchim.

A general restructuring of the civil administration is underway to adapt Nepal's administration to the country's new federal structure. For the most part, it is a functioning federal democracy. With the shift to a federal structure, decision-making has been decentralized to some degree, and local administrations have taken on



significant new responsibilities, such as health care and education. However, significant capacity deficits exist, and the federal level continues to exert considerable influence and control over local and provincial authorities.

## 2 | Political Participation

The 2022 local, provincial and national elections were the second since the promulgation of the 2015 constitution. Though the period leading up to the elections was not without conflict, both the local elections in May and the provincial and national legislative elections in November took place without major electoral violence. Access to media outlets was reported to be fair to a great degree, with subsidized and free media access for parties. However, one of the most common forms of media relied on for elections was social media. Due to the fact that social media remains unregulated, there is no certainty regarding fair and equal access to social media platforms for campaigning. Additionally, subsidized or free media access may not be considered effective in places where campaigning largely relies on unregulated, door-to-door visits to engage directly with voters. Despite this, the Election Commission of Nepal is competent, and the elections were widely considered to have been free and fair. Voter turnout was 61% for the November federal and provincial elections, and 64% for the May local elections. Compared to the 2017 elections, there was only sporadic pre-electoral violence, though security forces were deployed to ensure free and fair elections. The Kathmandu Post elaborated that the elections overall remained peaceful, despite rare violent clashes. Voting was generally equally accessible to all eligible citizens, and active participation was encouraged. The Madhesi parties that threatened to boycott in 2017 confined their contestation to the electoral arena, and the issue of Madhesi secession appears to have become less volatile than previously. On the whole, the small degree of electoral violence in 2022 did not prevent the elections from being accessible and secure, and ballots remained secret.

Free and fair elections

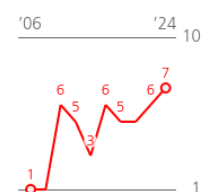
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Since the November 2013 elections to the second CA and the promulgation of the new constitution in 2015, democratically elected political representatives have had the effective power to govern. Their power remained somewhat constrained, however, due to various groups threatening to exercise veto power. More recently, however, no such contestation is evident.

Effective power to govern

7



The merger of the former CPN-M with the CPN-UML to form the Nepal Communist Party in 2018 marked a major milestone in terms of the CPN-M's move away from a veto player status. The merger dramatically split up in late 2020, and Prime Minister Oli precipitated a constitutional crisis by dissolving parliament. After widespread and overall peaceful protests, the crisis was effectively resolved by the Supreme Court in 2021.

While the Nepal Army (NA) was previously seen as a veto player, this is no longer the case. Over 1,400 former People’s Liberation Army (PLA) combatants have been integrated into the NA, making Nepal one of the few successful instances of post-conflict army integration worldwide. Concerns about a military coup have receded from public consciousness.

Other potential veto groups, such as large landowners and business elites, enjoy sufficient access to political parties and can thus try to influence policymaking through institutionalized politics. They therefore do not count as “veto groups” as defined in the BTI Codebook.

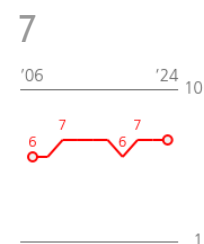
Finally, there are potential veto actors at the local levels, such as landowners, traditional elites, groups or individuals with control over means of violence and coercion. Though the political system has decentralized over time, these actors do not appear to be exercising a veto over local democratic decision-making.

Freedom of association and assembly is guaranteed under Article 17 of the 2015 constitution. Individuals in Nepal are free to join political and civil society groups, and many people possess multiple affiliations. That said, the constitution allows for “reasonable restrictions” to be imposed by ordinary laws in an extensive range of circumstances. During the protests in 2021, in response to Prime Minister Oli’s dissolution of parliament, coercive forces were restrained, and no substantial violence occurred. In general, groups operate freely, and mass rallies and activities are common both in urban centers and far-flung district headquarters. While activity of this variety was tempered by COVID-19-related restrictions, the 2021 protests demonstrated that the restrictions did not hamper the groups in the long term.

An exception to this pattern is found in public events involving the Tibetan community. While they lead lives in Nepal free of most restrictions, members of this community have sometimes been detained and arrested for staging protests and holding cultural festivals that mention the Dalai Lama. This distinct treatment is largely due to Chinese pressure on Nepal, which leads the state to not treat Tibetans equally, despite the implicit violation of international law in which the country engages.

Freedom of opinion and expression is guaranteed under Article 17 of the new constitution. In 1990, Nepal was the first South Asian country to constitutionally recognize the right to information (RTI) as a fundamental right. Still, the constitution allows for “reasonable restrictions” to be imposed by ordinary laws in an extensive range of circumstances. Recently, there have been no high-profile incidents in which freedom of expression has been curbed, which stands in contrast to events described in the previous report. Then, the arrest of Madhesi activist C.K. Raut on sedition charges and the deportation of Canadian citizen Robert Penner both occurred on the grounds that their speeches were disturbing Nepal’s social harmony and threatening national unity. In general, free expression is enjoyed by most in Nepal. An additional RTI Act was implemented in 2021, mainly aiming at effective RTI enactment.

Association /  
assembly rights



Freedom of  
expression



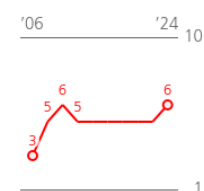
Nepal has a vibrant media landscape, with many newspapers in Nepali, English, and several ethnic and regional languages. A much-improved electric grid, complemented by satellite and mobile technology, has allowed many Nepalis to access social media, where many diverse voices are increasingly heard at the local, provincial and national levels. The 2022 Reporters Without Borders Press Freedom Index ranked Nepal at 76th out of 180 countries, compared to a rank of 120 out of 180 countries in 2014.

### 3 | Rule of Law

Nepal's 2015 constitution expressly provides for the separation of powers in Article 56. The principle is embedded at the level of institutional design, from the creation of three separate branches of government to extensive mechanisms intended to ensure compliance. There has been a formal system of checks and balances in place since 2000, with the provision of constitutional supremacy. The executive branch of government in Nepal is responsible for implementing legislation and order. It is also known as the Council of Ministers or Cabinet of Ministers. The executive has four main functions, including administrative functions, diplomatic functions – relating to foreign aid and foreign relations, financial mobilization and management, and army-related functions. The legislative branch of the government makes new laws, alters old ones and passes budget and tax bills implemented by the executive. The legislature can also raise concerns regarding the executive's policies and programs. The constitution weakens the judiciary's power slightly, especially as compared to the previous interim constitutions. Impeachment proceedings against Supreme Court justices can be initiated, and there is now a separate constitutional bench within the Supreme Court that reviews legislation. In practice, the institutional capital associated with Nepal's judiciary, especially vis-à-vis the other branches, has allowed it to withstand these relatively minor changes. Its effective resolution of a constitutional crisis in 2021 suggests that the separation of powers is functional. Nevertheless, problems remain, particularly regarding the executive's compliance with judicial orders. This became evident during the COVID-19 pandemic, when the administration did not comply with the restrictions imposed by the Supreme Court. Furthermore, in recent years, there has been criticism against Chief Justice Cholendra Shumsher Rana, who allegedly demanded a position in the executive cabinet while serving in the judiciary. This has damaged the perception of the institution's legitimacy and credibility.

Separation of powers

6



The institutional design of Nepal's judiciary is similar to that of other federal democracies, and particularly to that of India. There is now an independent three-tier judicial system, consisting of the Supreme Court, a high court for each province and a district court for each district. The Supreme Court is the highest court of the country and hears appeals from high courts, while high courts hear appeals from lower courts. The 2015 constitution also provides for a constitutional bench in the Supreme Court that can review legislation, which has now been implemented and begun work. The Supreme Court is weakened by an impeachment procedure in the 2015 constitution, which has a lower threshold than in previous constitutions. The nascent Judicial Council, which handles important issues relating to the judiciary, appears to be adding a layer of protection to the courts.

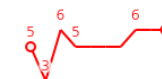
The Supreme Court has historically not shied away from displaying its independence and power. It recently impeached several political leaders on corruption charges and made several courageous decisions concerning transitional justice, citizenship, quotas, etc. The recurring problem the court faces, however, is compliance by other institutional actors with its verdicts. For example, the executive sometimes flouts them completely and, at other times, reluctantly complies, dragging its feet in the process. Civil society has been instrumental in forcing executive compliance in a number of instances. Recently, the Supreme Court settled the constitutional crisis in 2021 but also became mired in a crisis of its own when the Nepal Bar Association called for the resignation of Chief Justice Rana on grounds of corruption. Despite the claims, he refused to resign and remains on the bench.

The court system in Nepal remains inaccessible to most Nepalis due to insufficient geographical proximity to courts and scarce resources, both within the system and among many citizens. This is changing with decentralization. Justices of the Supreme Court are appointed by the president based on recommendations from the Judicial Council. They must be Nepali citizens, have a bachelor's degree in law and have worked as gazetted second-class officers in judicial service for at least four years. However, the judicial system suffers from several problems. The functional capacity of Nepali judges remains somewhat limited due to a lack of experience and training. Citizen awareness of the judicial process is low, and delays in the system contribute to widespread frustration with the courts and their inability to provide justice. Corruption is also a problem. According to the Nepal Bar Association, corruption is deeply rooted and particularly problematic in courts of first instance. Altogether, a large number of pending cases, delays in the implementation of court decisions and controversial appointments contribute to the overall impression that the judiciary must considerably improve before it can be considered fully independent.

Independent  
judiciary

6

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1

Civil society in Nepal has long described the climate in the country as being one of impunity. In a still relatively weak state with weak judicial capacity, the rule of law and protection of human rights are improving but still inconsistent. Certain aspects of the 2015 constitution contribute to this problem. For instance, the president has unrestricted authority to grant pardons. Consequently, the political elite rarely faces consequences for illegal actions. Nepal has also failed to prosecute the well-documented conflict-related crimes committed during the civil war. While over 60,000 individuals have reached out to Nepal's Truth and Reconciliation Commission and the Commission on Investigation of Disappeared Persons to report disappearances and crimes committed by the Maoists, the security forces and the political leadership, few cases have been investigated at all, and in none has an investigation been completed. This, according to many, including the U.N. High Commissioner for Human Rights, is because Nepal's transitional justice system still allows for full amnesty. Nepal's Supreme Court has ruled that the courts must provide justice in cases of conflict violations, invalidating the provision for amnesty, but the government has largely ignored this ruling. Considering this, it is hardly surprising that some have resorted to suing perpetrators in foreign courts. For instance, Colonel Kumar Lama was prosecuted for torture in the UK but acquitted in 2016. Others continue to live without much fear of prosecution. At this point, it seems unlikely that transitional justice will happen.

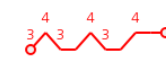
Corruption is often part of politics and business in Nepal. Funds, including aid money, continue to be misappropriated at all levels of government, and corruption scandals frequently make the news. Most political parties dispense patronage to members and supporters, both in terms of material resources and administrative favors, and company directors learned to function in such a system long ago. Many would say that corruption is bad and should be halted, but few have taken steps to stop the practice.

However, in some regards, progress has occurred. Nepal's anti-corruption body, the Commission for the Investigation of Abuse of Authority (CIAA), has arrested and jailed high-level government officials and politicians on corruption charges. The institution appears to be gaining momentum and, over the past few years, has started to adopt a life on its own, conducting numerous sting operations, stirring fear in those who continue corrupt practices and taking up a wide variety of cases. Overall, however, many corrupt officeholders and authorities who abuse their offices do so without fear of legal consequences.

Prosecution of  
office abuse

4

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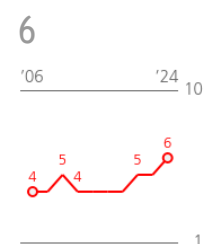
Nepal's 2015 constitution provides full protection for civil and political rights, and an impressive array of economic, social and cultural rights. Unfortunately, some of these are largely unsupported by various branches of government. Sexual and gender-based violence remain very prominent in Nepal, with 48% of women stating that they have experienced some form of violence in their lives. Sexual violence often goes unpunished, although this is changing. Discrimination based on the caste system, especially targeting low-caste Dalits, remains a significant problem, and cases often go unreported. Even when the cases are reported, very few actually result in any official action. The practice of child marriage is also very widespread, despite being prohibited by law: 40% of girls in Nepal are married by the age of 18, and 7% of girls are married under the vulnerable age of 15. COVID-19-related health care and vaccines were more easily accessed by those with wealth and status than those without wealth and status. Generally, levels of protection continue to depend on class and caste status. Lately, the police have shown considerable restraint in their response to political protests. While protests responding to Prime Minister Oli's dissolution of parliament in 2021 were widespread, they were almost entirely peaceful. Many are hopeful that grievances will now largely be dealt with through formal procedures, be it politically or judicially.

There are several organizations at the local and national level in Nepal that seek to reduce human rights violations. Notable among these are the Human Rights Organization of Nepal, the Terai Human Rights Defenders Alliance, The Advocacy Project and Amnesty Nepal. Unfortunately, these human rights organizations remain limited in their ability to make a difference. Recommendations from state actors, including the Judicial Commission, are sometimes considered but never implemented by the government.

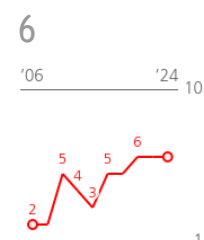
#### 4 | Stability of Democratic Institutions

Democratic institutions exist at the national, provincial and local levels and are stabilizing after a period of contestation. From the CA election in November 2013 until the recent 2022 elections, Nepal has had numerous prime ministers. These leaders led unstable coalitions, leading to largely incoherent and ineffective policymaking. After the legislative elections of 2017, which saw the success of a leftist alliance comprising the Communist Party of Nepal (UML) and the Communist Party of Nepal (Maoist Centre), Khadga Prasad Oli became prime minister for a second time after 2015/2016. As the leftist alliance was falling apart, Oli dissolved parliament in what many saw as an attempted power grab. The Supreme Court restored parliament, and Sher Bahadur Deuba (of Nepali Congress) was installed as prime minister. He finished his term by successfully conducting local, provincial and national elections in May and November 2022. The results of those elections left no clear victor. Nepal's various political parties struggled to form a government until former Maoist rebel leader Prachanda switched sides and became prime minister in late December. Citizens are generally now able to express dissatisfaction through existing institutions.

#### Civil rights



#### Performance of democratic institutions



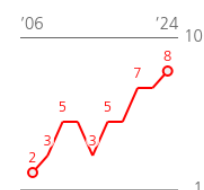
The vested interests of political party members continue to undermine democratic effectiveness. Patronage and clientelism remain relatively common, undermining the equitable provision of public goods and fair appointments to offices. The Bayesian Corruption Index (BCI), an index on which 100 indicates high corruption, placed Nepal at 54.3 in 2017, the last year it was calculated for Nepal. This can be compared to 28.2 in the United States, 15.8 in the United Kingdom and 41.4 in India. It should be noted that Nepal's corruption level, according to the BCI, decreased from the time period of 2005 to 2011, when scores ranged from 60.0 to 160.5. This change points to a movement toward a less corrupt and more institutionalized system of governance than previously existed. A recent trend toward independent candidates running for and winning elections also points to a shift away from control by vested interests.

In 2022, Nepal successfully conducted local, provincial and national-level elections that were generally seen as free and fair and associated with relatively low levels of violence. Nepalis largely consider elections as the proper arena for political contestation. Disadvantaged segments of society have acquired a voice in the process, thanks to the proportional election system quotas. These provisions have now been reduced under the new constitution, but they still play a role in the higher echelons of many political parties. However, this may change with the influx of independent candidates and popular dissatisfaction with traditional parties, which continue to suffer from weak democratic structures and norms.

The vast majority of political actors support the 2007 agreement on democratic transition and institutions. Support has increased secularly since 2007, as confirmed by the institutionalization of elections in the period since the conflict. Even the Madhesi parties, which threatened to boycott the 2017 local elections made no such threats in 2022. Among international organizations, the United States Agency for International Development (USAID) strongly advocates for democracy in Nepal by emphasizing “inclusive citizen participation and government accountability” and partnering with the government of Nepal. Other such institutions include the National Democratic Institute and local organizations that promote democracy. Overall, the response to democracy has been relatively positive and has led to favorable developments in the country.

Commitment to democratic institutions

8





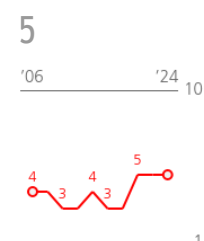
## 5 | Political and Social Integration

The political party system remains fairly factionalized, polarized and elite-dominated, even though disadvantaged groups are increasingly represented in the legislature due to proportional representation. Since the 2022 local elections, women hold 41.21% of elected positions in local councils and ward committees; many are political newcomers and/or Dalit. Furthermore, women make up 33.1% of parliament. However, unequal access and representation still exist in key parts of the government, political parties, administration, judiciary, media, the education system and in business. The recent influx of candidates running as independents suggests turbulence for the party system. The fact that this trend is popularly supported and does not carry the risk of much violence is promising.

The traditional parties – the Nepali Congress and various factions of the CPN – have strong social roots but continue to face difficulties recruiting and maintaining loyal cadres from Dalit and Janajati backgrounds. Furthermore, they lack adequate democratic and participatory mechanisms. Most political parties remain personality-oriented organizations with internally authoritarian power structures. Though power is typically concentrated in the party headquarters in the Kathmandu Valley, decentralization and competition from independent candidates have led many established politicians to spend more time in their constituencies and to focus more on local interests than they did before. Popular support for and trust in various political parties varies widely from year to year, as indicated by the Himalmedia Public Opinion Poll, with a strong trend in 2022 away from established parties. The success of the new Nepal Independent Party (NIP) suggests that the power structure has shifted.

In recent years, several new parties have emerged. These are largely organized around regional or ethnic affiliation, but also around ideology. The new NIP, which won a substantial number of seats in the 2022 elections, is neither identity-based nor ideologically coherent but represents a move away from the establishment. Some civil society organizations are accepted as more legitimate than others. Some maintain explicit political allegiances, and some even have political alliances, even if these are mostly hidden from the public. In addition, many ethnic and regional identity-based groups continue to perceive existing political parties as not fully representative since they seek to keep power in the hands of long-dominant, upper-caste Hindus. In contrast, elites view many regional and ethnic parties as exclusionary and potentially threatening to national unity. But this view has shifted as elite parties have become focused on electoral contestation.

Party system

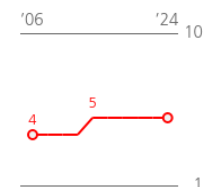




Since Nepal's transition to democracy in the 1990s, civic organizations and interest groups have established and taken root in society. These include labor unions, community-based groups, local NGOs and organizations for women's rights, which now play a role in representing social interests and mediation. Organizations such as the Nepal Federation of Indigenous Nationalities, the Nepal Bar Association, and the Federation of Nepali Journalists have exercised significant influence by fostering public debate and pressing for political commitments. 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, delivering services and/or exerting a strong influence in policy arenas. Such organizations also serve an important mediator role between citizens and policymakers. However, the effectiveness of these INGOs and NGOs is questionable, and, to some degree, they may undermine state capacity. Recent reporting suggests that interest groups have the power to exert heavy influence on Nepal's parliament.

#### Interest groups

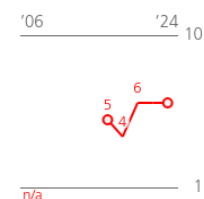
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The 2017 and 2022 elections seem to demonstrate that Nepali citizens largely understand and value the democratic process. While the promulgation of a controversial constitution, protracted protests in the Terai, slow progress on post-earthquake reconstruction and slow advancements on the transitional justice front may have weakened support for democracy in Nepal from 2015 to 2017, recent successful elections and the subsequent transfer of power between governments generate the impression of effective democratic institutionalization. While there is deep frustration with existing power structures and particularly with political parties that belong to the “establishment,” there is also excitement about political newcomers and enough participation to suggest that disaffection is not yet a problem.

#### Approval of democracy

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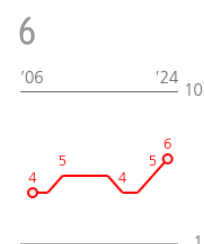
Country-level studies on the level of trust, strength and forms of social capital in Nepal are limited. The Asia Foundation's 2020 Survey of the Nepali People is the most recent effort at gathering data on trust in public institutions. It shows that trust in the media and local-level organizations is relatively high, and trust in national-level institutions has improved, except for trust in political parties. Other data exists as anthropological, ethnographic and subnational studies of social capital in Nepal. It remains uncertain if these insights can be viewed as representative of the whole society.

An often-cited survey (Himalmedia Public Opinion Poll 2013) suggests that the long-standing inability of high-level political actors to ensure the continuity of democratic institutions contributes to relatively low levels of public trust. This same survey was conducted in 2015 before the creation of the new constitution. Then, more than half of the respondents perceived Nepal's democracy to be in danger, and 46.8% of respondents stated that the condition of the country had worsened compared to previous years. While the 2018 iteration of the survey suggested continued disillusionment (especially with political parties), 43% of respondents reported that

government service delivery had already improved in the seven months since elected municipal and village councils assumed control of local governments. The Asia Foundation's Survey of the Nepali People in 2020 confirmed this trend and suggested increased trust in the federal government, federal parliament, provincial assemblies and local representatives, but decreased trust in political parties. All things considered, the data suggest that civil society may be productively intermediating between society and government, but that political parties are not particularly helpful in this regard.

Associational activities have improved in the last 30 years. Networks of cooperation and mutual support are well-developed, not only along political party, business and alumni lines, but also along ethnic, caste and regional lines. In many localities, such organizations filled the gaps that might otherwise have been filled by effectively decentralized state agencies. As decentralization has occurred, local governments have started to collaborate more with local associations and even reassume some traditional state activities. Concerning perceived relations with other people in a community, the Survey of the Nepalese People 2022 (The Asia Foundation) finds that 67.5% of people consider relations the same as before and 30.3% better than before. In 2020, the same survey found that 39.2% consider their relationship with other people in their community better than before. This decrease suggests that social capital has weakened in the past two years but is still relatively high. Many associations in Nepal act to further the interests of a specific group, whether defined in ethnic, religious or regional terms. Therefore, it could be argued that these networks might reproduce bonding social capital instead of bridging social capital and therefore do not support the formation of civic self-organization. However, Nepali youth seem much less inclined than their elders toward bonding social ties and initiatives such as the United Nations Development Program's (UNDP) Social Cohesion and Democratic Participation Program's (SCDP), which actively work to promote social cohesion and trust across community lines. According to the SCDP's 2019 Annual Progress Report, nearly 108,000 youth, women, marginalized groups, civil society members, government officials, political leaders and journalists have participated in their program to promote social cohesion through 550 community-level initiatives. Public surveys report a significant increase in Nepalis' positive outlook, with over 65.6% of citizens expressing optimism about the direction in which the country is progressing. Trust in Nepali institutions reached a high of over 91.8%; however, on the opposite end of the spectrum was trust in political parties, noted at approximately 56%. Given the entrenched caste system, developing solidarity among citizens continues to require focus and effort.

Social capital



## II. Economic Transformation

### 6 | Level of Socioeconomic Development

Socioeconomic exclusion remains a problem in Nepal. It is one of the poorest countries in the world, with a per capita gross national income (PPP) of about \$4,280 (2021), according to World Bank statistics, and a per capita gross domestic product (PPP) of \$4,261 (2021). Remittances have long represented and continue to represent a significant part of Nepal's revenue, estimated at 24.25% of GDP in 2020. According to the UNDP's Nepal Human Development Report 2020, the country ranked 143rd out of 189 countries, with a human development index (HDI) score of 0.602 (2021). Nepal's current HDI ranking places it behind Bangladesh (129) but ahead of Pakistan (161) and Afghanistan (180) in the region.

Detailed data provide further insights into Nepal's socioeconomic development. In 2021, Nepal's National Planning Commission (Multidimensional Poverty Index) reported that 17.4% of the population lives below the national poverty line. Several years ago, the World Bank indicated that the 2015 earthquakes directly caused an additional 3% of the population to fall into poverty. This could mean that up to one million additional people became poor. Recent data indicate that these natural disasters only had a minor impact on poverty reduction.

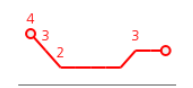
The UNDP Human Development Report, relying on World Bank data, continues to identify a Gini coefficient of 32.8 for Nepal, ranking it 145th out of 189 countries. However, this is 2010 data, so it should be understood as dated and taken with a grain of salt. The UNDP Gender Inequality Index for Nepal is 0.452, ranking it 113th out of the 162 countries in the 2021 index. Socioeconomic inequalities in Nepal based on gender, caste, ethnicity, language, region and sexual orientation remain structurally ingrained and pervasive, though gender dynamics have changed dramatically over the last 15 to 20 years. Long-standing social hierarchies continue to restrict access to political influence and economic opportunities for many marginalized groups. For instance, despite improvements in gender equality, Nepal ranks 96th among 146 countries in the Global Gender Gap 2022. This places Nepal above Sri Lanka (102), India (135) and Pakistan (153).

Question  
Score

Socioeconomic  
barriers

3

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Economic indicators		2019	2020	2021	2022
GDP	\$ M	34186.2	33433.7	36924.8	<b>40828.2</b>
GDP growth	%	6.7	-2.4	4.8	<b>5.6</b>
Inflation (CPI)	%	5.6	5.1	4.1	<b>7.7</b>
Unemployment	%	10.6	13.1	12.2	<b>11.1</b>
Foreign direct investment	% of GDP	0.5	0.4	0.5	<b>0.2</b>
Export growth	%	5.5	-15.9	-21.3	<b>34.1</b>
Import growth	%	5.8	-20.8	18.8	<b>15.1</b>
Current account balance	\$ M	-1753.6	-84.1	-5363.0	<b>-2470.6</b>
Public debt	% of GDP	34.0	43.3	43.3	<b>43.1</b>
External debt	\$ M	6513.5	7906.2	8856.0	-
Total debt service	\$ M	282.9	275.0	280.0	-
Net lending/borrowing	% of GDP	-4.8	-4.9	-4.0	-
Tax revenue	% of GDP	19.8	15.8	17.5	-
Government consumption	% of GDP	8.1	9.1	8.3	<b>8.5</b>
Public education spending	% of GDP	3.5	4.2	4.0	<b>3.6</b>
Public health spending	% of GDP	1.1	1.6	-	-
R&D expenditure	% of GDP	-	-	-	-
Military expenditure	% of GDP	1.2	1.3	1.2	<b>1.1</b>

Sources (as of December 2023): The World Bank, World Development Indicators | International Monetary Fund (IMF), World Economic Outlook | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database.

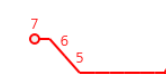
## 7 | Organization of the Market and Competition

Market forces in Nepal have been associated with inconsistent outcomes. Price hikes and artificial shortages related to basic goods are common and often tied to Nepal's limited arable land, growing population and historical dependence on imports from India. Nepal's landlocked position often presents a challenge to new businesses that would like to enter the market. The primary port for imported goods is in the Indian city of Kolkata. Airport transport also remains difficult because there is only one international airport in Nepal. According to the International Trade Administration, U.S. firms and other foreign investors have pointed out corruption as an obstacle

Market organization

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to maintaining any investment in Nepal, let alone expanding it in the long term. This corruption is allegedly evident when acquiring permits and approvals for businesses and during the awarding of contracts. The labor market also remains largely informal. Open borders allow cross-border mobility of labor between India and other neighboring countries. While growing trade with China and other countries may undercut further integration with India, Nepal remains weakly positioned to create market stability. Prices in Nepal are determined by external market forces; the prices of valuable goods like gold and silver, which often attract investment as part of cultural occasions in Nepal, are determined by global economic conditions, political events and market forces.

Based on recent data from the International Labor Organization (ILO), over 70% of the working population in Nepal is involved in the informal economy. The informal economy continues to expand rapidly. Workers face hardships and are often exploited because the government cannot regulate it. The ILO has authorized an examination of the Social Protection for People in the Informal Economy of Nepal to understand the potential of social protection for workers and other vulnerable groups compelled to work in the informal economy.

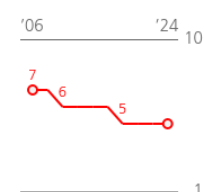
Apart from the World Trade Organization, Nepal is a member of two regional trade frameworks: the South Asia Free Trade Area (SAFTA), which includes Afghanistan, Bangladesh, Bhutan, India, the Maldives, Pakistan and Sri Lanka, and the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC).

While Nepal is not an inhospitable environment for foreign direct investment (FDI) in terms of its regulatory framework, the operation of foreign banks, repatriation of profits and currency exchange facilities continue to constrain foreign investment in practice. India remains the largest single provider of FDI in Nepal, accounting for 33.3% of paid-up FDI capital inflows in 2021. India is also Nepal's most significant trading partner, accounting for 68.73% of Nepal's exports and 63.10% of Nepal's imports in 2019. Nepal has recently increased its trade with China, in part to reduce its structural dependence on its southern neighbor. FDI from China accounted for 14.5% of paid-up capital inflows in 2021.

To fulfill its WTO obligations, Nepal passed the 2007 Competition Promotion and Market Protection Act, which aims to prevent monopolies and cartels. However, this regulatory framework has not been fully implemented. As is the case with many regulations in Nepal, the weakness of the state and its institutions has limited efforts to rein in powerful private actors. Efforts to dissolve syndicates have largely failed. On December 24, 2022, the Himalayan Times reported that "The Ministry of Culture, Tourism and Civil Aviation has directed the Civil Aviation Authority of Nepal to study the issue of cartels in domestic flights." In particular, Buddha, Yeti, Shree and Saury Airlines appear to have fixed prices. This evidence suggests that while the Competition Promotion and Market Promotion Board is still not fulfilling its assigned

Competition policy

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task, there is some willingness in the government to address this issue. Nepal is also not a member of the International Competition Network, which provides competition authorities with a well-focused and informal platform to network and raise concerns over competition.

Good governance, stable institutions and physical infrastructure are essential to facilitating foreign trade and foreign investment. With these essential prerequisites still not realized, Nepal has not experienced the large-scale benefits promised by its trade liberalization attempts. In addition, difficult geographic circumstances – in which the construction of industrial infrastructure is inherently challenging – and a poor industrial relations environment – which makes hiring and firing employees extremely difficult – have discouraged the growth of large industry.

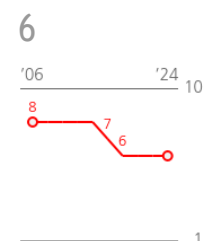
Nepal acceded to the World Trade Organization in April 2004 as the first Least Developed Country (LDC) to do so. Its commitments under the WTO framework are extensive, with most tariff lines bound at an average final bound rate of 26.1% in 2021. All trading partners hold at least Most Favored Nation (MFN) status. The effectively applied average tariff rate was 11.6% in 2020, which was higher than other countries in South Asia. In comparison, India had a rate of 6.2%, Pakistan had 8.7%, Bangladesh had 11.0% and the Maldives had 11.6%. This includes strategic sectors such as agriculture and manufacturing, where simple average MFN tariff rates continue to fall significantly below final bound lines. Import license requirements, in the form of nontariff measures, only affect a small number of products. This is notable considering Nepal’s developing economy. However, the institutional and legal structures needed to implement the WTO agreement remain underdeveloped. Red tape, delays and strikes have significantly discouraged investment in the country. Structural difficulties related to trade-related services and infrastructure have prevented the realization of potential comparative advantages.

The 2016 World Bank Report “From Evidence to Policy: Supporting Nepal’s Trade Integration Strategy” states that Nepal remains poorly integrated and would gain from integration into regional and global value chains. This remains true, though improvements are under way. In September, Nepal received a \$415 million package from the World Bank to support trade connectivity and related infrastructure.

Traders in Nepal face not only distance-related challenges but also transit challenges due to their landlocked position. These challenges include frequent checks by border security officers and police, time-consuming customs formalities, shortages of containers at the borders, differential tariff rates at the Kolkata port, and long delays. These issues obviously add to the cost of international trade.

Nepal’s customs system has improved with the opening of an integrated Raxaul Bazaar/Birgunj border crossing. However, customs clearance still remains a highly document-intensive and time-consuming formality. Customs officials demonstrate capricious behavior and remain interested in their own financial gain. Many traders endure arbitrary extortion of unofficial fees, which are considered unavoidable if one desires to reduce customs clearance times.

Liberalization of  
foreign trade



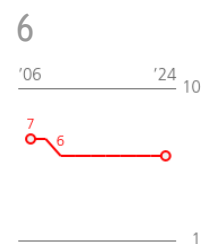
Though FDI inflows into Nepal have recently increased, they remain at a very low level overall. At 0.4% of GDP, Nepal's 2022 FDI inflows are even lower than those of its regional partners. According to the World Bank, this is partially explained by firms' perceived risks of operating in the country and a more restrictive investment regime than in similar countries. Restrictive FDI policies continue to compound the challenges the country faces in attracting foreign investment, though the 2019 Foreign Investment & Technology Transfer Act represents a significant step forward. Despite this improvement, Nepal continues to retain foreign ownership limits in several sectors, including tourism, agriculture, real estate and media.

Nepal has made some progress in improving its investor-unfriendly image. After enacting the Foreign Investment and Technology Act of 2019, which aimed to enhance the foreign direct investment (FDI) environment through the creation of a "single window system," FDI did increase. However, due to only partial implementation, many of the previous challenges to achieving the country's goals persist.

The 2021 Investment Climate Statement from the U.S. Department of State indicates that Nepal's banking sector is "relatively healthy, though fragmented, and NRB [Nepal Rastra Bank] bank supervision, while improving, remains weak." System assets totaled approximately \$48.6 billion in 2022. About 1.7% of loans are estimated to be nonperforming, which is the lowest rate in South Asia. However, several long-standing issues persist, including fragmentation of the banking sector, weak supervision from the country's central bank, the Nepal Rastra Bank, under-banking among the rural population and ownership of some banks by prominent businesses. The last aspect is problematic because it can create conflicts of interest.

The capital adequacy ratio also remained at a low of 13.1% in February 2023 and hovered around this figure throughout 2022. Nevertheless, progress has been made. There were 25 commercial banks in Nepal as of 2021, down from 78 less than a decade ago. Nepal's regulatory system relies on international norms developed by intergovernmental organizations including the United Nations and the WTO. Additionally, the Nepal Rastra Bank has implemented the revised version of the Basel III Capital Regulations for Class A Nepalese institutions. There is also a functioning capital market outside the formal banking sector, which includes the Nepal Stock Exchange (NEPSE) that is open to investors.

Banking system





## 8 | Monetary and fiscal 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 regard as important for overall macroeconomic stability. Accordingly, the value of the NPR fluctuates with that of the INR and depreciated considerably against the U.S. dollar in 2023, declining to NPR 132. The conversion on average was NPR 131 to \$1 in 2022 and NPR 118 to \$1 in 2021. Foreign exchange is not freely available. Under the 1962 Foreign Exchange (Regulation) Act, commercial transactions payable in convertible currency require approval from the central bank.

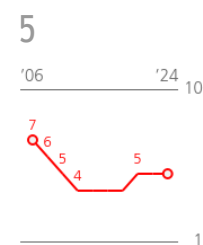
According to World Bank data, inflation was 5.6% in 2019 and has remained relatively stable since then, with inflation in 2021 at 4.1%. The central bank set an inflation target of 7% for the 2022/2023 fiscal year. Furthermore, it decreased the gap between deposit rates and lending ranges of commercial banks to 4.0 percentage points from the earlier set 4.4 percentage points. However, a 2022 IMF Nepal country report stated that Nepal's central bank (the Nepal Rastra Bank) had made "limited progress in implementing previous safeguards recommendations," but that financial reporting processes continue to fall short of international standards and the central bank framework must be modernized to strengthen its autonomy and accountability.

After the 2015 earthquakes, Nepal experienced a temporary decrease in revenue, particularly in the agriculture and tourism sectors. However, over the medium term, the country has had a steady and strong recovery. Unfortunately, the outbreak of COVID-19 further disrupted Nepal's economy, leading to increased expenditures and decreased revenues. In May 2020, Nepal received COVID-19-related assistance amounting to \$214 million. Thankfully, the country seems to be recovering well from the pandemic. Despite these challenges, Nepal's fiscal policy has been relatively responsible, especially when compared to countries such as Sri Lanka and Pakistan.

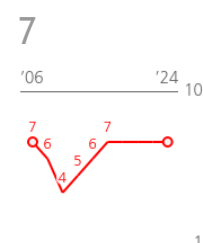
Nepal's federal fiscal deficit was recorded at 3.5% of GDP at the end of FY 2022, continuing a three-year decline after reaching a high of 5.4% of GDP in FY 2020. The national debt-to-GDP ratio in Nepal was reported to be 50.51% in 2023, an increase from 49.09% in 2022 and 45.81% in 2021. Additionally, Nepal's external debt amounted to \$8,855,972,582 in 2021, reflecting a 12.01% increase from the previous year. According to the World Bank, the total debt service as a percentage of GNI was 0.77% in 2021. Nepal's net lending or borrowing data was disclosed as NPR -257,162 million in 2022, representing a decrease from the previous year. Nepalese foreign exchange reserves measured \$9.3 billion in February 2023.

However, given Nepal's ongoing but declining reliance on remittances, debt dynamics remain vulnerable to fluctuations in remittance flows, as witnessed during the pandemic. The government has invested in infrastructure to promote domestic expansion and address the consequences of the pandemic. However, it currently confronts challenges stemming from global inflation, especially in energy and food prices.

### Monetary stability



### Fiscal stability





## 9 | Private Property

Despite the fact that property rights and the regulation of property are defined by the 2015 constitution, they are regularly violated. Some property – mostly land – confiscated during the conflict has yet to be returned. As part of the peace process that began in 2006, the Maoists agreed, in principle, to return all of it and have done so in most, but not all, cases. Problematically, there is no official data on contested titles.

Uncertain property rights pose a specific challenge for the poor, who frequently lack adequate documentation of land titles and struggle to navigate local courts and administration. Despite relatively easier access to land title offices under federalism, the poor still seem to experience a disproportionate disadvantage, especially women, who face obstacles to determining the locations of new administrative offices.

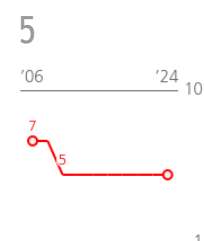
In addition, many individuals who have constructed additional structures on their land without proper documentation are now faced with the unfortunate situation of being unable to legally sell that land. This predicament often occurs when the land is divided among male heirs, resulting in the construction of individual dwellings for nuclear families. Moreover, there are numerous instances where developers have accepted deposits for land plots but are unable to fulfill their obligations due to oversubscription. Those who paid the deposits subsequently encounter challenges in reclaiming their money.

In spite of legal provisions declaring gender equality in property and inheritance, women often cannot make rightful claims due to continuing discrimination as a part of prevailing social practices. A sweeping bill that came into force in August 2018 has made some progress toward ameliorating this situation.

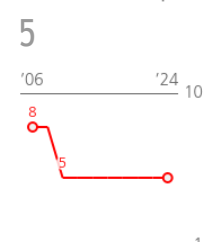
Private companies are constitutionally permitted and protected, with some restrictions on foreign ownership. Bureaucratic and legal hurdles to incorporating and registering a new firm are among the lowest in South Asia. The true obstacle to establishing a private commercial or industrial enterprise lies not in the registration process but in the political and bureaucratic interference encountered in day-to-day business operations.

According to the U.S. 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 14 months later in January 1994. A total of 23 state-owned corporations have been privatized, liquidated or dissolved to date. The process, however, has been static since 2003. Former public monopolies in banking, insurance, airline services, telecommunications and trade have been eliminated.

Property rights



Private enterprise



More than 80 public enterprises in diverse sectors were privatized in the 1990s. The process faced criticism as many newly privatized companies soon found themselves in difficult situations. 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 2022, there were 44 public enterprises in Nepal, with only 22 of them turning a profit in the fiscal year 2021/2022. Many have endured high cumulative losses and unfunded liabilities for years, due to operational inefficiencies and other problems. Because of their poor performance, public enterprises continue to burden taxpayers and consumers. However, further privatizations seem unlikely in the near term.

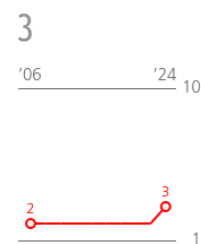
## 10 | Welfare Regime

Nepal's welfare system remains primarily confined to social networks rooted in familial structures. Non-governmental organizations (NGOs) seek to address this shortfall, but their contributions are predominantly restricted to targeted and fragmented services at the local level. In certain instances, these efforts actually undermine the state's endeavors to enhance its own service delivery capabilities. Consequently, the availability of social welfare options fluctuates significantly based on geographical location, access to international donors, and personal connections.

Family support structures are strong but weakened by widespread and long-term out-migration for work. Although both domestic transfers of wealth from urban to rural areas and remittances from workers abroad help compensate for social welfare costs, the physical absence of family members strains the social fabric.

Nepal's public expenditures on health, in terms of percentage of GDP and government expenditure, are relatively high by South Asian standards but still insufficient, as in almost all South Asian countries. The COVID-19 pandemic caused a surge in expenditures on public health, which grew from NPR 69 billion in fiscal year 2019/20 to NPR 81 billion in 2020/21, before another increase to NPR 123 billion in 2021/22. However, the fact that overall health expenditures fell back to NPR 69 billion in 2022/23 suggests that the increase was not due to structural changes in the public health sector but rather a reaction to the COVID-19-related emergency situation. Inefficient use of finances remains a significant problem. Private initiatives to improve social services are limited, and public social services are underdeveloped and insufficient to meet demand. That said, access to health care, in particular, has improved in recent years, and the COVID-19 pandemic actually accelerated this trend. Public health access is better in urban areas than in rural ones.

Social safety nets



A lack of social inequality on the basis of ethnicity, language, caste and gender was a defining feature of Nepal until very recently. Although discrimination related to caste was outlawed in principle in the 1960s, it continues to be a defining feature of life for many Nepali citizens in practice. Laws that discriminate based on gender have recently been abolished. Inheritance remains an issue for women in practical terms.

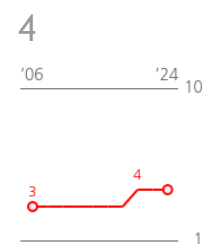
Since the end of the conflict in 2006, the implementation of a range of measures designed to reduce social inequality has begun. However, their impact remains limited. In 2007, a second amendment to the Civil Service Act introduced affirmative action provisions for the civil service, including the police, for the first time. These provisions aim to increase the representation of women, indigenous people, Madhesis, Dalits, disabled individuals and individuals from “backward” regions. Under a proportional representation system, the new constitution guarantees 40% of parliamentary seats to minority groups, but it also introduced the controversial category of Khas-Arya (i.e., high-caste Pahari Hindus, Bahun and Chhetri) for affirmative action purposes. Additionally, the new constitution mandates that political parties themselves must ensure the election of women to political office by fielding a certain percentage of female candidates in both first-past-the-post and closed list proportional races. Currently, women make up approximately 33% of political representatives at the national level and 40% at the local level.

Regarding access to education available to young girls and women in Nepal, studies report that a major issue is the high dropout rate of girls, particularly in the higher grades. This phenomenon persists, despite their achieving gender parity in primary school enrollment. Potential reasons for the dropout rate include living in remote areas, coming from low-income backgrounds, early marriage, and unfortunately, gender-based violence. Nepal has recently passed legislation prohibiting gender-based discrimination in employment; however, in 2022, approximately 90.5% of women had to resort to working in the informal sector. In these situations, they often face underpayment or no payment at all.

Male members of the Nepali-speaking, hill-dwelling Brahmin caste (Bahun), who make up only 12.2% of the country’s population, continue to disproportionately be placed in a significant number of new civil service posts, even though the overall proportion of positions they hold has slightly decreased. According to a recent report, 19.57% of recommended civil service applicants were Brahmin. Additionally, Brahmins from the Terai, as well as Kayasthas and Rajputs, are also overrepresented, despite constituting smaller percentages of the overall population. These same groups demonstrate dominance in the judiciary, education system, media, labor unions and even NGOs.

Nepal’s labor market offers highly unequal opportunities; the International Labor Organization (ILO) estimates that around 70% of the workforce in Nepal remains employed in the informal sector. These workers face numerous challenges and constraints, lacking protection in the form of basic social safety nets. They are

#### Equal opportunity



subjected to exploitation and deprived of basic working rights. The government has largely overlooked these abuses, but the labor market landscape is gradually changing with the implementation of a recent labor law.

According to Nepal's Ministry of Labor and Employment, in 2021/22, the Department of Foreign Employment issued 628,503 foreign labor permits. This number reflects an increase following a period of decline that began in 2013/2014. Saudi Arabia serves as the primary destination through the permit system for 2021/2022, accounting for 30% of permits issued. Conversely, Saudi men constitute a substantial proportion (29%) of registered labor migrants.

A significant proportion of international migrants from Nepal also migrate to India, where no visa or foreign labor permit is required. According to the World Bank's 2018 estimate, around 27% of Nepali migrants choose this route. Nepali migrants in India typically work in the private sector, primarily in manual labor positions in industries, construction, agriculture or the service sector – particularly in security. Their wages are generally low and working conditions often entail danger and degradation. Although reliable data is scarce, some estimates suggest that up to 200,000 Nepali women may be employed in the sex industry throughout India. Efforts by civil society to curb this migration trend have achieved some success, but little is being done to repatriate and rehabilitate those already ensnared in this sector. This is largely due to the social stigma surrounding sex work for many in Nepal.

## 11 | Economic Performance

Nepal remains one of the poorest countries in the world. According to the World Bank, per capita GDP growth in Nepal was 2.4% in 2021, with per capita GNI (PPP) at \$4,280 and per capita GDP (PPP) at \$4,261. The country's growth has been affected by earthquakes and trade disruptions in recent years. However, when these disruptions came to an end, inflation decreased to 3.2% and economic growth rebounded.

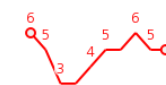
During the earthquake in 2015, Nepal experienced significant economic losses, leading to a drop in GDP growth from 6% in 2013 to 0.6% in 2015. However, in 2017, GDP growth spiked to 7.5% before experiencing a rapid decline to -4.1% in 2020 during the COVID-19 pandemic. Since then, the economy has somewhat recovered.

Nepal's strong domestic consumption continues to rely on inflows of remittances. These remittances accounted for just under 11.21% of GDP in 2002, reaching a peak of 31.43% in 2015, before decreasing to 24.25% in 2020.

Output strength

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Between 2013 and 2023, the Consumer Price Index (CPI) in Nepal averaged 122.13 points. Additionally, the unemployment rate in the country was 5.05% in 2021, marking a 0.33% increase from 2020.

As mentioned above, Nepal's external debt was \$8,855,972,582 in 2021, a 12.01% increase since 2020. Domestic public debt increased from 9.3% of GDP in 2015 to 38.25% by 2021. Nepal's reliance on remittances remains critical. Moreover, according to Nepal's National Planning Commission, Nepal faces a high trade deficit. Over the years, exports have stagnated, whereas imports have skyrocketed. Officially, Nepal aims to maintain a trade deficit of 20% of GDP, but the estimates for 2021 indicate that there is a deficit of around 33.39% of GDP. India commands the biggest share of Nepal's foreign trade, at approximately 64.1% in 2021, followed by China at 14%.

According to World Bank data, the labor force participation rate was 80% in 2021. However, the International Labor Organization (ILO) states that the majority of workers remain in vulnerable employment. This situation is compounded by the lack of social protection schemes and the temporary standstill the COVID-19 pandemic caused for Nepal's important tourism sector.

## 12 | Sustainability

Nepal experienced two major earthquakes in the spring of 2015. In the aftermath, certain measures were taken to enhance the country's readiness for future earthquakes. In addition to the considerable damage the earthquakes caused, prior extensive deforestation has rendered the country especially prone to landslides and flooding, particularly during the monsoon season. Although community forestry has succeeded in expanding forest coverage in various regions, Nepal, due to its distinct geographical location and intricate ecology, remains highly vulnerable to the adverse impacts of climate change.

The economic growth of recent years has been achieved at a high environmental cost, leading to additional environmental degradation, primarily in the forms of air pollution, poor water resource management and sanitation issues. The completion of the Melamchi Water Supply Project, which took over 20 years, has started to address water shortages in the overpopulated Kathmandu Valley. However, this water supply has been unreliable so far, requiring further work to mitigate flood damage. Meanwhile, air pollution and water sanitation issues persist, with only slight improvements. Notably, the demand for electric vehicles has risen alongside an increase in the dependability of the electric supply, leading to potential benefits for air quality in the Kathmandu Valley. Lastly, Nepal stands out among other countries in the region for its successful conservation of native flora and fauna, as well as its preservation of delicate ecosystems. This conservation effort is partly driven by the government's reliance on eco-tourism revenue.

Environmental  
policy

5

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Nepal's current Environmental Performance Index (EPI) score is 28.3, ranking it 162nd out of 180 countries. This places Nepal above India (180), Bangladesh (177) and Afghanistan (181), but below Pakistan (176), indicating that Nepal is part of a region that suffers from very poor environmental performance. Ambient air pollution remains a problem in Kathmandu. Particulate pollution mainly results from vehicle traffic, combustion emissions and dust resuspension, as well as other forms of combustion and industrial sources such as brick kilns within the valley. The 2022 EPI ranked Nepal quite poorly for air quality (unsafe levels of fine particulate matter), whereas drinking water and sanitation have improved. Nepal also continues to perform better on ecosystem vitality than previously.

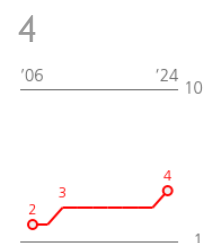
The country has a comprehensive set of environmental policies that date back to the 1970s when the royal family turned its own private hunting reserve into what is now Chitwan National Park. This was followed by similar policies. Subsequent efforts have been made in close coordination with the international donor community, which supports Nepal's relatively good performance in the areas of conservation/biodiversity and forestry. Large swaths of Nepal's forests are administered through community forest user groups, groups of locals who present plans to sustainably manage government-owned forest land. Forest coverage has increased in some of these areas, while in others there is a struggle to prevent further deforestation.

The expansion of sustainable energy is slow but has recently gained momentum. The primary household energy source outside urban centers is biomass (firewood). Nepal also has several operational hydro projects distributed throughout the country, which supply 96.2% of the country's generating capacity. The government, with support from donor agencies and bilateral aid, continues to invest in the renewable energy sector. Progress has been slow but steady. Various donor agencies assist companies with investments in energy efficiency and sustainable energy sources.

Though Nepal completed its last national census in 2021, only preliminary data has been released, which excludes the literacy rate. UNESCO estimates the country's adult literacy rate at 67.91% to 78.59% among adult men and 59.72% among women. However, these data are somewhat misleading, especially since literacy among 15- to 24-year-olds in Nepal is very high (>80%) and more gender equal. According to World Bank data, Nepal's public expenditure on education amounts to 4.4% of GDP. The Ministry of Education launched a school sector reform program for 2009 to 2015, with an estimated budget of \$568 million. The World Bank claims that the primary school completion rate significantly improved between 2013 and 2015. In light of this, the demonstrated literacy rate, particularly among 15- to 24-year-olds, should climb once the 2021 census data are released.

Nepal has also recently transitioned from a nationally conducted school-leaving certificate examination (SLC), which acted as an "iron gate" for many students having attended government schools in rural areas, to a Secondary Education Examination (SEE). One of the main problems with the SLC was that a student who

Education policy /  
R&D



did very poorly in one or two subjects would fail the exam, even if he or she did quite well elsewhere. The SEE, in contrast, essentially takes an average grade across all subjects and, depending on that grade, allows the student to move on to secondary education. Pass rates in 2022 were 95.7%, meaning that most exam takers could move on to 11th grade. Under the SLC system, overall exam pass rates were often below 50%.

Other reforms in higher education are underway, but implementation has been slow. Additionally, underfunding remains a problem – according to UNESCO, 13.19% of overall public spending was allocated to education in 2020, well short of Nepal’s goal of spending 20% of its budget on education. Lastly, overall national spending on research and development remains so low as to be insignificant. It will take some time before the country has a thriving R&D sector.

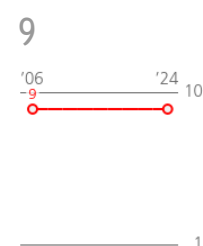
## Governance

### I. Level of Difficulty

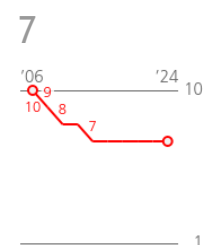
Political leaders in Nepal continue to face significant structural constraints to achieving good governance goals. Highly unfavorable conditions for economic and political transformation include a low level of economic and social development; a population with relatively low, though improving, educational achievement; the geographical disadvantages of being a landlocked state without many resources; and a solidifying but still fairly weak state apparatus. Nepal's environment is prone to suffering the consequences of natural disasters, as seen during the devastating 2015 and 2022 earthquakes, the landslides that destroy its infrastructure during every monsoon season and, lastly, man-made ecological degradation. The country's terrain is challenging to navigate, but the state is starting to meaningfully move away from its historical centralization in Kathmandu. Infrastructure remains a problem, although investments in this sector are beginning to pay dividends. Federalism and the rise of independent politicians have contributed to policymakers learning to assess citizen aspirations and needs more effectively, as well as to meet face-to-face with citizens. Still, poverty remains problematic, and educational resources are scarce in many parts of the country. Rapid urbanization and an ongoing brain drain also present unique policy challenges, though the COVID-19 pandemic saw the repatriation of many Nepali expats. The political leadership is largely at fault for Nepal's governance problems, notwithstanding the structural constraints, but a nascent trend toward electing political outsiders may breathe life and accountability into the system.

Nepal has long been a major recipient of official development assistance. Governance is supported by a host of international and national NGOs, sometimes at the long-term expense of state capacity. Spaces for civic participation are relatively open in Nepal. This has contributed to the emergence of a variety of indigenous civil society movements. Many forms of engagement center around very specific local, as opposed to national, affiliations and identities. A wide range of civil society organizations operate even in the most remote and impoverished areas of the country. Some examples of NGOs in Nepal include Aama Samuha, which strives to spread awareness of women's rights; Child Workers in Nepal (CWIN), whose goal is to aid children at risk; DidiBahini, which seeks gender equality and social justice; and Maiti Nepal, an organization that focuses on human trafficking and preventing violence against women and children. Over time, some of these local affiliations have grown into national-level organizations and/or movements, but others remain local, reflecting the diversity of political, social and economic life in Nepal.

Structural constraints



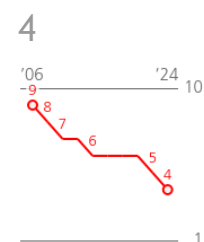
Civil society traditions





Political elites have instrumentally used polarization techniques to create cleavages along ethnic and regional lines. However, recent voting patterns suggest a shift away from identity politics. The new Rashtriya Swatantra Party, which focuses on and unites independent candidates, won an unexpectedly high number of seats in the 2022 elections. Still, many minority ethnolinguistic groups remain dissatisfied with their representation in the system. Fortunately, outright violence rarely occurs, and most Nepalis seem to turn to electoral politics or the courts to settle disputes and grievances. Nepal's new institutional framework of federalism appears better suited to managing these concerns than its former institutions.

#### Conflict intensity



## II. Governance Performance

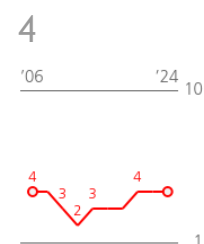
### 14 | Steering Capability

Though the structural constraints on governance in Nepal are high, the political leadership's low steering capability underlies the difficulty Nepal has had pursuing a development agenda. The heterogeneous character of multiparty coalition governments before 2004, between 2006 and 2012, and again since January 2014 makes it difficult, even for determined policymakers, to set strategic, long-term priorities. Despite this, the government of Nepal has attempted to identify four overarching goals in the sectors of disaster risk financing and management of climate risks. These focus on the financial priorities in the event of any disaster and the adjustments that would have to be made to account for unforeseen events. Important policy decisions are frequently subject to fierce distributional battles among different ministries, at both the political and administrative levels. This tendency is now being replicated at the provincial and local levels, with the step-by-step institution of federalism and decentralization.

A series of unstable coalition governments have made it challenging to pursue clear policies. Meanwhile, the domination of politics by a long-standing but small number of individuals has increased the tendency for personality-based politics and factional rivalries. This is compounded by the segmentation of the cabinet along party lines, which causes coordination problems among different ministries. Weak prime ministerial leadership has also been associated with limited control over ministries across different parties. On the positive side, with the political struggle over and the character of the Nepali state settled, the political cover for the government's lack of attention to administrative reforms and long-deferred governance tasks disappeared, at least in the medium term.

#### Question Score

#### Prioritization



In addition, there have been few internal regulatory impact assessments (though NGOs regularly provide guidance), and there is no strategic planning unit. This would make it challenging for any government to strategize and organize its policy measures. There is a national planning process, however, which has been in place since 1956. It produces five-year national development plans, with mixed evaluations in terms of success. Federalism has not changed the process substantially, but empowering provincial and local governments to produce their own development plans has limited the scope of the national planning process.

The governments in power during the review period have not been particularly effective at implementation. A constitutional crisis undermined implementation for some time, but federalism is increasingly taking root, and this is forcing parties to learn and to innovate beyond the electoral arena. The distribution of resources close to the ground is encouraging parties, whether governing or not, to tailor policies to local needs. In the past, many policies were colored by ethnic politics, but recent electoral results suggest a move away from identity and establishment parties and toward political newcomers.

Even when there is consensus about a particular policy, the crucial bottleneck lies less in drafting it well than in the government's struggle to implement it. Successive governments have instituted countless industrial growth, investment and trade-promotion policies, often with substantial, systematic donor input, but the effect on the ground has been limited. This is not completely a consequence of poor governance at the top but is also attributable to a pervasive lack of expertise and capacity at every level of the government bureaucracy. One example of such inefficiency is the National Reconstruction Authority's delayed implementation and continued struggle to bring relief to millions of earthquake victims across the country. More recently, the government demonstrated slightly more capacity in response to the COVID-19 pandemic, but its management was still marked by deficiencies. Another policy the government advocated for was "Forest for prosperity," which aimed to divide the forest into regions and develop scientific forest management. However, implementation failed because the government was unable to identify, protect or manage the forest and forest products. Emblematically, the government launched a campaign to "consume indigenous goods, encourage domestic production," but did not take meaningful steps to promote domestic agricultural production.

Implementation

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The government of Nepal continues to rely on its steadily improving National Monitoring and Evaluation System and the practices it engages in to ensure effective oversight of policies before and after they are implemented. This includes a performance-based budget release system that links the budget to the performance of a policy, along with a public expenditure tracking survey (PETS), which traces budget paths and project implementation to assure that expenditures reach targeted groups at the appropriate time. International organizations provide expert groups that analyze the implementation and effectiveness of policies across Nepal. The World Health Organization also has a Technical Advisory Group (TAG) with independent members who are experts in monitoring and evaluating policies, programs, health care and other social services. Researchers and policy experts in Nepal continue to publish evaluations of various maternal policies. A collaborative report was published in 2023 on the “National Health Insurance Program of Nepal” and whether “political promises are translated into actions.” The authors included Nepali public health professionals and staff at the Ministry of Federal Affairs.

## 15 | Resource Efficiency

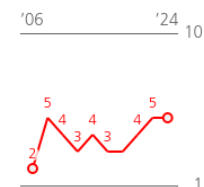
Many recent administrations, including the UML-led government (2015 – 2016), the Congress-led governments (2016 – 2017 and 2021 – 2022) and the CPN government (2017 – 2021), have struggled to efficiently use available economic and human resources to promote their economic and social policies. The most significant step forward in recent years was the near-elimination of electricity cuts that started under a Maoist-Congress coalition government. While people in Nepal often endured 16-hour per day cuts a decade ago, it now exports excess power. The government management of the Melamchi Pipeline was similar, though this project has recently been completed. During the COVID-19 crisis, the Nepali government effectively marshaled the resources it had, acquired additional resources and provided a reasonably effective pandemic response. More recently, a whole host of infrastructure projects, particularly roads and tunnels that will cut travel times for both people and goods in Nepal, appear to be advancing at a decent pace.

One of Nepal’s main resources is its youth and their productivity. Nepal continues to face a domestic job shortage, further aggravated by the thousands of Nepalis who returned home during the pandemic. However, as pandemic conditions eased, many returned to work abroad, also reintroducing remittance flows as an important asset for the country’s economy.

Development aid from India, China and the West plays an important role in Nepal’s budget. Monitoring of these funds remains problematic but has improved, with civil society acting as a watchdog. Nepal’s administrative and civil services remain underfunded and understaffed, and their decision-making processes continue to be fragmented. Problems of timely spending also contribute to serious delays and wasted resources with regard to infrastructure and other projects. As decentralization deepens under federalism, however, citizens seem satisfied with local government performance.

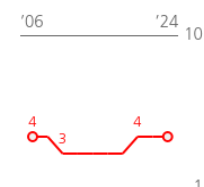
### Policy learning

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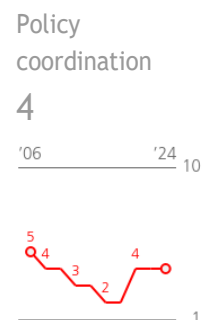


### Efficient use of assets

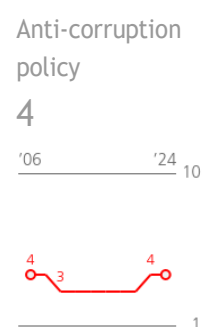
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The current coalition government is the 12th government formed in the last 10 years. This level of turnover contributes to problems with policy coordination. Few major policies are evidence-based, nonpartisan or based on consultations with a wide range of experts. Political parties in Nepal are plentiful, and to win elections, they have to be increasingly flexible about the politicians they recruit and the voters they try to sway. A single political party may be associated with conflicting interests and policy objectives; smaller parties negotiate coalitions with larger ones, while remaining deeply divided over policy objectives. Few parties have time to implement their policy agendas before losing the next election, which also hampers the efficient use of resources. Policy coordination under such volatile circumstances is challenging.



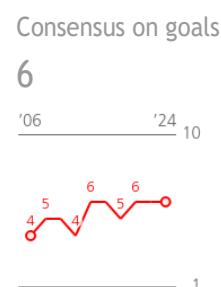
Corruption and poor use of public resources are common in Nepal. Regulations and bodies that exist to ensure transparency have largely been ineffective to date. That said, the Commission for the Investigation of Abuse of Authority (CIAA), which had been plagued by understaffing and controversy, has been making progress lately. For instance, its recent active stance and aggressive pursuit of corruption investigations suggests a changing of the tides. To make meaningful progress, however, it will require far more resources than it has and the widespread support of the Nepali people. It will also have to demonstrate its efficacy by going after powerful, well-connected targets.



Corruption among government officials, mainly through the distribution of permits and approvals, the procurement of goods and services, and the awarding of contracts, continues to be a problem. For those who lack connections in high places, bribes remain a common way to obtain access to public services or to accomplish even ordinary activities like securing a driver’s license or a birth certificate. Reportedly, with decentralization, these problems have decreased in frequency. This is because with the government close to the ground, individuals are finding it easier and cheaper to secure government services than before.

**16 | Consensus-Building**

Nepal’s 125 ethnic groups, 127 spoken languages, myriad caste and jati groups, and varied ecosystems present a distinct challenge to political consensus. Fortunately, Nepal’s political parties have a long history of support for democracy that dates back to well before the democratization process started in the 1990s. The CPN-M, when it committed to peace, agreed to conduct politics within constitutional democratic boundaries and, despite some early problems with party discipline, has largely done so. The Maoist-Congress coalition government (2015 – 2017), as well as the Maoist-Congress pre-electoral coalition in the lead-up to the 2022 elections, suggest that support for peace and for democracy is strong in Nepal and that this support includes all major segments of society.



Still, after the 2022 elections, it took a full five weeks to form a government, and it is unclear how long the renewed alliance between the CPN-Maoist Center and CPN-UML will last. It can be said that consensus around goals is tenuous at best, even if support for democracy is strong.

Nepal's various communist parties have surprised critics by the degree to which they are willing to operate within a market economy, even though not all of them are supportive of it. This should hardly be surprising, given how the market operates in neighboring China under the Chinese Communist Party. Indeed, most Nepalis associate communism with better and more equal provision of public goods like education and health care, both of which incorporate public as well as private providers.

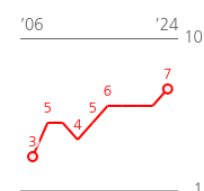
Despite its long history of protest movements, there is a pro-democratic consensus among all major political actors. Federalism, as it has been implemented, has lessened the abilities of single actors to concentrate power. Even those parts of the state apparatus that are not subject to democratic processes, like the Nepal Armed Forces (NAF), do not present a major threat to the pro-democratic consensus.

Other potential sources of dissent from the pro-democratic consensus do not appear to be an imminent threat. The former royal family, for its part, has not attempted a return to power, despite the royalist political party (Rashtriya Prajatantra Party) having enjoyed renewed support in the 2022 elections. Conservative parties running on platforms that propagate a return to Hindu values and culturally homogenous nationalism do not appear poised to make gains, unlike parties in neighboring India. While Nepal does have a long history of politics being played out in the streets rather than through institutional mechanisms, the frequency and tenor of protests have changed dramatically over the last few years. Social mobilization does still occur, but the focus has shifted somewhat toward longer-term strategies and organizations, as opposed to sudden regime change.

The most significant problem Nepal faces in terms of consensus-building is the tendency of the political elite to engage in identity politics, particularly over the last few years. Identity-based issues were once ignored because of presumed cultural homogeneity during the monarchy and the political, social and economic domination of the high-caste Hindu elite, which benefited from the maintenance of the status quo. Identity politics have become effective, however, in improving the rights of marginalized groups. They have also contributed to the establishment of a more inclusive state than before through federalism. However, identity-based political mobilization threatens to fragment the political spectrum and to prevent political parties from doing little more than identity-based distribution of state resources. The rise of the National Independent Party (Rashtriya Swatantra Party) portends a shift away from identity politics and toward political outsiders. Its ability to moderate cleavage-based conflict remains untested, but the political support RSP candidates enjoyed in the 2022 elections suggests that they have widespread public backing.

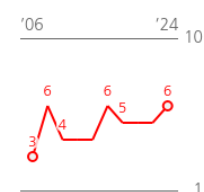
Anti-democratic actors

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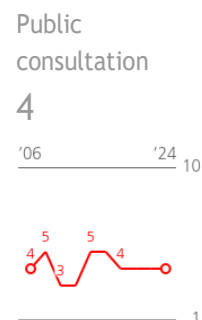


Cleavage / conflict management

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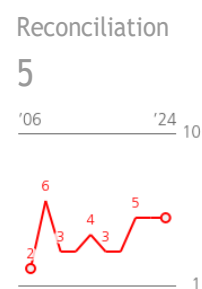


The political leadership has become less repressive and more consultative over the years. Parliamentary consultation nevertheless appears to be elite-centered and technocratic. According to the national media, in May 2022, the federal parliament did not consult the public during the process of over 100 legislative acts. Other forms of public consultation have been tried out, such as the 2nd National Dialogue Platform on Anticipatory Humanitarian Action in Kathmandu on May 11 and May 12, 2022. The event served as a consultation platform, with actors including provincial and local government officials, NGO staff and academics. This platform was initiated in reaction to the 2022 earthquake.



As a result of this liberalization, there has been increased activity among non-governmental organizations and civil society groups over the last few years. Advocacy on behalf of women and minorities has increased. However, as a result of this identity-based activism, many citizens see civil society as dominated by the same identity cleavages they perceive in the political arena. This is in part because organizations often attract members along party lines. In addition, many civil society organizations are highly dependent on donor funding. While funding is certainly vital, it also skews agendas toward donors’ funding priorities. It should not be surprising, then, that the legitimacy of social movements, civic associations and non-governmental organizations is sometimes politically determined. Few organizations are accepted as legitimate across the political spectrum. In addition, there is the persistent problem that ethnic and regional identity-based groups perceive mainstream political parties as representing the long-dominant, upper-caste Hindus, though decentralization and federalism have diminished these concerns. Survey data suggest Nepalis prefer a government that is close to the ground.

Class-based tensions drove rural support for the Maoists. While some of the grievances that led to conflict in the past have been addressed, others raised during the conflict have not. Generally speaking, there has been almost no progress on the Truth & Reconciliation front. Perpetrators of abuse during the conflict have not been charged, while victims’ concerns remain unaddressed.



Still, changes are taking place and reconciliation has slowly accelerated as a result of decentralization and federalism. Nepal, like many countries, has experienced a growing rural-urban divide over the last 20 to 30 years, with urbanization and outward migration leaving few working-age men in rural areas. For many years, rural areas remained poor, and people largely lived on subsistence agriculture and remittances. Because of improvements in communications, the rural poor were aware of their relative deprivation, particularly as compared to their urban counterparts. Their concerns were prominent in Nepali politics for years. Federalism and infrastructure improvements suggest that in the future, a higher degree of mobility than exists now, both physical and social, is possible.

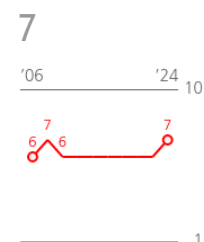
## 17 | International Cooperation

Nepal has a long history of working with international partners. These partnerships have yielded results, especially in the areas of education, health, drinking water quality, telecommunications, road construction, power generation and environmental conservation. The development agenda is set in large part by the National Development Plans, which envisage important but non-specific roles for international partners. One current focus is on improving the mobilization of (I)NGOs for development priorities and increasing transparency in their use of their resources. The work of INGOs is now coordinated through the federal Ministry of Women, Children and Senior Citizens, which approves policy objectives and funding allocations. While the state struggled initially with earthquake reconstruction, a number of post-earthquake milestones have now been met, including the reopening of the Dharahara Tower. This, combined with Nepal's response to the COVID-19 pandemic, suggests increased state capacity and a more productive relationship than previously with the international community.

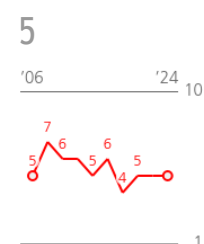
Nepali governments historically and currently cooperate relatively well with international donors and agencies. This is not without costs, however, as donors have long exerted policy influence in Nepal. In the past, international assistance was rarely driven by conditions on the ground in Nepal or the demands of average Nepalis. This, however, has shifted with the changes in the political landscape. Protests over a \$500 Millennium Challenge Corporation grant from the U.S. government to fund electric transmission lines and roads are indicative of this shift. Now, local voices are heard in the implementation of projects. The Nepali state has almost never been in a position to turn down assistance, however. While this dependent relationship has skewed domestic politics and likely resulted in continued weak state capacity in the past, the government has been more assertive lately in terms of securing aid that works for a wide population segment, such as through the mechanisms discussed above.

Nepal is a member state of the International Labor Organization (ILO). No breaches of ILO rules have been reported since it became a member. Concerning climate change, the country is highly vulnerable, particularly to increased water levels from melting glaciers, and has pledged to reach net-zero greenhouse gas emissions by 2045. The Paris Climate Accord was signed on April 22, 2016, and ratified on October 5, 2016. According to Climate Transparency 2020, taking current measures into account, Nepal is not on track to reach the necessary goals for a 1.5°C warming.

Effective use of support

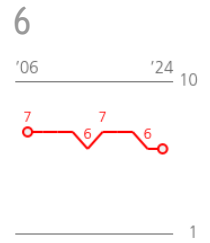


Credibility



In terms of regional cooperation, Nepal's relationship with China is improving, while its relationship with India continues to recover from the 2015 blockade in their bilateral relations. For many years now, Nepal has pivoted back and forth between Indian and Chinese aid, seemingly adopting a policy of playing these two regional powers off against each other. This strategy has worked well for Nepal, though it is not without its problems. Recent Chinese and Indian border incursions have strained ties. Nepal cannot fight either power, so it is diplomatically contesting both, even as India and China also skirmish with each other along their shared border. Even once these particular border issues are settled, Nepal seems destined to remain caught up in these broad regional dynamics.

### Regional cooperation





## Strategic Outlook

Having sustained progress over the past couple of years, even in the face of the COVID-19 pandemic, and having recently completed the second round of local, provincial and national-level elections under the 2015 constitution, Nepal appears to be following a more democratic and less violent political path than it did five years ago. While the memory of K.P. Oli's 2020 dissolution of parliament remains fresh, the fact that the resulting protests remained largely peaceful, that the Nepali Supreme Court effectively resolved the related constitutional crisis and that free and fair elections ensued suggests that Nepal should continue along this trajectory. The challenging and often tumultuous process of democratization seems to be in Nepal's past at this point, with the task of democratic consolidation ahead.

In certain respects, democracy revolves around establishing routines scholars refer to as institutionalization. This should be Nepal's central focus moving forward. While there may be missteps and periods of instability, political actors returning to democratic fundamentals and principles will drive the process of institutionalization.

However, it is worth noting that smooth sailing is not on the immediate horizon. For many in Nepal, 2022 marked the year when their frustration with the political establishment exploded, reshaping the political landscape. Nepalis are not weary of democracy itself but fatigued by the familiar political figures who continually make promises that they fail to fulfill. They desire the tangible benefits of democracy. Although it will take time for these benefits to materialize, the fact that these frustrations were channeled into the formal political system is promising. Their grievances found expression in the new Rastriya Swatantra Party (National Independent Party) and took shape through the campaigns of numerous political newcomers who chose to be the change they wished to see in the world by engaging in politics.

Established political parties and figures should take the population's actions seriously. In the November elections, many experienced politicians were defeated, not necessarily due to their incompetence but because the need to govern democratically in a diverse, developing nation is often underestimated. Thus, established politicians would be wise to share power, welcome newcomers and offer them opportunities to contribute to politics. The more this occurs, the higher the likelihood that street politics and political violence will wane and become relics of the past.

Should this transformation occur, it would signify a substantial political accomplishment and confer economic advantages as well. Stability and predictability are highly regarded by the business community. They are attributes that have been in short supply globally as of late. Nepal is currently striving to emerge from the pandemic-induced economic downturn that has affected much of the world. As economies closed down, many of Nepal's expatriate workers returned, leading to a halt in remittances. As the global economy reopens, most of these workers are now re-engaged abroad, once again sending money back to their loved ones in Nepal. While this is a positive development, it is insufficient. Like its southern neighbor India, Nepal must focus on

increasing the number of domestic jobs it generates to put its substantial youth population to work, which could become a political liability in multiple ways if not adequately employed. Furthermore, Nepal should take substantial steps to promote exports. Its assets extend beyond its people. The relative weakness of the Nepali rupee against the dollar should facilitate export promotion. Lastly, Nepal must address the largely overlooked issue of non-payment within the business community, partially driven by high interest rates. Businesses postpone payments to collect interest on deposits. If money does not begin to circulate again, business relationships could deteriorate. The trust and social capital that underpin Nepal's business environment could take years to recover if they are substantially eroded.

While improvements have been observed in governance in Nepal, particularly influenced by the pandemic, challenges persist. Addressing corruption, which spurs the frustration average Nepalis feel toward the political establishment, must be prioritized. To be taken seriously, the Commission for the Investigation of Abuse of Authority (CIAA) needs more resources than it has and should pursue investigations against high-ranking figures. If Nepal successfully addressed corruption and turned the corner on this issue, it would mark a significant milestone in its history, finally giving average Nepalis a genuine sense of self-governance.